Redemption of debenture by Purchase in Open Mkt.

- Purchase for immediate cancellation
- Purchase for investment (in this case debenture known as "Own Debenture")

[I] Purchase for immediate cancellation

Purchase on due date when no sinking fund Exists	Purchase on due date when Sinking Fund (DRFI) Exists
① Purchase debenture ↓	① Sale of DRF Investment ↓
② Profit / Loss on Purchase transfer to CAPITAL RESERVE ↓	② Profit / Loss on sale of DRFI transfer to DRF A/c ↓
③ Transfer of DRR To G/R	③ Purchase of debenture ↓
	④ Profit / Loss on Purchase transfer to DRF A/c ↓
	⑤ Transfer of DRF to General Reserve.

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Journal Entries

When Sinking fund not Exist

① Purchase of debenture and cancellation

Debenture
* Loss on Red. of Deb. A/c
 To Bank
* To Gain on Redem. of Deb

* Only one of two appear.

② Transfer of Profit / Loss to Capital Reserve.

→ If Profit
Gain on Red. of Deb
 To Capital Reserve

→ If Loss
Capital Reserve
Sec. Prem. A/c
 To Loss on Rede. of Deb.

③ Transfer of DRR to General Res.

DRR A/c Dr.
 To General Reserve.

When Sinking Fund Exists

① Sale of sinking fund investment.
Bank
 To DRFI A/c

Profit
DRFI A/c
 To DRR

Loss on Sale
DRR A/c
 To DRFI A/c

② Purchase of debenture
Debenture
* Loss on Red. of Debenture
 To Bank
* To Gain on Red. of Deb.

③ Transfer of Profit / Loss to DRF

Profit
Profit on Red. of Deb
 To DRF A/c

Sale
DRF A/c
 To Loss on Red. of Debenture.

④ Transfer of DRF to G/R

DRF A/c Dr.
 To G/R A/c.

ILLUSTRATION 33. (Redemption of Debenture)

XY Ltd. had issued 10,000 debentures of ₹ 100 each at par. The Company purchased 5,000 debentures from the open market for immediate cancellation at ₹ 95 each on the due date of debenture interest. The company paid the debenture interest on the due date. There was a balance of ₹ 5,00,000 in the Debenture Redemption Reserve Account and ₹ 75,000 in Debenture Redemption Investment Account. The company did not realise the investments. Pass the journal entries for purchase of own debentures for immediate cancellation.

SOLUTION

JOURNAL OF XY LTD.

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Debentures A/c	Dr.		5,00,000	
	To Bank A/c				4,75,000
	To Gain on Cancellation of Debentures A/c				25,000
	(Being purchase and cancellation of debentures)				
	Gain on Cancellation of Debentures A/c	Dr.		25,000	
	To Capital Reserve A/c				25,000
	(Being transfer of profit on cancellation of debentures to capital reserve)				
	Debenture Redemption Reserve A/c	Dr.		2,50,000	
	To General Reserve A/c				2,50,000
	(Being transfer of proportionate amount of DRR to General Reserve)				

[II] Purchase of Own Debenture on the due date of int as : Investment and cancellation / Sale at later stage.

When Sinking fund does not exist

① Purchase of own debenture
⇓
② Interest payable to outsiders
⇓
③ Cancellation of own debenture
⇓
④ Profit / Loss on Cancellation transfer to Capital Reserve.
⇓
⑤ DRR transfer to G/R
⇓
⑥ Sale of own debenture.

When Sinking fund Exists.

Sale of Sinking fund
⇓
Profit / Loss on Sale transfer to DRF A/C
⇓
Purchase of own debenture
⇓
Int on debenture paid
⇓
Cancellation of own debenture
⇓
Profit or Loss on Cancellation transfer to DRF A/c
⇓
DRF transfer to G/R

Journal Entry

When no Sinking fund Exist

① Purchase of own debenture

Own Debenture A/c
    To Bank A/c

When Sinking fund Exist

① For Sale of DRF Investment

Bank A/c
* DRF A/c (if loss)
    To DRF I A/c
* To DRF A/c (if profit)

② Purchase of own Debenture

Own Debenture
    To Bank A/c.

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No Sinking fund	With Sinking fund.
2) Int payable on Debenture to outsiders and on own Debenture	3) for int payable
Debenture Int To Bank To Int on Own Debenture	→ (Same)
3) For Cancellation of own Debenture	4) for Cancellation of Own Deb.
Debenture A/c Dr. * Loss on Red. of Deb. A/c To Own Debenture * To Gain on Red. of Deb.	→ (Same)
4) Profit / Loss transfer to Capital Reserve	5) Profit / Loss transfer to DRF A/c
Profit: Profit on Red. To Capital Rese.	(i) If Profit Profit on Red of Deb To DRF A/c
Loss: Capital Reserve, Sec. Prem. To Loss on Red. of Deb	(ii) If Loss DRF A/c Dr. To Loss on Red. of Deb. A/c
5) DRR transfer to G/R DRR A/c Dr. To General Reserve	6) DRF transfer to G/R DRF A/c Dr. To General Reserve
6) Sale of own Debenture. Bank A/c * Loss on Sale of Own Deb. To Own Debenture * To Profit on Sale of Own Deb.	⇒ (Same)

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ILLUSTRATION 36. Purchase of own debentures and sale of own debentures)

On 1st April, 2019, Sunshine Ltd. had 10,000, 12% Debentures of ₹ 100 each. On this date the company purchased 2,000 own debentures @ ₹ 96 each in the open market. Out of these, 1200 debentures were sold by the company on 30th September, 2019 @ ₹ 95 each. Interest is payable on 30th September and 31st March. Journalise the transactions for the year ended 31st March, 2020.

