CHAPTER 7

REDEMPTION OF PREFERENCE SHARES

LEARNING OUTCOMES

After studying this unit, you will be able to–

- understand the meaning of redemption and the purpose of issuing redeemable preference shares;
- learn various provisions of the Companies Act, 2013 regarding preference shares and their redemption;
- familiarise yourself with various methods of redemption of fully paid-up preference shares: (i) by Fresh issue of shares; (ii) by Capitalisation of undistributed profits; (iii) Combination of (i) and (ii);
- understand the logic behind the creation of capital redemption reserve account;
- learn the accounting treatment for redemption of fully paid-up preference shares, partly called-up preference shares and fully called-up but partly paid-up preference shares.

CHAPTER OVERVIEW

Methods of redemption of Preference shares

- By Fresh issue of shares (a)
- (b) Capitalisation of undistributed profits
- Combination of (a) and (b)

1. INTRODUCTION

Redemption is the process of repaying an obligation, at prearranged amounts and timings. It is a contract giving the right to redeem preference shares within or at the end of a given time period at an agreed price. These shares are issued on the terms that shareholders will at a future date be repaid the amount which they invested in the company (along with frequent payment of a specified amount as return on investment during the tenure of the preference shares). The redemption date is the maturity date, which specifies when repayment takes place and is usually printed on the preference share certificate. Through the process of redemption, a company can also adjust its financial structure, for example, by eliminating preference shares and replacing those with other securities if future growth of the company makes such change advantageous.

2. PURPOSE OF ISSUING REDEEMABLE PREFERENCE SHARES

A company may issue redeemable preference shares because of the following:

1 It is a proper way of raising finance in a dull primary market.

2. A company may face difficulty in raising share capital, as its shares are not traded on the stock exchange. Potential investors, hesitant in putting money

into shares that cannot easily be sold, may be encouraged to invest if the shares are redeemable by the company.

3 The preference shares may be redeemed when there is a surplus of capital and the surplus funds cannot be utilised in the business for profitable use.

In India, the issue and redemption of preference shares is governed by Section 55 of the Companies Act, 2013.

3. PROVISIONS OF THE COMPANIES ACT (SECTION 55)

A company limited by shares if so authorised by its Articles, may issue preference shares which at the option of the company, are liable to be redeemed within a period, normally not exceeding 20 years from the date of their issue. It should be noted that:

(a) no shares can be redeemed except out of profit of the company which would otherwise be available for dividend or out of proceeds of fresh issue of shares made for the purpose of redemption;

(b) no such shares can be redeemed unless they are fully paid;

(c) (i) in case of such class of companies, as may be prescribed and whose financial statement comply with the accounting standards prescribed for such class of companies under Section 133, the premium, if any, payable on redemption shall be provided for out of the profits of the company, before the shares are redeemed:

Provided also that premium, if any, payable on redemption of any preference shares issued on or before the commencement of this Act by any such company shall be provided for out of the profits of the company or out of the company's securities premium account, before such shares are redeemed.

(ii) in case of other companies (not falling under (i) above), the premium, if any payable on redemption shall be provided for out of the profits of the company or out of the company's securities premium account, before such shares are redeemed.

(d) where any such shares are proposed to be redeemed out of the profits of the company, there shall, out of profits which would otherwise have been available for dividends, be transferred to a reserve account to be called

Capital Redemption Reserve Account, a sum equal to the nominal amount of the shares redeemed; and the provisions of the Act relating to the reduction of the share capital of a company shall, except as provided in the Section, apply as if the Capital Redemption Reserve (CRR) Account were the paid-up share capital of the company. The utilisation of CRR Account is further restricted to issuance of fully paid-up bonus shares only.

From the legal provision outlined above, it is apparent that on the redemption of redeemable preference shares out of accumulated profits it will be necessary to transfer to the Capital Redemption Reserve Account an amount equal to the amount repaid on the redemption of preference shares on account of face value less proceeds of a fresh issue of capital made for the purpose of redemption. The object is that with the repayment of redeemable preference shares, the security for creditors/ bankers, etc. should not be reduced. At times, a part of the preference share capital may be redeemed out of accumulated profits and the balance out of a fresh issue.

4. METHODS OF REDEMPTION OF FULLY PAID-UP SHARES

Redemption of preference shares means repayment by the company of the obligation on account of shares issued. According to the Companies Act, 2013, preference shares issued by a company must be redeemed within the maximum period (normally 20 years) allowed under the Act. Thus, a company cannot issue irredeemable preference shares. Section 55 of the Companies Act, 2013, deals with provisions relating to redemption of preference shares. It ensures that there is no reduction in shareholders' funds due to redemption and, thus, the interest of outsiders is not affected. For this, it requires that either fresh issue of shares is made or distributable profits are retained and transferred to 'Capital Redemption Reserve Account'.

The rationale behind these provisions is to protect the interest of outsiders to whom the amount is payable before redemption of preference share capital. The interest of outsiders is protected if the nominal value of capital redeemed is substituted, thus, ensuring the same amount of shareholders fund. In case of redemption of preference shares out of proceeds of a fresh issue of shares, replacement of capital and tangible assets is obvious. But, if redemption is done out of distributable profits, replacement of capital is ensured in an indirect manner by retention of profit by transfer to Capital Redemption Reserve. In this case, the amount which would have gone to shareholders in the form of dividend is retained in the business and is used for settling the claim of preference shareholders. Thus, there is no additional claim on net assets of the Company. The transfer of divisible profits to Capital Redemption Reserve makes them non-distributable profits. As Capital Redemption Reserve can be used only for issue of fully paid bonus shares, profits retained in the business ultimately get converted into share capital.

Security cover available to outside stakeholders depends upon called-up capital as well as uncalled capital to be demanded by the company as per its requirements. To ensure that the interests of outsiders are not reduced, Section 55 provides for redemption of only fully paid-up shares.

From the above paras, it can be concluded that the 'gap' created in the company's capital by the redemption of redeemable preference shares much be filled in by:

(a) the proceeds of a fresh issue of shares;

(b) the capitalisation of undistributed profits; or

(c) a combination of (a) and (b).

4.1 REDEMPTION OF PREFERENCE SHARES BY FRESH ISSUE OF SHARES

One of the methods for redemption of preference shares is to use the proceeds of a fresh issue of shares. A company can issue new shares (equity share or preference share) and the proceeds from such new shares can be used for redemption of preference shares.

The proceeds from issue of debentures cannot be utilised for the purpose.

A problem arises when a fresh issue is made for the purpose of redemption of preference shares, at a premium. The point to ponder is that whether the proceeds of a fresh issue of shares will include the amount of securities premium for the purpose of redemption of preference shares.

For securities premium account, Section 52 of the Companies Act, 2013 provides that the securities premium account may be applied by the company;

(a) Towards issue of un-issued shares of the company to be issued to members of the company as fully paid bonus securities

(b) To write off preliminary expenses of the company

(c) To write off the expenses of, or commission paid, or discount allowed on any of the securities or debentures of the company

(d) To provide for premium on the redemption of redeemable preference shares or debentures of the company.

(e) For the purchase of its own shares or other securities.

Note : If may be noted that certain class of Companies whose financial statements comply with the Accounting Standards as prescribed under Section 133 of the Companies Act, 2013, can't apply the securities premium account for the purposes (b) and (d) mentioned above.

Note : All the questions in this chapter have been solved on the basis that the companies referred in the questions are governed by Section 133 of the Companies Act, 2013 and comply with the Accounting Standards prescribed for them. Accordingly the balance in securities premium account has not been utilized for the purpose of premium payable on redemption of preference shares.

Any other way, except the above prescribed ways, in which securities premium account is utilised will be in contravention of law.

Thus, the proceeds of a fresh issue of shares will not include the amount of securities premium for the purpose of redemption of preference shares.

4.1.1 Reasons for issue of New Equity Shares

A company may prefer issue of new equity shares for the following reasons:

(a) When the company has come to realise that the capital is needed permanently and it makes more sense to issue Equity Shares in place of Redeemable Preference Shares which carry a fixed rate of dividend.

(b) When the balance of profit, which would otherwise be available for dividend, is insufficient.

(c) When the liquidity position of the company is not good enough.

4.1.2 Advantages of redemption of preference shares by issue of fresh equity shares

Following are the advantages of redemption of preference shares by the issue of fresh equity shares:

(1) No cash outflow of money – now or later.

(2) New equity shares may be valued at a premium.

(3) Shareholders retain their equity interest.

4.1.3 Disadvantages of redemption of preference shares by issue of fresh equity shares

The disadvantages are:

(1) There will be dilution of future earnings;

(2) Share-holding in the company is changed.

4.1.4 Accounting Entries

1. When new shares are issued at par

   Bank Account Dr.

   To Share Capital Account

   (Being the issue of ....shares of ₹......each for thepurpose of redemption of preference shares, as per Board's Resolution No...... dated.......)

2. When new shares are issued at a premium

   Bank Account Dr.

   To Share Capital Account

   To Securities Premium Account

   (Being the issue of ....shares of ₹......each at a premium of ₹......each for the purpose of redemption of preference shares as per Board's Resolution No..... dated......)

3. When preference shares are redeemed at par

   Redeemable Preference Share Capital Account Dr.

   To Preference Shareholders Account

4. When preference shares are redeemed at a premium

   Redeemable Preference Share Capital Account Dr.

   Premium on Redemption of Preference Shares Account Dr.

   To Preference Shareholders Account

5. When payment is made to preference shareholders

Preference Shareholders Account Dr.

To Bank Account

6. For adjustment of premium on redemption

Profit and Loss Account Dr.

To Premium on Redemption of Preference Shares Account

Illustration 1

Hinduja Company Ltd. had 5,000, 8% Redeemable Preference Shares of ₹100 each, fully paid up. The company decided to redeem these preference shares at par by the issue of sufficient number of equity shares of ₹10 each fully paid up at par. You are required to pass necessary Journal Entries including cash transactions in the books of the company.

Solution

In the books of Hinduja Company Ltd.

Journal Entries

Date	Particulars		Dr. (₹)	Cr. (₹)
	Bank A/c	Dr.	5,00,000	
	To Equity Share Capital A/c			5,00,000
	(Being the issue of 50,000 Equity Shares of ₹10 each at par for the purpose of redemption of preference shares, as per Board Resolution No ....dated........)			
	8% Redeemable Preference Share Capital A/c	Dr.	5,00,000	
	To Preference Shareholders A/c			5,00,000
	(Being the amount payable on redemption of preference shares transferred to Preference Shareholders Account)			
	Preference Shareholders A/c	Dr.	5,00,000	
	To Bank A/c			5,00,000
	(Being the amount paid on redemption of preference shares)			

Illustration 2

C Ltd. had 10,000, 10% Redeemable Preference Shares of ₹100 each, fully paid up. The company decided to redeem these preference shares at par, by issue of sufficient number of equity shares of ₹10 each at a premium of ₹2 per share as fully paid up. You are required to pass necessary Journal Entries including cash transactions in the books of the company.

Solution

In the books of C Ltd.

Journal Entries

Date	*Particulars*		*Dr. (₹)*	*Cr. (₹)*
	Bank A/c	Dr.	12,00,000	
	To Equity Share Capital A/c			10,00,000
	To Securities Premium A/c			2,00,000
	(Being the issue of 1,00,000 Equity Shares of ₹10 each at a premium of ₹2 per share as per Board's Resolution No..... dated..........)			
	10% Redeemable Preference Share Capital A/c	Dr.	10,00,000	
	To Preference Shareholders A/c			10,00,000
	(Being the amount payable on redemption of preference shares transferred to Preference Shareholders A/c)			
	Preference Shareholders A/c	Dr.	10,00,000	
	To Bank A/c			10,00,000
	(Being the amount paid on redemption of preference shares)			

Note: Amount required for redemption is ₹ 10,00,000. Therefore, face value of equity shares to be issued for this purpose must be equal to ₹ 10,00,000. Premium received on new issue cannot be used to finance the redemption.

Illustration 3

G India Ltd. had 9,000 10% redeemable Preference Shares of ₹ 10 each, fully paid up. The company decided to redeem these preference shares at par by the issue of sufficient number of equity shares of ₹ 9 each fully paid up.

You are required to pass necessary Journal Entries including cash transactions in the books of the company.

Solution

In the books of G India Limited

Journal

Date	*Particulars*		*Dr. (₹)*	*Cr. (₹)*
	Bank A/c	Dr.	90,000	
	To Equity Share Capital A/c			90,000
	(Being the issue of 10,000 Equity Shares of ₹9 each at par, as per Board's Resolution No.......Dated.....)			
	10% Redeemable Preference Shares Capital A/c	Dr.	90,000	
	To Preference Shareholders A/c			90,000
	(Being the amount payable on redemption of preference shares transferred to Preference Shareholders A/c)			
	Preference Shareholders A/c	Dr.	90,000	
	To Bank A/c			90,000
	(Being the amount paid on redemption of preference shares)			

4.1.5 Calculation of Minimum Fresh Issue of Shares

Sometimes, examination problem does not specify the number of shares to be issued for the purpose of redemption of preference shares and requires that the minimum number of shares should be issued to ensure that provisions of Section 55 of the Companies Act, 2013, are not violated. This is done in four steps as given below:

(1) In such cases, the maximum amount of reserves and surplus available for redemption is ascertained taking into account the balances appearing in the balance sheet before redemption and the additional information provided in the problem. For example, if balance of general reserve in the balance sheet is ₹1,00,000 and additional information provides that the Board of Directors have decided that the balance of general reserve should not be less than ₹40,000 under any circumstances, then, the maximum amount of general reserve available for redemption is ₹60,000.

