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Unit – 6

Leasing and Hire Purchasing

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Leasing

- A contractual arrangement in which owner of an asset (less the right to use the asset to another party (lessee) for an agre time for consideration in the form of periodic rentals.
- At the end of the lease the asset goes back to the lesso contract is renewed.

As per IAS -17 lease is " an agreement where by the lesso the lessee in return for rent the right to use an asset for an agre time."

Features

- Parties must be competent to contact
- No transfer of ownership to the lessee
- Goods are transferred for a specific purpose
- Lessee should return exactly the same goods
- Lease rentals are payable in monthly installments
- Equipment leases are for capital investment not exceeding R
- Equipment leasing covers a wide range of equipments suc machinery, vehicle, office equipment, computers, automobi

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Parties involved in Lease

Lessor

Owner or lender
Specialised leasing companies
Banks
Specialised financial institutions
One-off lessors
Manufacturer lessors

Lessee

User or renter or tenant
Corporate customers
PSUs
Consumers
Mid cap companies
Commercial vehicles
Earth-moving machinery customers
Govt departments

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Contents of Leasing agreement

- Particulars of the parties
- Description of the asset
- Effective date, Primary period and renewal
- Initial deposit, rental and payment terms
- Manufacturer's warranty
- Ownership
- Delivery and installation terms
- Repair and alteration
- Insurance
- Sub-lease
- Surrender
- Default
- Arbitration
- Taxes and govt dues
- Termination clause
- Restricted activity

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Steps in Leasing agreement

- Lessee has to decide about the type of asset required
- Lessee has to determine the manufacturer of the asse
- Lessee has to enter into a lease agreement with regar
  - irrevocability during basic lease period
  - amount and timing of rental payment
  - option of renewal/purchase at the end of the basic lease
  - responsibility to pay for repairs, taxes, insurance, expen
- After the agreement manufacturer has to supply the a
- After the asset is delivered and accepted by the lesse lessor has to make payment to the manufacturer.

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Types of Lease

- Operating or service lease
- Financial lease
- Sale and lease back
- Direct Lease
  - Bipartite lease
  - Tripartite lease
- Single investor lease
- Leveraged lease
- Domestic lease
- International lease
  - Import lease
  - Cross boarder lease

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Legal Frame work

- No separate statue regarding leasing
- Laws relating to bailment are applicable
- Provisions of the sections 150-168 of the Indian contra applicable
- Lessor has the duty to deliver the asset to the lessee
- Authorise the lessee to use the asset
- Leave the asset in the possession of the lessee
- Lessee has obligation to pay the lease rentals as specif lease agreement
- Lessee has the obligation to protect the lessors title to t
- Take reasonable care of the asset
- Return the leased asset on the expiry of the lease perio

Advantages and disadvantages of leasing – