



Collegedunia NCERT Notes

The Ultimate NCERT Revision Guide for Class 12 Accountancy

Part 2 Chapter 2: Issue and Redemption of Debentures

What this chapter covers: meaning of a debenture and its difference from a share; types of debentures by security, tenure, convertibility, coupon and registration; the six issue-redemption combinations and their journal entries; over-subscription handling; issue for consideration other than cash; issue as collateral security; debenture interest and TDS; writing off discount or loss on issue; the four methods of redemption (lump sum, instalment, open-market purchase, conversion); Debenture Redemption Reserve (DRR) and Debenture Redemption Investment (DRI) under the Companies Act, 2013. Session 2026-27.

Also see for this chapter: [NCERT Solutions](#) | [Formula Sheet](#)

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1 Introduction: Why a Company Issues Debentures

A company raises long-term funds in two broad ways, by issuing **shares** (owned capital) and by issuing **debentures** (borrowed capital). Share capital is rarely enough on its own, so most companies also raise debt through debentures, either by private placement with financial institutions or by a public offer.

The word “debenture” comes from the Latin *debere*, meaning “to borrow”. A debenture is a written instrument, issued under the common seal of the company, that acknowledges a debt. It carries a promise to repay the principal on (or before) a specified date and to pay interest at a fixed rate, usually half-yearly, on

the nominal value.

Statutory definition, Section 2(30), Companies Act 2013

“Debenture” includes debenture stock, bonds and any other instrument of a company evidencing a debt, whether constituting a charge on the assets of the company or not.

1.1 Bond vs Debenture

A bond is also a debt acknowledgement. Traditionally bonds were issued by governments and debentures by companies, but the two terms are now used interchangeably. In the rest of these notes, “debenture” means any such long-term debt security of a company.

1.2 Share vs Debenture, the seven-point comparison

Both shares and debentures raise long-term funds, but they sit on opposite sides of the balance sheet and behave very differently in law and in cash terms.

Basis	Share	Debenture
Status	Owned capital, shareholder is a part-owner	Borrowed capital, debentureholder is a creditor
Return	Dividend; variable; only out of profits	Interest; fixed; payable even if there is a loss
Nature of return	Appropriation of profit	Charge against profit
Repayment	Generally never repaid during life of company (except buy-back)	Issued for a specified period; repayable on maturity
Voting rights	Equity shareholders have voting rights	Debentureholders have no voting rights
Security	Not secured by any charge	Usually secured by a fixed or floating charge
Convertibility	Cannot be converted into debentures	May be converted into shares if terms so provide (convertible debentures)

Real-World Application

Bharat Petroleum, NHA and Power Finance Corporation routinely raise thousands of crores through public-issue debentures because the cost of debt (interest, tax-deductible) is lower than the cost of equity (dividend, paid after tax), and unlike equity, debentures do not dilute promoter control.

2 Types of Debentures

Debentures are classified along five independent dimensions. The same debenture certificate can be, for example, “Secured + Redeemable + Convertible + Coupon-bearing + Registered” all at once.

2.1 By security, secured vs unsecured

Secured (mortgage) debentures carry a charge on the assets of the company. A *fixed charge* attaches to a specific identifiable asset (a particular plot of land, a particular plant). A *floating charge* hovers over the general assets of the company and crystallises only on default.

Unsecured (naked) debentures have no asset backing, they rank only as general creditors on a winding-up.

2.2 By tenure, redeemable vs irredeemable

Redeemable debentures are repayable after a fixed period (e.g. 5, 7 or 10 years). **Irredeemable (perpetual) debentures** carry no fixed redemption date and are repaid only on the company’s winding-up. Note: after the Companies Act 2013, Indian companies cannot issue perpetual debentures; the term survives mainly in theory and in older corporate balance sheets.

2.3 By convertibility, convertible vs non-convertible

Convertible debentures (CD) carry an option to be converted into equity shares (or new debentures) at a stated price after a stated period. They split further into *Fully Convertible (FCD)* where 100% of face value converts, and *Partly Convertible (PCD)* where only a part converts and the rest is redeemed in cash.

Non-convertible debentures (NCD) carry no such option, they are pure debt instruments. NCDs typically carry a higher coupon to compensate for the lack of the equity upside.

2.4 By coupon rate, specific-rate vs zero-coupon

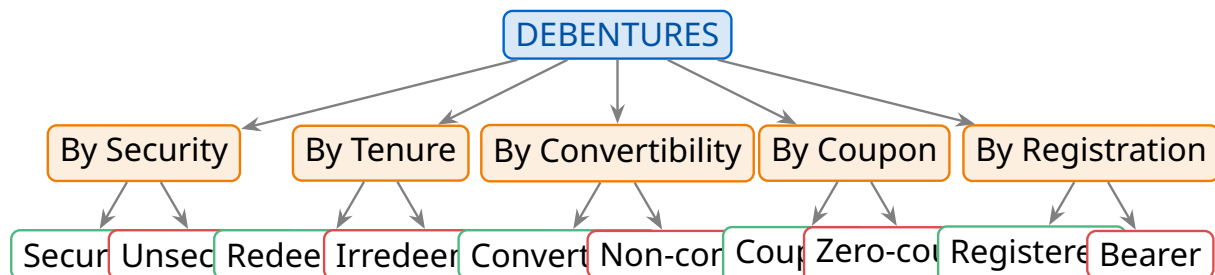
Specific-rate debentures carry a stated interest rate, e.g. “9% Debentures of Rs. 100”. **Zero-coupon debentures** pay no periodic interest; they are issued at a deep discount and redeemed at face value, so the investor’s return is the implicit “interest” built into the discount.

2.5 By registration, registered vs bearer

Registered debentures are recorded in the company’s register of debentureholders and are transferred only by a written instrument of transfer. **Bearer debentures** are not recorded in the register and are transferred by delivery.