(2) After ascertaining the maximum amount of reserves and surplus available for redemption, adjustment for premium on redemption payable out of profits is made and then it is compared with the nominal value of shares to be redeemed. By comparison, one gets the minimum proceeds of fresh issue as Section 55 permits redemption either out of proceeds of fresh issue or out of divisible profits. Thus,

Minimum Proceeds of Fresh Issue of shares :

Nominal value of preference shares to be redeemed – Maximum amount of reserve and surplus available for redemption.

(3) After computation of minimum proceeds, the minimum number of shares to be issued are determined by dividing minimum proceeds by the proceeds of one share. This is done as follows:

Minimum Number of Shares = Minimum proceeds to comply with Section 55/ face value of one share

Proceeds of one share mean the par value of a share issued, if it is issued at par or premium. However, in case of issue of share at a discount, it refers to the discounted value.

(4) Minimum number of shares calculated as per (3) above, needs to be adjusted due to various reasons. Firstly, shares fractions cannot be issued. Thus, if minimum number of shares as per (3) above includes a fraction, it must be approximated to the next higher figure to ensure that provisions of Section 55 are not violated. Secondly, if the examination problem states that the proceeds/number of shares should be a multiple of say, 10 or 50 or 100, then again the next higher multiple should be considered.

Illustration 4

The Board of Directors of a Company decide to issue minimum number of equity shares of ₹ 9 to redeem ₹ 5,00,000 preference shares. The maximum amount of divisible profits available for redemption is ₹ 3,00,000. Calculate the number of shares to be issued by the company to ensure that provisions of Section 55 are not violated. Also determine the number of shares if the company decides to issue shares in multiples of ₹50 only.

Solution

Nominal value of preference shares	₹ 5,00,000
Maximum possible redemption out of profits	₹ 3,00,000
Minimum proceeds of fresh issue	₹ 5,00,000 – 3,00,000 = ₹ 2,00,000
Proceed of one share	= ₹ 9
Minimum number of shares	$= \frac{2,00,000}{9}$ = 22,222.22 shares

As fractional shares are not permitted, the minimum number of shares to be issued is 22,223 shares.

If shares are to be issued in multiples of 50, then the next higher figure which is a multiple of 50 is 22,250. Hence, minimum number of shares to be issued in such a case is 22,250 shares.

4.1.6 Fresh Issue at a Premium and Minimum Fresh Issue

The calculation of minimum number of shares, when fresh issue is at a premium should be handled very carefully Minimum fresh issue cannot be calculated unless one knows the profits available for replacement of preference shares and profit available for replacement cannot be determined unless one knows the portion of profit available for redemption which is required for paying premium on redemption. To tackle this, assume that profits available for redemption is not required for paying premium on redemption of preference shares. In other words, it means that securities premium including premium on fresh issue is comparatively more than premium on redemption.

If the above assumption holds good, minimum number of shares can be calculated in a simple manner without use of equation. But, if above condition does not hold good, then an equation is used to determine the minimum number of shares.

4.1.7 Minimum Fresh Issue to Provide Funds for Redemption

Besides, ensuring compliance with Section 55, the fresh issue of shares is made to provide funds for making payment to preference shareholders. To calculate minimum number of fresh shares to be issued to provide funds, amount payable to preference shareholders is compared with funds available for redemption and the balance of funds to be raised by fresh issue of shares are calculated. The amount to be raised is divided by the issue price of a share (amount payable by shareholder including premium, if any, on fresh issue) to compute the minimum number of shares to be issued.

Illustration 5

The Balance Sheet of X Ltd. as on 31st March, 20X3 is as follows:

	Particulars	*₹*
	EQUITY AND LIABILITIES	
1.	***Shareholders' funds***	
	a Share capital	*2,90,000*
	b Reserves and Surplus	*48,000*
2.	***Current liabilities***	
	Trade Payables	*56,500*
	Total	***3,94,500***
	ASSETS	
1.	***PPE***	
	Tangible asset	*3,45,000*
	Non-current investments	*18,500*
2.	***Current Assets***	
	Cash and cash equivalents (bank)	*31,000*
	Total	***3,94,500***

The share capital of the company consists of ₹50 each equity shares of ₹2,25,000 and ₹100 each Preference shares of ₹65,000(issued on 1.4.20X1). Reserves and Surplus comprises Profit and Loss Account only.

In order to facilitate the redemption of preference shares at a premium of 10%, the Company decided:

(a) *to sell all the investments for ₹15,000.*

(b) *to finance part of redemption from company funds, subject to, leaving a bank balance of ₹12,000.*

(c) *to issue minimum equity share of ₹ 60 each share to raise the balance of funds required.*

You are required to pass:

The necessary Journal Entries to record the above transactions and prepare the balance sheet as on completion of the above transactions.

Solution

Journal

Date	Particulars		Dr. (₹)	Cr. (₹)
	Bank A/c	Dr.	37,500	
	To Share Application A/c			37,500
	(For application money received on 625 shares @ ₹ 60 per share)			
	Share Application A/c	Dr.	37,500	
	To Equity Share Capital A/c			37,500
	(For disposition of application money received)			
	Preference Share Capital A/c	Dr.	65,000	
	Premium on Redemption of Preference Shares A/c	Dr.	6,500	
	To Preference Shareholders A/c			71,500
	(For amount payable on redemption of preference shares)			
	Profit and Loss A/c*	Dr.	6,500	
	To Premium on Redemption of Preference Shares A/c			6,500
	(For writing off premium on redemption out of profits)			

	Bank A/c	Dr.	15,000	
	Profit and Loss A/c (loss on sale) A/c	Dr.	3,500	
	To Investment A/c			18,500
	(For sale of investments at a loss of ₹ 3,500)			
	Profit and Loss A/c	Dr.	33,750	
	To Capital Redemption Reserve A/c			33,750
	(For transfer to CRR out of divisible profits an amount equivalent to excess of nominal value of preference shares over proceeds (face value of equity shares) i.e., ₹ 65,000 - ₹ 31,250)			
	Preference Shareholders A/c	Dr.	71,500	
	To Bank A/c			71,500
	(For payment of preference shareholders)			

Balance Sheet (after redemption)

	Particulars	Notes No.	₹
	EQUITY AND LIABILITIES		
1.	**Shareholders' funds**		
	a) Share capital	1	2,62,500
	b) Reserves and Surplus	2	38,000
2.	**Current liabilities**		
	Trade Payables		56,500
	Total		3,57,000
	ASSETS		
1.	**PPE**		
	Tangible asset		3,45,000
2.	**Current Assets**		
	Cash and cash equivalents (bank)	3	12,000
	Total		3,57,000

