

Quadrant II – Notes

Programme: Bachelor of Commerce (Third Year)

Subject: Commerce

Paper Code: UCOD125

Paper Title: DSE – 7 Accounting II

Unit: Unit III – Redemption of Debentures

Module Name: Redemption of Debentures- Problem-Solution as per Insurance Policy Method

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Insurance Policy Method- Meaning.

Under this method, to make provision for redemption of debentures, one insurance policy is to be taken. Hence a fixed amount of premium is paid every year to the insurance company, which in turn agrees to pay the necessary amount for the redemption of debentures after the expiry of a specified period. In this method the amount of annual contribution to the Sinking fund is utilized for paying premium for this insurance policy, instead of investing this amount in outside securities. This method avoids the possibility of any loss on realization of investments.

Following Journal entries will be passed under this method:

In Each year:

(i) For Payment of Insurance Premium:

Debenture Redemption Fund Policy A/c Dr.

To Bank A/c

(ii) For appropriation of Amount of Premium:

Profit and Loss Appropriate A/c Dr.

To Debenture Redemption Fund A/c

In the Last year:

(i) For the Amount Received from Insurance Company:

Bank A/c Dr.

To Debenture Redemption Fund Policy A/c

(ii) For Profit on Insurance Policy:

Debenture Redemption Fund Policy A/c Dr.

To Debenture Redemption Fund A/c

(iii) For Amount paid to Debenture-holders:

Debentures A/c Dr.

To Bank A/c

(iv) For Balance of Debenture Redemption Fund A/c Transferred to General Reserve:

Debentures Redemption Fund A/c Dr.

To General Reserve A/c

Illustration on Redemption of Debentures- Insurance Policy Method

On 1-1-2017 Globex Ltd. issued 100, 8% Debentures of Rs. 100 each at par- repayable also at par. The term of issues included that the company must provide a sinking fund for redemption of debentures on 31-12-2019.

The Board of Directors decided to take out an insurance policy to provide the necessary cash, the annual premium being Rs. 3,141 on which the return is 3% p.a. compound interest. [calculation to be made to nearest rupee]

You are required to show in the books of Globex Ltd.

- 8% Debenture Account
- Debenture Redemption Fund Account
- Debenture Redemption Insurance Policy
- Debenture holders Account

For the years 2017 to 2019

Insurance Policy Method- Solution					
Ledger Account					
8% Debenture Account					
Date	Particulars	Amount	Date	Particulars	Amount
31.12.17	To Balance c/d	10,000	1.1.17	By Bank A/c	10,000
		<u>10,000</u>			<u>10,000</u>
31.12.18	To Balance c/d	10,000	1.1.18	By Bank A/c	10,000
		<u>10,000</u>			<u>10,000</u>
31.12.19	To Debenture holder A/c	10,000	1.1.19	By Bank A/c	10,000
		<u>10,000</u>			<u>10,000</u>
Debenture Redemption Fund Account					
Date	Particulars	Amount	Date	Particulars	Amount
31.12.17	To Balance c/d	3,235	31.12.17	By P/L a/c	3,141
			31.12.17	By Debenture Redemption Policy	94 (3,141 X 3%)
		<u>3,235</u>			<u>3,235</u>
31.12.18	To Balance c/d	6,567	1.1.18	By Balance b/d	3,235
			31.12.18	By P/L a/c	3,141
			31.12.18	By Debenture Redemption Policy	191 (6,376 X 3%)
		<u>6,567</u>			<u>6,567</u>
31.12.2019	To Balance c/d	10,000	1.1.19	By Balance b/d	6,567
			31.12.19	By P/L a/c	3,141
			31.12.19	By Debenture Redemption Policy	292 (9,708 X 3%)
		<u>10,000</u>			<u>10,000</u>
Debenture Redemption Insurance Policy					
Date	Particular	Amount	Date	Particular	Amount
1.1.17	To Bank (premium)	3,141	31.12.17	By Balance c/d	3,235
31.12.17	To Debenture Redemption Fund	94			
		<u>3,235</u>			<u>3,235</u>
1.1.18	To Balance b/d	3,235	31.12.18	By Balance c/d	6,567
1.1.18	To Bank (premium)	3,141			
31.12.18	To Debenture Redemption Fund A/c	191			
		<u>6,567</u>			<u>6,567</u>
1.1.19	To Balance b/d	6,567	31.12.19	By Bank a/c (Policy money realised)	10,000
1.1.19	To Bank (premium)	3,141			
31.12.19	To Debenture Redemption Fund	292			
		<u>10,000</u>			<u>10,000</u>
Debenture holders Account					
Date	Particular	Amount	Date	Particular	Amount
31.12.19	To Bank a/c	10000	31.12.19	By 8% Debenture A/c	10000
		<u>10,000</u>			<u>10,000</u>