Debentures are payable to whoever holds the certificate; they are transferable by mere delivery, like cash. Interest on bearer debentures is paid against coupons clipped from the certificate.

2.6 Visual map of debenture types



Memory Aid

S-T-C-C-R, Security, Tenure, Convertibility, Coupon, Registration. The five lenses through which any debenture can be classified.

3 Issue of Debentures, The Three Pricing Levels

Like shares, debentures can be issued *at par*, *at a premium* or *at a discount*.

- **At par**, issue price equals face value (e.g. Rs. 100 debenture issued at Rs. 100).
- **At a premium**, issue price exceeds face value (e.g. Rs. 100 issued at Rs. 105). The Rs. 5 excess is credited to *Securities Premium Reserve*.
- **At a discount**, issue price is below face value (e.g. Rs. 100 issued at Rs. 95). The Rs. 5 short-fall is debited to *Discount on Issue of Debentures A/c* (a capital loss to be written off).

In every case, the *nominal* (face) value is what is credited to the Debentures Account, because that is the amount the company owes on redemption.

3.1 Money called in one stage vs in instalments

Debenture issue money is usually called in one lump sum (Application & Allotment together). Occasionally it is called in two stages, Application and Allotment, the same way share issues call money. The journal entries follow exactly the same pattern as shares, only the account heads change to "Debenture Application & Allotment A/c" and "%-Debentures A/c".

3.2 Journal entries, the canonical issue-at-par case

Issue at par, redeemable at par

(a) Receipt of application money:

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

(b) Allotment of debentures:

Debenture Application & Allotment A/c Dr.
 To %-Debentures A/c

3.3 Issue at a discount

When debentures are issued at a discount, the discount is treated as a capital loss. It is debited to *Discount on Issue of Debentures A/c* at the time of allotment.

Issue at a discount, redeemable at par

Bank A/c Dr.
 To Debenture Application & Allotment A/c
 Debenture Application & Allotment A/c Dr.
 Discount on Issue of Debentures A/c Dr.
 To %-Debentures A/c

Maximum discount is governed by SEBI guidelines; in practice it is fixed by the board with shareholder approval.

3.4 Issue at a premium

The premium is credited to **Securities Premium Reserve A/c**, exactly as for shares. Securities Premium can be used (under Section 52 of the Companies Act, 2013) for: issuing fully-paid bonus shares, writing off preliminary expenses, writing off discount/commission on issue of shares or debentures, and providing for the premium payable on redemption of redeemable preference shares or debentures.

Issue at a premium, redeemable at par

Bank A/c Dr.
 To Debenture Application & Allotment A/c
 Debenture Application & Allotment A/c Dr.
 To %-Debentures A/c
 To Securities Premium Reserve A/c

Quick Tip

Whatever the issue price, the **credit to “%-Debentures A/c” is always the nominal value**. The premium goes to Securities Premium; the discount sits as a Dr. balance to be written off. This single rule resolves 90% of the confusion in this chapter.

4 Terms of Issue, The Six Standard Combinations

A debenture has two prices that matter: the **price at which it is issued** and the **price at which it will be redeemed**. Each can be at par, at a discount, or at a premium, giving the six classical combinations every student must memorise.

The six issue-redemption combinations

1. Issued at par, redeemable at par
2. Issued at a discount, redeemable at par
3. Issued at a premium, redeemable at par
4. Issued at par, redeemable at a premium
5. Issued at a discount, redeemable at a premium
6. Issued at a premium, redeemable at a premium

The accounting twist appears whenever **redemption is at a premium**. The premium payable in the future is a liability today, it is credited to **Premium on Redemption of Debentures A/c** (a long-term provision) at the time of issue, and the matching debit goes to **Loss on Issue of Debentures A/c**.

Loss on Issue of Debentures, when does it arise?

Loss on Issue of Debentures A/c is debited with:

- the **premium payable on redemption**, AND
- the **discount on issue**, if any (only when redemption is at a premium and issue is at a discount).

If redemption is at par, there is no Loss on Issue, any issue discount is debited only to “Discount on Issue of Debentures A/c”.

4.1 Diagrammatic view of the six cases

The six combinations form a 3×2 grid. The colour shows where Loss on Issue is involved.



4.2 Worked example, one debenture, six entries

Suppose a company issues Rs. 1,00,000 of 9% debentures of Rs. 100 each, with each pair of issue-and-redemption terms set at a 5% discount or premium where required. The amount of money received and the structure of the allotment journal in each case:

Case	Terms	Issue	Cash in	Loss on Issue	Key credit (besides Debentures)
1	Par / Par	100	1,00,000	-	none
2	5% Disc / Par	95	95,000	-	Discount on Issue Dr. 5,000
3	5% Prem / Par	105	1,05,000	-	Securities Premium Cr. 5,000
4	Par / 5% Prem	100	1,00,000	5,000	Premium on Redemption Cr. 5,000
5	5% Disc / 5% Prem	95	95,000	10,000	Premium on Redemption Cr. 5,000
6	5% Prem / 5% Prem	105	1,05,000	5,000	Sec. Premium 5,000; Prem on Red. 5,000

Watch out: the Cash inflow depends on the **issue** price only, never the redemption terms. In Case 5 (issue at 95, redeem at 105) the bank receives Rs. 95,000, NOT Rs. 90,000. The Rs. 10 hit per debenture (5 discount + 5 redemption premium) sits in “Loss on Issue” and is written off out of profits or Securities Premium.

Quick Tip

Mental shortcut for the allotment entry in Cases 4-6: write the Premium on Redemption credit *first* (always equal to the future premium), then plug the difference into **Loss on Issue** on the Dr. side. The figures fall out automatically.

Pricing ↓ Mode →	Cash	Vendor (other than cash)	Collateral (loan security)
At Par	Bank Dr. Deb. Cr.	Vendor Dr. Deb. Cr.	Suspense Dr. Deb. Cr.
At Premium	Bank Dr. Deb. Cr. + SPR Cr.	Vendor Dr. Deb. Cr. + SPR Cr.	Suspense Dr. Deb. Cr. + SPR Cr.
At Discount	Bank Dr. Discount Dr. Deb. Cr.	Vendor Dr. Discount Dr. Deb. Cr.	(rare; nominal only)

Master matrix of all nine debenture-issue combinations (three pricing levels × three modes). The Debenture A/c is always credited at face value; the premium / discount goes to the SPR or Discount on Issue A/c respectively.

5 Over-subscription of Debentures

When the public applies for more debentures than the company has offered, the issue is **over-subscribed**. The company cannot allot more than the offered quantity. Three options are available, and a single issue often uses a mix:

1. **Reject excess applications**, application money refunded.
2. **Pro-rata allotment**, excess money on partially-accepted applications is adjusted against the next call.
3. **Full acceptance up to allotment + refund the rest.**

Standard over-subscription entries

(i) Allotment of accepted applications:

Application A/c Dr.
To Debentures A/c

(ii) Refund of rejected applications:

Application A/c Dr.
To Bank A/c

(iii) Excess application → first call (pro-rata):

Application A/c Dr.
To Call A/c

Two anchors that resolve every over-subscription sum

Anchor 1: Total Bank receipt = Money on rejected applications (which must be refunded) *plus* Money on accepted applications (which is partly allotment

+ partly excess-adjusted-to-call).

Anchor 2: Application A/c is always closed at the end, its debits (allotment, refund, call-adjustment) must equal its credit (cash received).

6 Issue of Debentures for Consideration Other Than Cash

A company can issue debentures to its vendors (often for purchase of plant, business, or land) instead of paying cash. This is called *issue for consideration other than cash*. The journal works in two stages.

6.1 Stage 1: recording the purchase

Purchase of assets from vendor

Sundry Assets A/c Dr. (at agreed value)
 To Sundry Liabilities A/c (if any, taken over)
 To Vendor A/c (purchase consideration, balancing figure)

If Sundry Assets > Sundry Liabilities + Vendor ⇒ Goodwill A/c is Dr.

If Sundry Assets < Sundry Liabilities + Vendor ⇒ Capital Reserve A/c is Cr.

6.2 Stage 2: settling the vendor with debentures

This is where the issue price (par / premium / discount) determines the number of debentures handed over.

Number of debentures to be issued

$$\text{No. of debentures} = \frac{\text{Purchase Consideration}}{\text{Issue Price per debenture}}$$

Cases:

- **At par:** Vendor A/c Dr. → %-Debentures A/c (same amount).
- **At a premium:** Vendor A/c Dr. → %-Debentures A/c (nominal) + Securities Premium Reserve A/c (premium).
- **At a discount:** Vendor A/c Dr. + Discount on Issue of Debentures A/c Dr. → %-Debentures A/c (nominal).

Quick Tip

Trap question: "Issue debentures to vendor at 10% discount to settle a purchase consideration of Rs. 9,00,000." Number of Rs. 100 debentures =

$9,00,000/90 = 10,000$ debentures. NOT 9,000. Always divide by issue price, not face value.

7 Issue of Debentures as Collateral Security

When a company takes a loan from a bank, the bank may insist on debentures as *additional* security alongside the primary security (typically a mortgage on the plant or stock). These debentures are issued *collaterally*: they have no separate accounting existence so long as the company services the loan, but the bank can claim them if the company defaults.

Two accounting treatments are permitted; both are commonly examined.

7.1 Method I, No journal entry, only disclosure

No accounting entry is passed at issue. A note is appended to the Long-term Borrowings schedule of the Balance Sheet: "Secured Loan of Rs. ____ from XYZ Bank, collaterally secured by issue of ____, %-Debentures of Rs. ____ each".

7.2 Method II, Journal entry through Debenture Suspense A/c

Collateral issue, Suspense method

On issue as collateral:

Debenture Suspense A/cDr. (nominal value)
To %-Debentures A/c

On repayment of loan (debentures return / lapse):

%-Debentures A/cDr.
To Debenture Suspense A/c

Both the Debenture Suspense A/c (asset side) and the Debentures A/c (liabilities side) appear at nominal value, exactly offsetting each other. On repayment of the loan, both are reversed.

Common Mistake

Collateral debentures are NOT secured borrowings in the bank's primary security sense, they are a fall-back. The bank will encash them only if the company defaults on the cash loan. Do not record any interest expense on collateral debentures.

8 Interest on Debentures

Interest on debentures is a **charge against profit**, not an appropriation. It must be paid whether or not the company has earned a profit. Under the Income-tax Act 1961, the company must deduct TDS at the prescribed rate (currently 10% under Section 193, subject to thresholds) before paying interest to debentureholders.

8.1 Standard journal sequence

Interest & TDS, four-step cycle

1. Interest becomes due:

Debenture Interest A/c	Dr.
To Income Tax Payable A/c (TDS)	
To Debentureholders A/c (net)	

2. Net interest paid:

Debentureholders A/c	Dr.
To Bank A/c	

3. TDS deposited with Government:

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

4. Year-end transfer to P&L:

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

8.2 Worked example, 10% debentures, half-yearly interest

A company has 10,000, 10% debentures of Rs. 100 each outstanding the whole year. Interest is payable half-yearly on 30 September and 31 March. TDS rate = 10%.

- Annual interest = $10,00,000 \times 10\% = \text{Rs. } 1,00,000$.
- Half-yearly = Rs. 50,000.
- TDS per half = Rs. 5,000; Net cash to holders per half = Rs. 45,000.

Quick Tip

In a single MCQ, the choices often differ by whether interest is computed on **nominal** value or on **issue** value. Always use **nominal value**, the coupon rate (e.g. 9%) is by definition a rate on face value, even for debentures issued at a discount.

9 Writing Off Discount/Loss on Issue of Debentures

“Discount on Issue of Debentures” and “Loss on Issue of Debentures” are both *capital losses*. They carry a debit balance and have to be written off so they do not stay on the balance sheet forever.

9.1 Order of sources for write-off

Section 52 priority for writing off capital losses

1. **Securities Premium Reserve** (preferred, as Section 52 explicitly permits this use)
2. **Statement of Profit & Loss** (when Securities Premium is exhausted or unavailable)

A company must first exhaust Securities Premium Reserve before charging the P&L. The write-off is made *in the year of issue* for the full amount (the older “proportionate write-off over the life of the debentures” method is no longer Ind-AS compliant for newly issued debentures).

9.2 Journal entries for write-off

Writing off Discount/Loss on Issue

Out of Securities Premium Reserve:

Securities Premium Reserve A/c Dr.
 To Discount on Issue of Debentures A/c
 To Loss on Issue of Debentures A/c

Out of Statement of P&L (when SPR insufficient):

Statement of Profit & Loss Dr.
 To Discount on Issue of Debentures A/c
 To Loss on Issue of Debentures A/c

9.3 Worked example, write-off when SPR is partial

X Ltd. issues 150, 7% debentures of Rs. 1,000 each at a 5% discount, redeemable at a 10% premium. Securities Premium Reserve balance on the date of issue = Rs. 20,000.

- Discount on Issue = $150 \times 1,000 \times 5\% = \text{Rs. } 7,500$.
- Premium on Redemption = $150 \times 1,000 \times 10\% = \text{Rs. } 15,000$.
- **Loss on Issue A/c (Dr. balance)** = Discount + Redemption Premium = Rs. 22,500.

Write-off:

- Out of Securities Premium Reserve: Rs. 20,000.
- Out of Statement of Profit & Loss: Rs. 2,500 (the balance).

Common Mistake

A common slip: students try to write off only the *discount on issue* (Rs. 7,500) and forget the premium-on-redemption portion (Rs. 15,000). When debentures are issued at a discount AND redeemable at a premium, the entire combined figure sits in Loss on Issue and is written off together, there is no separate Discount on Issue Account in this case.

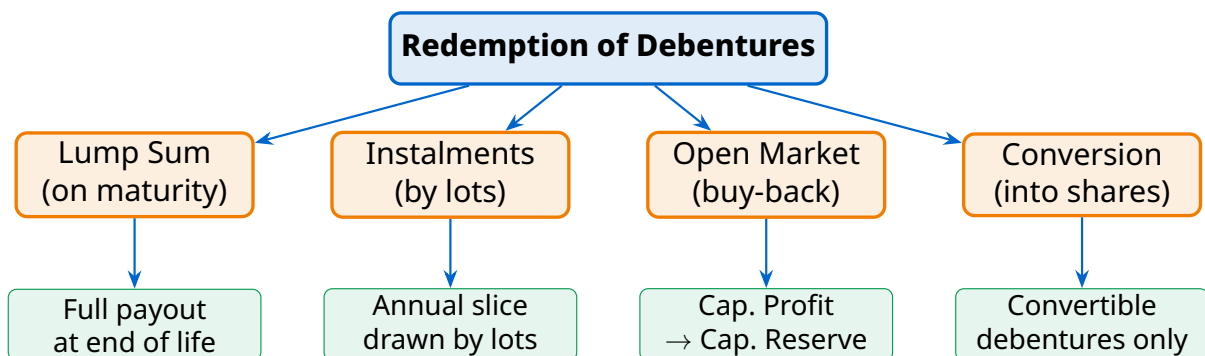
Solve the Part 2 Chapter 2 NCERT Exercises

10 Redemption of Debentures, The Big Picture

Redemption means discharging the company’s liability to the debentureholders. It is the second half of the debenture cycle. Four methods are recognised:

Four methods of redemption

1. **Payment in lump sum**, the entire face value (plus any premium) is paid on the maturity date.
2. **Payment in instalments**, a fixed number of debentures is redeemed each year by drawing lots.
3. **Purchase in the open market**, the company buys back its own debentures at the prevailing market price and cancels them.
4. **Conversion into shares or new debentures**, only for convertible debentures.



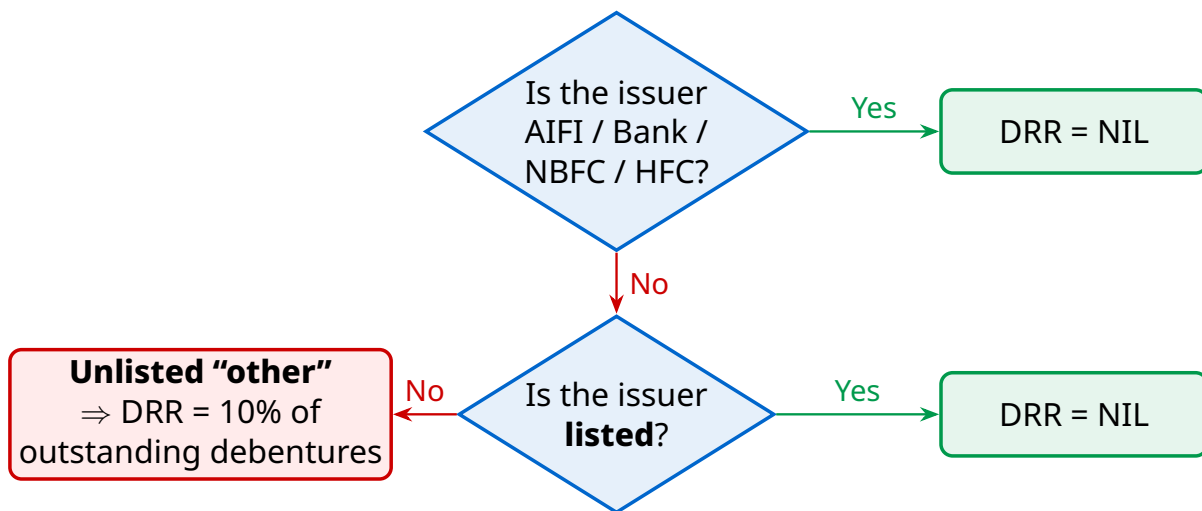
Four routes a company can take to extinguish its debenture liability. The accounting entries diverge sharply across the four, but every route runs through the DRR + DRI compliance gate first.

Before drilling into each method, two regulatory anchors govern *all* of them: the Debenture Redemption Reserve (DRR) and the Debenture Redemption Investment (DRI).

10.1 Debenture Redemption Reserve (DRR), Section 71(4)

DRR is an appropriation of profit that ring-fences cash for future redemption. The rule (post-2019 amendment to the Companies Act):

Type of issuer	DRR requirement
All-India financial institutions (AIFIs) regulated by RBI	NIL
Banking companies regulated by RBI	NIL
NBFCs registered with RBI	NIL
Housing Finance Companies registered with NHB	NIL
Listed companies (whether public or private)	NIL
Unlisted companies (other than those above)	10% of outstanding debentures



DRR decision tree under Sec 71(4): the only category that must create a Debenture Redemption Reserve at 10% is the "unlisted other" company. Listed and regulated issuers carry NIL DRR.

10.2 Debenture Redemption Investment (DRI), Rule 18(7)(c)

In addition to DRR, every company (except the exempted classes above for DRR purposes, check current MCA notification) that is going to redeem debentures in a financial year must, on or before the 30th of April of that year, **invest or deposit at least 15% of the value of debentures maturing in that financial year** in one or more of:

1. Deposits with any scheduled bank, free from charge or lien.
2. Securities of the Central or any State Government.
3. Securities covered by Section 20(a)-(d) and (ee) of the Indian Trusts Act, 1882.
4. Bonds issued by other companies notified under Section 20(f) of that Act.

DRI quantum

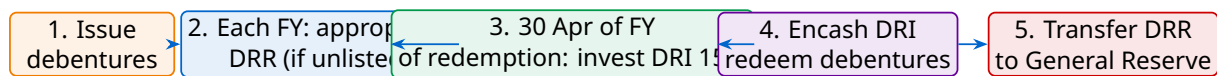
$$\text{Min. DRI} = 15\% \times \text{Face value of debentures maturing in the FY}$$

The investment must be made on/before 30 April of the FY of redemption and may be encashed only for redemption.

Memory Aid

D-R-R = Double Ratio Rule: 10% (DRR, an appropriation) + 15% (DRI, an investment). The first is a slice of profit, the second is a slice of cash, different rules, different ratios, different ledger heads.

10.3 DRR and DRI through the redemption timeline



11 Method 1, Redemption by Payment in Lump Sum

The most common method. The company pays the entire principal (plus any redemption premium) on the maturity date.

11.1 Journal entries, redemption at par

Lump-sum redemption at par

(a) Amount due:

%-Debentures A/c Dr.
 To Debentureholders A/c

(b) Payment to holders:

Debentureholders A/c Dr.
 To Bank A/c

11.2 Journal entries, redemption at premium

Lump-sum redemption at premium

(a) Amount due (face + premium):

%-Debentures A/c Dr. (face value)
 Premium on Redemption of Debentures A/c ... Dr. (redemption premium)
 To Debentureholders A/c (total)

(b) Payment:

Debentureholders A/c Dr.
 To Bank A/c

The "Premium on Redemption of Debentures A/c" was credited *at the time of issue* (when Loss on Issue was debited). At redemption it is debited and thereby closed.

11.3 Worked example, listed company, lump-sum redemption

XYZ Ltd. (**listed**) issued 200, 15% debentures of Rs. 100 each on 1 April 2016 at 10% discount, redeemable at 10% premium on 31 March 2020.

- Face value = Rs. 20,000. Cash received on issue = Rs. 18,000.
- Loss on Issue = Discount (Rs. 2,000) + Redemption Premium (Rs. 2,000) = Rs. 4,000.
- DRR, **NIL** (listed company).
- DRI, must invest 15% of Rs. 20,000 = Rs. 3,000 on/before 30 April 2019.

Key entries:

1. **1 Apr 2016**, Bank A/c Dr. 18,000 / To Debenture Appl. A/c 18,000. Allotment: Appl. A/c Dr. 18,000 + Loss on Issue Dr. 4,000 / To Debentures A/c 20,000 + To Premium on Redemption A/c 2,000.
2. **30 Apr 2019**, Debenture Redemption Investment A/c Dr. 3,000 / To Bank 3,000.
3. **31 Mar 2020**, Bank A/c Dr. 3,000 / To DRI 3,000 (encashment). Then Debentures A/c Dr. 20,000 + Premium on Redemption A/c Dr. 2,000 / To Debentureholders 22,000. Finally Debentureholders A/c Dr. 22,000 / To Bank 22,000.

11.4 Same example as "other unlisted" company

The only differences: **DRR = 10% of Rs. 20,000 = Rs. 2,000** (created out of P&L before redemption), and DRR is later transferred to General Reserve once redemption is complete:

- Before redemption: Statement of P&L Dr. 2,000 / To Debenture Redemption Reserve 2,000.
- After redemption: Debenture Redemption Reserve A/c Dr. 2,000 / To General Reserve 2,000.

Quick Tip

Two-line rule for the exam: (1) Listed \Rightarrow DRR = 0, DRI = 15%. (2) Other unlisted \Rightarrow DRR = 10%, DRI = 15%. Both classes invest DRI; only unlisted appropriate DRR.

12 Method 2, Redemption by Payment in Instalments

When the prospectus specifies that debentures will be redeemed in equal annual instalments (e.g. "redeem 200 debentures every year for 5 years"), the company selects the actual certificate numbers each year by **draw of lots**. The accounting is identical to lump-sum redemption, repeated each year for the slice being redeemed.