Notes to accounts

			₹
1.	**Share Capital**		
	Equity share capital (2,25,000 + 37,500)		2,62,500
2.	**Reserves and Surplus**		
	Capital Redemption Reserve		33,750
	Profit and Loss Account (48,000 – 6,500 – 3,500 – 33,750)		4,250
			38,000
3.	**Cash and cash equivalents**		
	Balances with banks (31,000 + 37,500 +15,000 – 71,500)		12,000

Working Note:

Calculation of Number of Shares:	₹
Amount payable on redemption	71,500
Less: Sale price of investment	(15,000)
	56,500
Less: Available bank balance (31,000 - 12,000)	(19,000)
Funds from fresh issue	37,500

∴ No. of shares = 37,500/60=625 shares

4.2 REDEMPTION OF PREFERENCE SHARES BY CAPITALISATION OF UNDISTRIBUTED PROFITS

Another method for redemption of preference shares, as per the Companies Act, is to use the distributable profits in place of issuing new shares. When shares are redeemed by utilising distributable profit, an amount equal to the face value of shares redeemed is transferred to Capital Redemption Reserve Account by debiting the distributable profit. In other words, some of the distributable profits are kept aside to ensure that it can never be distributed to shareholders as dividend.

In this connection, the provisions of the Companies Act state that 'When any such shares are redeemed otherwise than out of the proceeds of a fresh issue, there shall out of profits which would otherwise have been available for dividend, be transferred to a reserve fund to be called the Capital Redemption Reserve

Account sum equal to the nominal amount of the shares redeemed'.

4.2.1 Advantages of redemption of preference shares by capitalisation of undistributed profits

The advantages of redemption of preference shares by capitalisation of undistributed profits are:

(1) No change in the percentage of equity share-holding of the company;

(2) Surplus funds can be used.

4.2.2 Disadvantages of redemption of preference shares by capitalisation of undistributed profits

The disadvantage of redemption of preference shares by capitalisation of undistributed profits is that there may be a reduction in liquidity.

Accounting Entries

1. When shares are redeemed at par

Redeemable Preference Share Capital Account Dr.

To Preference Shareholders Account

(Being the amount payable on redemption of preference shares transferred to Preference Shareholders Account)

2. When shares are redeemed at a premium

Redeemable Preference Share Capital Account Dr.

Premium on Redemptions of Preference Shares Account Dr.

To Preference Shareholders Account

(Being the amount payable on redemption transferred to Preference Shareholders Account)

3. When payment is made to preference shareholders

Preference Shareholders Account Dr.

To Bank Account

(Being the payment to preference shareholders as per terms)

4. For adjustment of premium of redemption

Profit and Loss Account Dr.

To Premium on Redemption of Preference Shares Account

(Being the premium on redemption adjusted against Profit and Loss Account)

5. For transferring nominal amount of shares redeemed to Capital Redemption Reserve Account

General Reserve Account Dr.

Profit and Loss Account Dr.

To Capital Redemption Reserve Account

(Being the amount transferred to Capital Redemption Reserve Account as per the requirement of the Act).

Illustration 6

The following are the extracts from the Balance Sheet of ABC Ltd. as on 31st December, 20X1.

Share capital: 40,000 Equity shares of ₹ 10 each fully paid – ₹ 4,00,000; 1,000 10% Redeemable preference shares of ₹ 100 each fully paid – ₹ 1,00,000.

Reserve & Surplus: Capital reserve – ₹ 50,000; Securities premium – ₹ 50,000; General reserve –₹ 75,000; Profit and Loss Account – ₹ 35,000

On 1st January 20X2, the Board of Directors decided to redeem the preference shares at par by utilisation of reserve.

You are required to pass necessary Journal Entries including cash transactions in the books of the company.

Solution

In the books of ABC Limited
Journal Entries

Date	Particulars		Dr. (₹)	Cr. (₹)
20X2				
Jan 1	10% Redeemable Preference Share Capital A/c	Dr.	1,00,000	
	To Preference Shareholders A/c			1,00,000
	(Being the amount payable on redemption transferred to Preference Shareholders Account)			

	Preference Shareholders A/c	Dr.	1,00,000	
	To Bank A/c			1,00,000
	(Being the amount paid on redemption of preference shares)			
	General Reserve A/c	Dr.	75,000	
	Profit & Loss A/c	Dr.	25,000	
	To Capital Redemption Reserve A/c			1,00,000
	(Being the amount transferred to Capital Redemption Reserve Account as per the requirement of the Act)			

Note: Securities premium and capital reserve cannot be utilised for transfer to Capital Redemption Reserve.

4.3 REDEMPTION OF PREFERENCE SHARES BY COMBINATION OF FRESH ISSUE AND CAPITALISATION OF UNDISTRIBUTED PROFITS

A company can redeem the preference shares partly from the proceeds from new issue and partly out of profits. In order to fill in the 'gap' between the face value of shares redeemed and the proceeds of new issue, a transfer should be made from distributable profits (Profit & Loss Account, General Reserve and other Free Reserves) to Capital Redemption Reserve Account.

Formula:

(i) Amount to be Transferred to Capital Redemption Reserve

	₹
Face value of shares redeemed	***
Less: Proceeds from new issue	***
	***

(ii) Proceeds to be collected from New Issue

	₹
Face value of shares redeemed	***
Less: Profits available for distribution as dividend	***
	***

Illustration 7

C Limited had 3,000, 12% Redeemable Preference Shares of ₹100 each, fully paid up. The company had to redeem these shares at a premium of 10%.

It was decided by the company to issue the following:

(i) 25,000 Equity Shares of ₹10 each at par,

(ii) 1,000 14% Debentures of ₹100 each.

The issue was fully subscribed and all amounts were received in full. The payment was duly made. The company had sufficient profits. Show Journal Entries in the books of the company.

Solution

In the books of C Limited
Journal Entries

Date	Particulars		Dr. (₹)	Cr. (₹)
	Bank A/c	Dr.	2,50,000	
	To Equity Share Capital A/c			2,50,000
	(Being the issue of 25,000 equity shares of ₹ 10 each at par as per Board's resolution No......dated.....)			
	Bank A/c	Dr.	1,00,000	
	To 14% Debenture A/c			1,00,000
	(Being the issue of 1,000 Debentures of ₹ 100 each as per Board's Resolution No.....dated......)			
	12% Redeemable Preference Share Capital A/c	Dr.	3,00,000	
	Premium on Redemption of Preference Shares A/c	Dr.	30,000	
	To Preference Shareholders A/c			3,30,000
	(Being the amount payable on redemption transferred to Preference Shareholders Account)			
	Preference Shareholders A/c	Dr.	3,30,000	

	To Bank A/c (Being the amount paid on redemption of preference shares)			3,30,000
	Profit & Loss A/c To Premium on Redemption of Preference Shares A/c (Being the adjustment of premium on redemption against Profits & Loss Account)	Dr.	30,000	30,000
	Profit & Loss A/c To Capital Redemption Reserve A/c (Being the amount transferred to Capital Redemption Reserve Account as per the requirement of the Act)	Dr.	50,000	50,000

Working Note:

Amount to be transferred to Capital Redemption Reserve Account

Face value of shares to be redeemed	3,00,000
Less: Proceeds from new issue	(2,50,000)
Total Balance	50,000

Illustration 8

The capital structure of a company consists of 20,000 Equity Shares of ₹ 10 each fully paid up and 1,000 8% Redeemable Preference Shares of ₹ 100 each fully paid up (issued on 1.4.20X1).

Undistributed reserve and surplus stood as: General Reserve ₹ 80,000; Profit and Loss Account ₹ 20,000; Investment Allowance Reserve out of which ₹ 5,000, (not free for distribution as dividend) ₹ 10,000; Securities Premium ₹ 2,000, Cash at bank amounted to ₹ 98,000. Preference shares are to be redeemed at a Premium of 10% and for the purpose of redemption, the directors are empowered to make fresh issue of Equity Shares at par after utilising the undistributed reserve and surplus, subject to the conditions that a sum of ₹ 20,000 shall be retained in general reserve and which should not be utilised.

Pass Journal Entries to give effect to the above arrangements and also show how the relevant items will appear in the Balance Sheet of the company after the *redemption carried out.*

Solution

In the books of ....
Journal Entries

Date	Particulars		Dr. (₹)	Cr. (₹)
	Bank A/c	Dr.	25,000	
	To Equity Share Capital A/c			25,000
	(Being the issue of 2,500 Equity Shares of ₹ 10 each at a premium of Re. 1 per share as per Board's Resolution No.....dated.......)			
	8% Redeemable Preference Share Capital A/c	Dr.	1,00,000	
	Premium on Redemption of Preference Shares A/c	Dr.	10,000	
	To Preference Shareholders A/c			1,10,000
	(Being the amount paid on redemption transferred to Preference Shareholders Account)			
	Preference Shareholders A/c	Dr.	1,10,000	
	To Bank A/c			1,10,000
	(Being the amount paid on redemption of preference shares)			
	Profit & Loss A/c	Dr.	10,000	
	To Premium on Redemption of Preference Shares A/c			10,000
	(Being the premium payable on redemption is adjusted against Profit & Loss Account)			
	General Reserve A/c	Dr.	60,000	
	Profit & Loss A/c	Dr.	10,000	
	Investment Allowance Reserve A/c	Dr.	5,000	
	To Capital Redemption Reserve A/c			75,000
	(Being the amount transferred to Capital Redemption Reserve Account as per the requirement of the Act)			

Balance Sheet as on ....[Extracts]

	Particulars	Notes No.	₹
	EQUITY AND LIABILITIES		
1.	**Shareholders' funds**		
	a Share capital	1	2,25,000
	b Reserves and Surplus	2	1,02,000
	Total		?
	ASSETS		
2.	**Current Assets**		
	Cash and cash equivalents (98,000 + 25,000 – 1,10,000)		13,000
	Total		?

Notes to accounts

1.	**Share Capital**		
	22,500 Equity shares (20,000 + 2,500) of ₹10 each fully paid up		2,25,000
2.	**Reserves and Surplus**		
	General Reserve		20,000
	Securities Premium		2,000
	Capital Redemption Reserve		75,000
	Investment Allowance Reserve		5,000
			1,02,000

Working Note:

No of Shares to be issued for redemption of Preference Shares:

Face value of shares redeemed		₹1,00,000
Less: Profit available for distribution as dividend:		
General Reserve : ₹(80,000-20,000)	₹60,000	
Profit and Loss (20,000 – 10,000 set aside for		

adjusting premium payable on redemption of preference shares)	₹10,000	
Investment Allowance Reserve: (₹ 10,000-5,000)	₹ 5,000	(₹ 75,000)
		₹ 25,000

Therefore, No. of shares to be issued = 25,000/₹10 = 2,500 shares.

4.4 SALE OF INVESTMENTS TO PROVIDE SUFFICIENT FUNDS FOR REDEMPTION

Companies may have sufficient investments, which can be sold, in the market to arrange funds for redemption of preference shares.

5. REDEMPTION OF PARTLY CALLED-UP PREFERENCE SHARES

One of the conditions of redemption is that only fully paid up preference shares can be redeemed by a company. If the examination problem states that it is decided to redeem preference shares which are partly called up, then it is assumed that final call on these shares is demanded and received before proceeding with redemption of these shares. If information about both fully paid and partly paid preference shares is provided, then, only fully paid shares are redeemed.

Illustration 9

The Balance Sheet of XYZ as at 31st December, 20X1 inter alia includes the following:

	₹
50,000, 8% Preference Shares of ₹100 each, ₹70 paid up	*35,00,000*
1,00,000 Equity Shares of ₹100 each fully paid up	*1,00,00,000*
Securities Premium	*5,00,000*
Capital Redemption Reserve	*20,00,000*
General Reserve	*50,00,000*

Under the terms of their issue, the preference shares are redeemable on 31st March, 20X2 at 5% premium. In order to finance the redemption, the company makes a rights issue of 50,000 equity shares of ₹ 100 each at ₹ 110 per share, ₹ 20 being *payable on application, ₹ 35 (including premium) on allotment and the balance on 1st January, 20X3. The issue was fully subscribed and allotment made on 1st March, 20X2. The money due on allotment were received by 31st March, 20X2. The preference shares were redeemed after fulfilling the necessary conditions of Section 55 of the Companies Act, 2013.*

You are asked to pass the necessary Journal Entries and show the relevant extracts from the balance sheet as on 31st March, 20X2 with the corresponding figures as on 31st December, 20X1.