SOLUTION

JOURNAL OF SUNSHINE LTD.

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
2019 Apr. 1	Own Debentures A/c	Dr.		1,92,000	
	To Bank A/c				1,92,000
	(Being the purchase of 2,000 own debentures @ ₹ 96 each)				
2019 Sept. 30	Debenture Interest A/c	Dr.		60,000	
	To Debentureholders A/c				48,000
	To Interest on Own Debentures A/c				12,000
	(Being interest on 8,000 debentures credited for six months to outside debentureholders and interest on 2,000 own debentures credited to Interest on Own Deb. A/c)				
"	Debentureholders A/c			48,000	
	To Bank A/c				48,000
	(Interest paid to outside debentureholders)				
"	Bank A/c (1,200 x ₹ 95)	Dr.		1,14,000	
	Loss on sale of Own Debentures A/c	Dr.		1,200	
	To Own Debentures A/c (1,200 x ₹ 96)				1,15,200
	(Being sale of own debentures and excess of cost over sale proceeds debited to Loss on Sale of Own Debentures A/c)				
2020 Mar. 31	Debenture Interest A/c	Dr.		60,000	
	To Debentureholders A/c				55,200
	To Interest on Own Debentures A/c				4,800
	(Being the interest for six months on 9,200 debentures payable to outside debentureholders and interest on 800 debentures held by the company itself)				
"	Profit and Loss A/c	Dr.		1,20,000	
	To Debenture Interest A/c				1,20,000
	(Being the debenture interest transferred to Profit and Loss A/c)				

Date	*Particulars*		*L.F.*	*Dr. (₹)*	*Cr. (₹)*
Mar. 31	Profit and Loss A/c	Dr.		1,200	
	To Loss on Sale of Own Debentures A/c				1,200
	(Being loss on sale of own debentures transferred to Profit and Loss A/c)				
"	Interest on Own Debentures	Dr.		16,800	
	To Profit and Loss A/c				16,800
	(Being interest on own debentures transferred to Profit and Loss A/c)				

Date / /
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[III] Cum Interest and Ex-Interest Quotation.

⇒ When debenture are purchase in open market on a date other than date of payment of interest, distinction must be made b/w capital portion ~~&~~ Revenue portion

⇒ Capital portion ⇒ is cost of debenture
⇒ Revenue portion is interest from last date of payment of interest to the date of purchase.

⇒ Price quotation debend upon whether it is Cum-Interest or Ex-Interest

⇒ Cum-Interest means inclusive of Interest. In other word, Price Quotation already include Interest

Payment to Seller = Quotation Price

⇒ Ex-Interest means exclusive of Interest. In this case buyer has to made extra payment of Interest accrued upto date of purchase.

⇒ Date of Interest ⇒ 31st March, 30th Sep, 30th June, 31st Dec

ILLUSTRATION 41. (Purchase of debentures for immediate cancellation)

A listed company purchased from the market its own 400, 12% debentures of ₹ 100 each at ₹ 90 on 31st December, 2019. Pass the necessary Journal entries on 31st December, 2019 in the following cases:

(i) When debentures are purchased cum-interest and cancelled immediately,

(ii) When debentures are purchased ex-interest and not cancelled immediately.

Debenture interest is paid on 30th September and 31st March. Accounts are closed on 31st March. Assume that the company is not required to create Debenture Redemption Reserve.

[B.Com. (H), Delhi, 2009, Modified]

SOLUTION

(*i*) When debentures are purchased cum-interest and cancelled immediately

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2019					
Dec. 31	12% Debentures A/c	Dr.		40,000	
	Debenture Interest A/c	Dr.		1,200	
	To Bank A/c				36,000
	To Gain on Redemption of Debentures A/c				5,200
	(Being purchase of 400 own 12% debentures at ₹ 90 cum-interest for immediate cancellation)				
	Gain on Redemption of Debentures A/c	Dr.		5,200	
	To Capital Reserve A/c				5,200
	(Being transfer of profit on redemption)				

(*ii*) When debentures are purchased ex-interest and not cancelled immediately

JOURNAL

Date	*Particulars*		*L.F.*	*Dr.* (₹)	*Cr.* (₹)
2019					
Dec. 31	Own Debentures A/c	Dr.		36,000	
	Debenture Interest A/c	Dr.		1,200	
	To Bank A/c				37,200
	(Being purchase of 400 own 12% debentures at ₹ 90 ex-interest as investment)				

Working Notes:

(1) Debenture interest for expired period, i.e., from 1st October, 2008 to 31st December, 2008
= (40,000 x 12/100) x 3/12 = ₹ 1,200

(2) Cost of debentures purchased at ₹ 90 cum-interest for immediate cancellation
= 400 x 90 = ₹ 36,000.

(3) Cost of debentures purchased at ₹ 90 ex-interest as investment
= 400 x ₹ 90 + Interest for expired period ₹ 1,200
= ₹ 36,000 + ₹ 1,200 = ₹ 37,200