12.1 Journal entries each year

Instalment redemption, per-year entries

Each year:

%-Debentures A/c	Dr. (face value of slice)
[Premium on Redemption A/c	Dr. if redeemed at premium]
To Debentureholders A/c	
Debentureholders A/c	Dr.
To Bank A/c	

12.2 DRI under instalment redemption, the rolling rule

Because debentures are redeemed in instalments, DRI is not realised in full on the first redemption. Instead:

- **Initial investment**, 15% of the face value of the first year's instalment, on/before 30 April of that year.
- **Each subsequent year**, top up the DRI balance so it equals 15% of the *next* year's redemption.
- **On the final instalment**, realise all remaining DRI.

12.3 Worked example, Kays Ltd. four-year staggered redemption

Kays Ltd. has 10,000 debentures of Rs. 100 each (= Rs. 10,00,000 face) to redeem as: 2,000 on 31 Jan 2017; 3,000 on 31 Jan 2018; 3,000 on 31 Jan 2019; 2,000 on 31 Jan 2020.

DRI deadline	Next year's redemption	Required DRI	Action
30 Apr 2016	Rs. 2,00,000	Rs. 30,000	Invest Rs. 30,000
30 Apr 2017	Rs. 3,00,000	Rs. 45,000	Top up by Rs. 15,000 (DRI now 45k)
30 Apr 2018	Rs. 3,00,000	Rs. 45,000	No change (already at 45k)
On 31 Jan 2019 re-emption	,	,	Encash Rs. 15,000 (DRI now 30k, i.e. 15% of Rs. 2,00,000 due next)
On 31 Jan 2020 re-emption	,	,	Encash full remaining Rs. 30,000

Common Mistake

The DRI is sized against **next year's** redemption, not this year's. So after each year's redemption you may either need to encash some DRI (if next year's slice is smaller) or invest more (if next year's slice is larger). Always recompute 15% of the *forthcoming* slice.

13 Method 3, Redemption by Purchase in the Open Market

Once issued, debentures trade in the market like any other security. If the market price drops below face value, a company with surplus cash can buy back its own debentures and cancel them, a profitable form of redemption.

13.1 Two sub-cases, purchase below par vs above par

Sub-case A, bought at a price BELOW face value (profit):

Open-market purchase at a discount

Purchase + immediate cancellation:

%-Debentures A/c Dr. (face value)
 To Bank A/c (price paid)
 To Profit on Redemption of Debentures A/c (face – paid)

Transfer profit:

Profit on Redemption A/c Dr.
 To Capital Reserve A/c

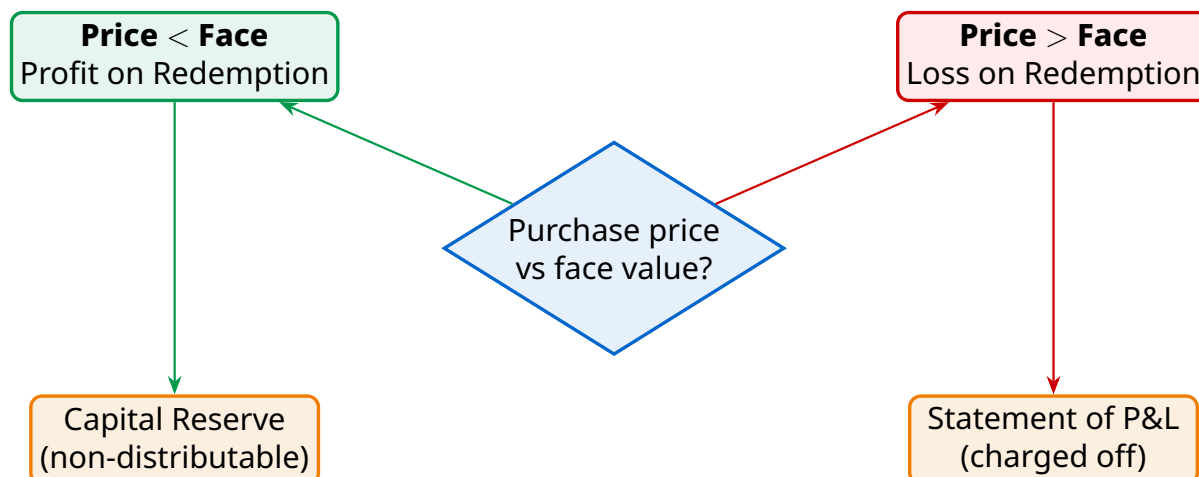
The profit is a capital profit (not available for dividend) and is parked in **Capital Reserve**.

Sub-case B, bought at a price ABOVE face value (loss):

Open-market purchase at a premium

%-Debentures A/c Dr. (face value)
 Loss on Redemption of Debentures A/c Dr. (paid – face)
 To Bank A/c (price paid)

Statement of P&L Dr.
 To Loss on Redemption of Debentures A/c



Open-market redemption: the same purchase splits in two book-keeping routes depending on whether the company bought below or above face value. A profit is capital and never feeds dividend; a loss is revenue and goes through the P&L.

13.2 Why a company buys back in the open market

1. Surplus cash can be deployed productively before maturity.
2. If market price falls below face value, the company saves money.
3. Reduces future interest outflow.
4. Improves debt-to-equity ratio (a positive signal for credit rating).

13.3 Worked example, own debenture bought at 92

X Ltd. buys back debentures of face value Rs. 20,000 (i.e. 200 debentures of Rs. 100 each) at Rs. 92 each. Total paid = Rs. 18,400.

- Profit on redemption = Rs. 20,000 – Rs. 18,400 = Rs. 1,600 → Capital Reserve.

Entries:

- Debentures A/c Dr. 20,000 / To Bank 18,400 / To Profit on Redemption 1,600.
- Profit on Redemption A/c Dr. 1,600 / To Capital Reserve 1,600.

Real-World Application

Reliance Industries has done large open-market repurchases of its own NCDs whenever the yield environment shifts (rates rise → NCD prices fall → repurchase becomes cheap). This neutralises interest-rate risk and books a small

capital reserve in each tranche.