Solution

Journal Entries

			₹	₹
	8% Preference Share Final Call A/c	Dr.	15,00,000	
	To 8% Preference Share Capital A/c			15,00,000
	(For final call made on preference shares @ ₹ 30 each to make them fully paid up)			
	Bank A/c	Dr.	15,00,000	
	To 8% Preference Share Final Call A/c			15,00,000
	(For receipt of final call money on preference shares)			
	Bank A/c	Dr.	10,00,000	
	To Equity Share Application A/c			10,00,000
	(For receipt of application money on 50,000 equity shares @ ₹ 20 per share)			
	Equity Share Application A/c	Dr.	10,00,000	
	To Equity Share Capital A/c			10,00,000
	(For capitalisation of application money received)			
	Equity Share Allotment A/c	Dr.	17,50,000	
	To Equity Share Capital A/c			12,50,000
	To Securities Premium A/c			5,00,000
	(For allotment money due on 50,000 equity shares @ ₹ 35 per share including a premium of₹ 10 per share)			
	Bank A/c	Dr.	17,50,000	
	To Equity Share Allotment A/c			17,50,000
	(For receipt of allotment money on equity shares)			

	8% Preference Share Capital A/c Premium on Redemption of Preference Shares A/c To Preference Shareholders A/c (For amount payable to preference shareholders on redemption at 5% premium)	Dr. Dr.	50,00,000 2,50,000	 52,50,000
	General Reserve A/c To Premium on Redemption A/c (For writing off premium on redemption of preference shares)	Dr.	2,50,000	 2,50,000
	General Reserve A/c To Capital Redemption Reserve A/c (For transfer of CRR the amount not covered by the proceeds of fresh issue of equity shares i.e., 50,00,000 - 10,00,000 - 12,50,000)	Dr.	27,50,000	 27,50,000
	Preference Shareholders A/c To Bank A/c (For amount paid to preference shareholders)	Dr.	52,50,000	 52,50,000

Balance Sheet (extracts)

	Particulars	Notes No.	As at 31.3.20X2	As at 31.12.20X1
			₹	₹
	EQUITY AND LIABILITIES			
1.	**Shareholders' funds**			
	a) Share capital	1	1,22,50,000	1,35,00,000
	b) Reserves and Surplus	2	77,50,000	75,00,000

Notes to accounts

		As at 31.3.20X2	As at 31.12.20X1
1.	**Share Capital**		
	Issued, Subscribed and Paid up:		
	1,00,000 Equity shares of ₹100 each fully paid up	1,00,00,000	1,00,00,000
	50,000 Equity shares of ₹100 each ₹45 paid up	22,50,000	-

	50,000, 8% Preference shares of ₹100 each, ₹70 called up	-	35,00,000
		1,22,50,000	1,35,00,000
2.	**Reserves and Surplus**		
	Capital Redemption Reserve	47,50,000	20,00,000
	Securities Premium (5,00,000 + 5,00,000)	10,00,000	5,00,000
	General Reserve	20,00,000	50,00,000
		77,50,000	75,00,000

Note: Amount received (excluding premium) on fresh issue of shares till the date of redemption should be considered for calculation of proceeds of fresh issue of shares. Thus, proceeds of fresh issue of shares are ₹22,50,000 (₹10,00,000 application money plus ₹12,50,000 received on allotment towards share capital).

6. REDEMPTION OF FULLY CALLED BUT PARTLY PAID-UP PREFERENCE SHARES

The problem of unpaid calls on fully called up shares may be studied under following categories:

6.1 WHEN CALLS-IN-ARREARS IS RECEIVED BY THE COMPANY

If the amount of unpaid calls is received by the Company before redemption, the entry passed is as under:

Bank A/c Dr.

To Calls-in-Arrears A/c

After receipt of calls in arrears, the shares become fully paid up and, then, company can proceed with redemption in the normal course.

6.2 IN CASE OF FORFEITED SHARES

If, on getting a proper notice from the company, the shareholders fail to pay the unpaid calls, the Board of Directors may decide to forfeit the shares and cancel these shares instead of reissuing the forfeited shares because redemption of these shares is due immediately or in near future. In this case, entry for forfeiture is passed as usual.

SUMMARY

- Redemption is the process of repaying an obligation, at prearranged amount and timing.
- In India, the issue and redemption of preference shares is governed by Section 55 of the Companies Act, 2013.
- A company limited by shares if so authorised by its Articles, may issue preference shares which at the option of the company, are liable to be redeemed. It should be noted that:
  - (a) no shares can be redeemed except out of profit of the company which would otherwise be available for dividend or out of proceeds of fresh issue of shares made for the purpose of redemption;
  - (b) no such shares can be redeemed unless they are fully paid;
- Methods of redemption of fully paid-up preference shares: (i) by Fresh issue of shares; (ii) by Capitalisation of undistributed profits; (iii) Combination of (i) and (ii),

TEST YOUR KNOWLEDGE

MCQ

1. Securities premium cannot be used to ______.
   - (a) Issue bonus shares
   - (b) Redeem preference shares
   - (c) Write-off preliminary expenses
2. S Ltd. issued 2,000, 10% Preference shares of ₹100 each at par on 1.4.20X1, which are redeemable at a premium of 10%. For the purpose of redemption, the company issued 1,500 Equity Shares of ₹100 each at a premium of 20% per share. At the time of redemption of Preference Shares, the amount to be transferred by the company to the Capital Redemption Reserve Account = ?
   - (a) ₹50,000
   - (b) ₹40,000
   - (c) ₹2,00,000
3. Which of the following cannot be used for the purpose of creation of capital redemption reserve account?

(a) Profit and loss account (credit balance)

(b) General reserve account

(c) Unclaimed dividend account

4 According to Section 52 of the Companies Act, 2013, the amount in the Securities Premium A/c cannot be used for the purpose of

(a) Issue of fully paid bonus shares

(b) Writing off losses of the company

(c) For purchase of own securities

5. Which of the following can be utilized for redemption of preference shares?

(a) The proceeds of fresh issue of equity shares

(b) The proceeds of issue of debentures

(c) The proceeds of issue of fixed deposit

6. Which of the following statements is True?

(a) Capital redemption reserve cannot be used for writing off miscellaneous expenses and losses

(b) Capital profit realized in cash cannot be used for payment of dividend

(c) Reserves created by revaluation of fixed assets are not permitted to be capitalized

7. Which of the following accounts can be used for transfer to capital redemption reserve account?

(a) General reserve account

(b) Forfeited shares account

(c) Profit prior to incorporation

8. Preference shares amounting to ₹2,00,000 (already issued on 1.4.20X1) are redeemed at a premium of 5%, by issue of shares amounting to ₹1,00,000 at a premium of 10%. The amount to be transferred to capital redemption reserve = ?

(a) ₹1,05,000

(b) ₹1,00,000

(c) ₹2,00,000

THEORETICAL QUESTIONS

1. What is the purpose of issuing redeemable preference shares?
2. What are the provisions of the Companies Act, 2013 related with redemption of preference shares? Explain in brief.

PRACTICAL QUESTIONS

Question 1

The books of B Ltd. showed the following balance on 31st December, 20X3:

30,000 Equity Shares of ₹10 each fully paid; 18,000 12% Redeemable Preference Shares of ₹10 each fully paid; 4,000 10% Redeemable Preference Shares of ₹10 each, ₹8 paid up (all shares issued on 1st April, 20X2).

Undistributed Reserve and Surplus stood as: Profit and Loss Account ₹80,000; General Reserve ₹1,20,000; Securities Premium Account ₹15,000 and Capital Reserve ₹21,000.