Watch out: “Profit on Redemption” is a **capital** profit and must go to **Capital Reserve**; do not credit it to the Statement of P&L. “Loss on Redemption”, by contrast, is a **revenue** loss and is debited to the Statement of P&L.

14 Method 4, Redemption by Conversion

Only available for convertible debentures. The debentureholder takes shares (or fresh debentures) instead of cash on redemption. The number of shares depends on whether the new shares are issued at par, at a discount, or at a premium.

14.1 Number of shares to be issued

Conversion, the share count

$$\text{No. of shares} = \frac{\text{Amount payable on debentures (face + redemption premium)}}{\text{Issue price of the new share}}$$

If the debentures were *originally* issued at a discount and the terms say “only actual cash received is convertible” (Section 71 read with SEBI Convertible Debenture rules), use the discounted issue proceeds, not the face value.

14.2 Journal entries, standard at-par-or-premium conversion

Conversion entries

(a) Amount due on redemption:

%-Debentures A/c	Dr. (face)
[Premium on Redemption A/c	Dr. if any]
To Debentureholders A/c	

(b) Issue of new shares to debentureholders:

Debentureholders A/c	Dr.
To Equity Share Capital A/c (nominal)	
To Securities Premium Reserve A/c (if shares issued at premium)	

14.3 Worked example, conversion at a premium

Arjun Plastics Ltd. redeems 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.

- Amount due on debentures = Rs. 1,00,000.
- Issue price per share = Rs. 12.50 (= 10 + 2.50).

- Number of equity shares issued = $1,00,000/12.50 = 8,000$ shares.
- Share capital credited = $8,000 \times 10 = \text{Rs. } 80,000$.
- Securities Premium credited = $8,000 \times 2.50 = \text{Rs. } 20,000$.

Common Mistake

Students often divide by the face value (Rs. 10) instead of the issue price (Rs. 12.50). Number of shares is always = Amount due \div Issue price per share, never \div face value. The same trap as in “issue for consideration other than cash”.

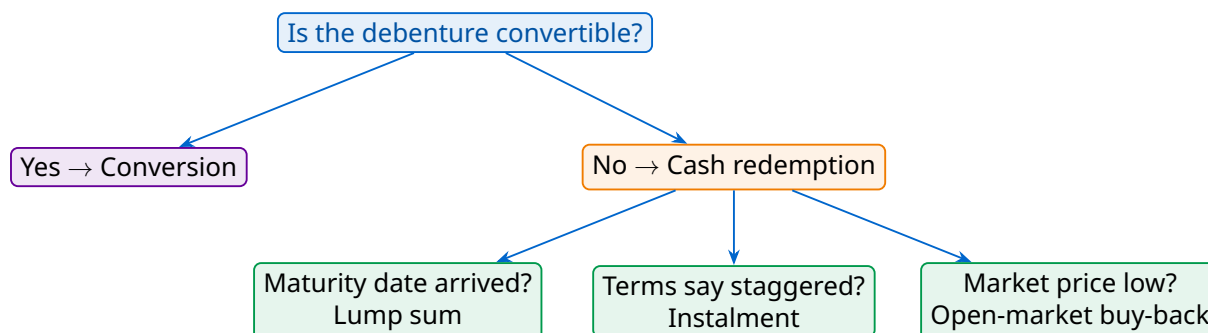
Real-World Application

The Tata Group, Reliance Industries, NTPC and HDFC have all priced large NCD tranches with embedded conversion options over the past two decades. A 2024 example: Reliance Industries’ Rs. 20,000-crore optionally-convertible debenture programme is structured precisely on the conversion-at-premium template you have just worked through.

15 Comparing the Four Methods of Redemption

Method	Trigger	Profit/Loss land- ing	Cash outflow at re- demption
Lump sum	Maturity date	No P&L (just face + premium)	Full face + premium
Instalment	Each year per terms of issue	No P&L (each slice as in lump-sum)	Slice value each year
Open market (below par)	At company’s option	Profit \rightarrow Capital Reserve	Below face value
Open market (above par)	At company’s option	Loss \rightarrow P&L	Above face value
Conversion	At debenture-holder’s option (convertible debentures)	No P&L (transfers to share capital and SPR)	Zero cash; equity issued instead

15.1 Decision tree, which method when



16 Disclosure in the Company’s Balance Sheet

Under Schedule III of the Companies Act 2013, debentures appear under **Non-current Liabilities** → **Long-term Borrowings** (if maturity is more than 12 months away) or under **Current Liabilities** → **Other Current Liabilities** → **Current maturities of long-term debt** (if maturity is within 12 months).

16.1 Key line items and their location

Item	Where it appears in the Balance Sheet
%-Debentures (long-term portion)	Non-current Liabilities → Long-term Borrowings
%-Debentures (current maturities)	Current Liabilities → Other Current Liabilities
Premium on Redemption of Debentures	Non-current Liabilities → Long-term Borrowings (until matured)
Debenture Suspense A/c (collateral, Method II)	Other Non-current Assets (note: shown as deduction from %-Debentures in the notes to accounts)
Securities Premium Reserve	Shareholders’ Funds → Reserves & Surplus
Debenture Redemption Reserve (DRR)	Shareholders’ Funds → Reserves & Surplus
Debenture Redemption Investment (DRI)	Non-current Investments
Discount / Loss on Issue (unwritten-off)	Other Non-current Assets (until written off in year of issue)

Quick Tip

“Premium on Redemption of Debentures” is a **liability**, not an asset, it represents the extra money the company will have to pay on redemption. It sits next to the debentures themselves in Long-term Borrowings until paid out.

17 Common Exam Pitfalls, A Consolidated List

Six recurring slips show up in CBSE / boards / CUET papers each year. Internalise the rule against each one before you sit the paper.

1. **Crediting Debentures A/c at issue price.** *Watch out:* the credit is *always* at face value. Premium goes to SPR; discount goes to Discount on Issue.
2. **Forgetting Premium on Redemption at issue.** If redemption is at a premium, the premium **MUST** be credited *at issue time*, with a matching debit to Loss on Issue, not at redemption time.
3. **Calculating no. of debentures by face value.** For “issue for consideration other than cash” or for vendor issues, divide the purchase consideration by *issue price*, not face value.
4. **Using profit-on-redemption as revenue profit.** Open-market profit is a *capital* profit → Capital Reserve. Open-market loss is *revenue* → Statement of P&L.
5. **Sizing DRI against the wrong year’s slice.** DRI for FY 2024-25 is sized on debentures **maturing in FY 2024-25**, and must be deposited on or before 30 April 2024.
6. **DRR for listed companies.** Listed-company DRR = NIL. Don’t add 10% just because the question is about a public company.

Common Mistake

The single biggest trap: confusing the *issue-side* premium (Securities Premium Reserve, credited at issue) with the *redemption-side* premium (Premium on Redemption of Debentures, a liability). Both are credited at issue time, but they sit on opposite sides of the balance sheet: SPR is part of Reserves & Surplus; Premium on Redemption is part of Long-term Borrowings until paid out.

18 Important Sections & Rules

Section / Rule	What it covers
Sec. 2(30)	Definition of “debenture”
Sec. 52	Permitted uses of Securities Premium (incl. writing off Loss on Issue of Debentures)
Sec. 71	Issue and redemption set of rules; DRR; conversion conditions
Sec. 73-76	Borrowing-related provisions (deposits, debt instruments)
Rule 18(7)(b)	DRR requirement (10% for unlisted “other” companies)
Rule 18(7)(c)	DRI requirement (15% of debentures maturing in the FY)
Schedule III	Balance sheet disclosure format and classification
Sec. 193 IT Act 1961	TDS on interest payable on debentures

19 Quick Reference Summary, All Key Journals on One Page

Issue, the three pricing patterns

1. **At par:** Bank Dr. / Appl. Cr. ; Appl. Dr. / Debentures Cr.
2. **At premium:** Bank Dr. / Appl. Cr. ; Appl. Dr. / Debentures Cr. + Sec. Premium Cr.
3. **At discount:** Bank Dr. / Appl. Cr. ; Appl. Dr. + Discount on Issue Dr. / Debentures Cr.

Redemption at a premium, always book at issue

[Discount Dr. if applicable] + Loss on Issue Dr. / Debentures Cr. + Premium on Redemption Cr.

Write-off of Discount / Loss on Issue

Securities Premium Dr. (first); then Statement of P&L Dr. / Discount or Loss on Issue Cr.

Interest on debentures

Deb. Interest Dr. / Income Tax Payable + Debentureholders Cr.; Pay Debentureholders Dr. / Bank Cr.; Pay TDS Income Tax Payable Dr. / Bank Cr.; Year-end P&L Dr. / Deb. Interest Cr.

Redemption, the four methods

Lump sum: Debentures Dr. [+ Prem. on Red. Dr.] / Debentureholders Cr. ; Debentureholders Dr. / Bank Cr.

Instalment: Same entry, repeated each year for the slice.

Open market (profit): Debentures Dr. / Bank Cr. + Profit on Red. Cr. ; Profit on Red. Dr. / Capital Reserve Cr.

Conversion: Debentures Dr. [+ Prem. on Red. Dr.] / Debentureholders Cr. ; Debentureholders Dr. / Share Capital Cr. [+ Sec. Prem. Cr.].

Statutory checklist before any redemption

- Have I created DRR (10% if I am an "other unlisted" company)?
- Have I invested DRI (15% of debentures maturing this FY, on/before 30 April)?
- Have I encashed DRI on the redemption date and transferred it to Bank?
- Have I transferred DRR to General Reserve after final redemption?

20 Practice Problems for Self-Study

1. A Ltd. issued 5,000, 8% debentures of Rs. 100 each at a discount of 6% redeemable at a premium of 4%. Pass the journal entries on issue, and show the Loss on Issue write-off, assuming the company has a Securities Premium balance of Rs. 25,000.
2. P Ltd. a listed company, has 20,000, 9% debentures of Rs. 100 each maturing on 31 March 2027. Compute the minimum DRI requirement, the deadline for investment, and the journal entry at the time of investment.
3. Q Ltd. buys back, in the open market, debentures of face value Rs. 5,00,000 at Rs. 96 each. Pass the necessary journal entries.
4. R Ltd. converts 2,000, 12% debentures of Rs. 100 each into equity shares of Rs. 10 each at a premium of 25%. Compute the number of shares to be issued and pass the journal entries.
5. S Ltd. (other unlisted) issues 1,000, 10% debentures of Rs. 100 each at par, redeemable in equal annual instalments of 200 debentures starting at the end of year 3. Compute the DRR amount and the rolling DRI schedule.

21 Connection With Other Chapters

- **Part 2 Chapter 1 (Accounting for Share Capital):** Securities Premium Reserve and the writing-off mechanics are identical to those for shares. The over-subscription protocol is the same.
- **Part 2 Chapter 3 (Financial Statements of a Company):** Debentures are disclosed under Long-term Borrowings; DRR sits in Reserves & Surplus; DRI under Non-current Investments. Master this chapter's classification table before attempting Part 2 Chapter 3.
- **Part 2 Chapter 4 (Analysis of Financial Statements) & Part 2 Chapter 1 (Accounting Ratios):** Debentures push up the debt-equity ratio and reduce the interest-coverage ratio. Understanding the issue-redemption mechanics here is what makes the ratio interpretation in those chapters meaningful.

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Continue learning:

- [Ch 8: Analysis of Financial Statements](#)
- [Ch 10: Cash Flow Statement](#)
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End of Notes, Class 12 Accountancy Part 2 Chapter 2, Session 2026-27