For redemption, 3,000 equity shares of ₹10 each are issued at 10% premium. At the same time, Preference shares are redeemed on 1st January, 20X4 at a premium of ₹2 per share. The whereabouts of the holders of 100 shares of ₹10 each fully paid are not known.

A bonus issue of equity share was made at par, two shares being issued for every five held on that date out of the Capital Redemption Reserve Account. However, equity shares, issued for redemption are not eligible for bonus.

Show the necessary Journal Entries to record the transactions.

Question 2

The following is the summarised Balance Sheet of Bumbum Limited as at 31st March, 20X1:

	₹
Sources of funds	
Authorized capital	
50,000 Equity shares of ₹ 10 each	5,00,000
10,000 Preference shares of ₹ 100 each (8% redeemable)	10,00,000
	15,00,000
Issued, subscribed and paid up	

30,000 Equity shares of ₹ 10 each	3,00,000
5,000, 8% Redeemable Preference shares of ₹ 100 each	5,00,000
Reserves & Surplus	
Securities Premium	6,00,000
General Reserve	6,50,000
Profit & Loss A/c	40,000
2,500, 9% Debentures of ₹ 100 each	2,50,000
Trade payables	1,70,000
	25,10,000
Application of funds	
Fixed Assets (net)	7,80,000
Investments (market value ₹ 5,80,000)	4,90,000
Deferred Tax Assets	3,40,000
Trade receivables	6,20,000
Cash & Bank balance	2,80,000
	25,10,000

In Annual General Meeting held on 20th June, 20X1 the company passed the following resolutions:

(i) To split equity share of ₹ 10 each into 5 equity shares of ₹ 2 each from 1st July.

(ii) To redeem 8% preference shares at a premium of 5%.

(iii) To redeem 9% Debentures by making offer to debenture holders to convert their holdings into equity shares at ₹ 10 per share or accept cash on redemption.

(iv) To issue fully paid bonus shares in the ratio of one equity share for every 3 shares held on record date.

On 10th July, 20X1 investments were sold for ₹ 5,55,000 and preference shares were redeemed.

40% of Debenture holders exercised their option to accept cash and their claims were settled on 1st August, 20X1.

The company fixed 5th September, 20X1 as record date and bonus issue was concluded by 12th September, 20X1

You are requested to journalize the above transactions including cash transactions and prepare Balance Sheet as at 30th September, 20X1. All working notes should form part of your answer.

Question 3

The following is the summarized Balance Sheet of Trinity Ltd. as at 31.3.20X1:

Liabilities	₹	**Assets**	₹
Share Capital		Fixed Assets	
Authorised		Gross Block	3,00,000
10,000 10% Redeemable Preference Shares of ₹ 10 each	1,00,000	Less : Depreciation	1,00,000
			2,00,000
90,000 Equity Shares of ₹10 each	9,00,000	Investments	1,00,000
	10,00,000	Current Assets and Loans	
Issued, Subscribed and Paid-up Capital		and Advances	
10,000 10% Redeemable Preference		Inventory	45,000
Shares of ₹ 10 each	1,00,000	Trade receivables	25,000
10,000 Equity Shares of ₹ 10 each	1,00,000	Cash and Bank Balances	50,000
(A)	2,00,000		
Reserves and Surplus			
General Reserve	1,20,000		
Securities Premium	70,000		
Profit and Loss A/c	18,500		
(B)	2,08,500		
Current Liabilities and Provisions (C)	11,500		
Total (A + B + C)	4,20,000	Total	4,20,000

For the year ended 31.3.20X2, the company made a net profit of ₹35,000 after providing ₹20,000 depreciation.

The following additional information is available with regard to company's operation:

1. The preference dividend for the year ended 31.3.20X2 was paid.

2. Except cash and bank balances other current assets and current liabilities as on 31.3.20X2, was the same as on 31.3.20X1.

3. The company redeemed the preference shares at a premium of 10%.

4. The company issued bonus shares in the ratio of one share for every equity share held as on 31.3.20X2.

5. To meet the cash requirements of redemption, the company sold investments.

6. Investments were sold at 90% of cost on 31.3.20X2.

You are required to prepare necessary journal entries to record redemption and issue of bonus shares.

ANSWERS/ HINTS

MCQ

1. (b) **2.** (a)[1] **3.** (c) **4.** (b) **5.** (a) **6.** (a) **7.** (a) **8.** (b)[2]

THEORETICAL QUESTIONS

1. Refer para 2 of the chapter

2. Refer para 4 of the chapter.

PRACTICAL QUESTIONS

Answer 1

In the books of B Limited

Journal Entries

Date	***Particulars***		***Dr. (₹)***	***Cr. (₹)***
20X1	12% Redeemable Preference Share Capital A/c	Dr.	1,80,000	
Jan 1	Premium on Redemption of Preference Shares A/c	Dr.	36,000	
	To Preference Shareholders A/c			2,16,000

[1] 2,00,000 – 1,50,000

[2] 2,00,000 – 1,00,000

...	(Being the amount payable on redemption of 18,000 12% Redeemable Preference Shares transferred to Shareholders Account)			
	Preference Shareholders A/c	Dr.	2,14,800	
	To Bank A/c			2,14,800
	(Being the amount paid on redemption of 17,900 preference shares)			
	Bank A/c	Dr.	33,000	
	To Equity Shares Capital A/c			30,000
	To Securities Premium A/c			3,000
	(Being the issue of 3,000 Equity Shares of ₹ 10 each at a premium of 10% as per Board's Resolution No....... Dated......)			
	General Reserve A/c	Dr.	1,20,000	
	Profit & Loss A/c	Dr.	30,000	
	To Capital Redemption Reserve A/c			1,50,000
	(Being the amount transferred to Capital Redemption Reserve A/c as per the requirement of the Act.)			
	Capital Redemption Reserve A/c	Dr.	1,20,000	
	To Bonus to Shareholders A/c			1,20,000
	(Being the amount appropriated for issue of bonus share in the ratio of 5:2 as per shareholders Resolution No...... dated...)			
	Bonus to Shareholders A/c	Dr.	1,20,000	
	To Equity Share Capital A/c			1,20,000
	(Being the utilisation of bonus dividend for issue of 12,000 equity shares of ₹ 10 each fully paid)			
	Profit & Loss A/c	Dr.	36,000	
	To Premium on Redemption of			36,000

...

	Preference Shares A/c (Being premium on redemption of preference shares adjusted against to Profit & Loss Account)			

Working Note:

(1) Partly paid-up preference shares cannot be redeemed.

(2) Amount to be Transferred to Capital Redemption Reserve Account

Face value of share to be redeemed	₹1,80,000
Less: Proceeds from fresh issue (excluding premium)	(₹ 30,000)
	₹1,50,000

(3) No bonus shares on 3,000 equity shares issued for redemption.

Answer 2

Bumbum Limited
Journal Entries

20X1		***Dr. (₹)***	***Cr. (₹)***
July 1	Equity Share Capital A/c (₹ 10 each) Dr.	3,00,000	
	To Equity share capital A/c (₹ 2 each)		3,00,000
	(Being equity share of ₹10 each splitted into 5 equity shares of ₹ 2 each) {1,50,000 X 2}		
July 10	Cash & Bank balance A/c Dr.	5,55,000	
	To Investment A/c		4,90,000
	To Profit & Loss A/c		65,000
	(Being investment sold out and profit on sale credited to Profit & Loss A/c)		
July 10	8% Redeemable preference share capital A/c Dr.	5,00,000	
	Premium on redemption of pref. share A/c Dr.	25,000	
	To Preference shareholders A/c		5,25,000
	(Being amount payable to preference share holders on redemption) (refer W.N.1)		
July 10	Preference shareholders A/c Dr.	5,25,000	
	To Cash & bank A/c		5,25,000
	(Being amount paid to preference shareholders)		

July 10	General reserve A/c Dr. To Capital redemption reserve A/c (Being amount equal to nominal value of preference shares transferred to Capital Redemption Reserve A/c on its redemption as per the law)	5,00,000	 5,00,000
Aug 1	9% Debentures A/c Dr. Interest on debentures A/c (2,50,000 x 9% x 4/12) Dr. To Debenture holders A/c (Being amount payable to debenture holders along with interest payable)	2,50,000 7,500	 2,57,500
Aug. 1	Debenture holders A/c Dr. To Cash & bank A/c (1,00,000 + 7,500) To Equity share capital A/c (15,000 X 2) To Securities premium A/c (15,000 x 8) (Being claims of debenture holders satisfied) (refer W.N.2)	2,57,500	 1,07,500 30,000 1,20,000
Sept. 5	Capital Redemption Reserve A/c Dr. To Bonus to shareholders A/c (Being balance in capital redemption reserve capitalized to issue bonus shares) (refer W.N.3)	1,10,000	 1,10,000
Sept. 12	Bonus to shareholders A/c Dr. To Equity share capital A/c (Being 55,000 fully paid equity shares of ₹ 2 each issued as bonus in ratio of 1 share for every 3 shares held)	1,10,000	 1,10,000
Sept. 30	General Reserve A/c Dr. To Premium on redemption of preference shares A/c (Being premium on preference shares adjusted from general reserve)	25,000	 25,000

Sept. 30	Profit & Loss A/c Dr.	7,500	
	To Interest on debentures A/c		7,500
	(Being interest on debentures transferred to Profit and Loss Account)		

Balance Sheet as at 30th September, 20X1

		Particulars	Notes	₹
		Equity and Liabilities		
1		**Shareholders' funds**		
	a	Share capital	1	4,40,000
	b	Reserves and Surplus	2	13,32,500
2		**Current liabilities**		
	a	Trade Payables		1,70,000
		Total		**19,42,500**
		Assets		
1		**Non-current assets**		
	a	Property, Plant and Equipment		
		Tangible assets		7,80,000
	b	Deferred tax asset		3,40,000
2		**Current assets**		
		Trade receivables		6,20,000
		Cash and bank balances (W.N.4)		2,02,500
		Total		**19,42,500**

Notes to accounts

		₹	₹
1	**Share Capital**		
	Authorized share capital		
	2,50,000 Equity shares of ₹ 2 each	5,00,000	
	10,000 Preference shares of ₹100 each	10,00,000	15,00,000
	Issued, subscribed and paid up		
	2,20,000 Equity shares of ₹ 2 each		4,40,000
	[(30,000 x 5) + 15,000 + 55,000]		

2	**Reserves and Surplus**		
	Securities Premium A/c		
	Balance as per balance sheet	6,00,000	
	Add: Premium on equity shares issued on conversion of debentures (15,000 x 8)	1,20,000	
	Balance		7,20,000
	Capital Redemption Reserve (5,00,000-1,10,000)		3,90,000
	General Reserve (6,50,000 – 5,00,000- 25,000)		1,25,000
	Profit & Loss A/c	40,000	
	Add: Profit on sale of investment	65,000	
	Less: Interest on debentures	(7,500)	97,500
	Total		**13,32,500**

Working Notes:

		₹
1.	**Redemption of preference share:**	
	5,000 Preference shares of ₹ 100 each	5,00,000
	Premium on redemption @ 5%	25,000
	Amount Payable	5,25,000
2.	**Redemption of Debentures**	
	2,500 Debentures of ₹100 each	2,50,000
	Less: Cash option exercised by 40% holders	(1,00,000)
	Conversion option exercised by remaining 60%	1,50,000
	Equity shares issued on conversion $= \frac{1,50,000}{10} =$ 15,000 shares	
3.	**Issue of Bonus Shares**	
	Existing equity shares after split (30,000 x 5)	1,50,000 shares
	Equity shares issued on conversion	15,000 shares
	Equity shares entitled for bonus	1,65,000 shares
	Bonus shares (1 share for every 3 shares held) to be	55,000 shares

issued	
4. **Cash and Bank Balance**	
Balance as per balance sheet	2,80,000
Add: Realization on sale of investment	5,55,000
	8,35,000
Less: Paid to preference share holders	(5,25,000)
Paid to Debentureholders (7,500 + 1,00,000)	(1,07,500)
Balance	2,02,500
5. Interest of ₹7,500 paid to debenture holders have been debited to Profit & Loss Account.	

Answer3

Journal Entries in the Books of Trinity Ltd.

		Dr.	Cr.
		₹	₹
General Reserve A/c	Dr.	10,000	
To Premium on Redemption of Preference shares			10,000
(Being amount of premium payable on redemption of preference shares)			
10% Redeemable Preference Capital	Dr.	1,00,000	
Premium on redemption of Preference Shares	Dr.	10,000	
To Preference Shareholders			1,10,000
(Being the amount payable to preference shareholders on redemption)			
General Reserve A/c	Dr.	1,00,000	
To Capital Redemption Reserve			1,00,000
(Being transfer to the latter account on redemption of shares)			
Bank A/c	Dr.	90,000	
Profit and Loss A/c	Dr.	10,000	
To Investments			1,00,000
(Being amount realised on sale of Investments and			

loss thereon adjusted)			
Preference shareholders A/c	Dr.	1,10,000	
To Bank			1,10,000
(Being payment made to preference shareholders)			
Capital Redemption Reserve A/c	Dr.	1,00,000	
To Bonus to Shareholders			1,00,000
(Amount adjusted for issuing bonus share in the ratio of 1 : 1)			
Bonus to Shareholders A/c	Dr.	1,00,000	
To Equity Share Capital			1,00,000
(Balance on former account transferred to latter)			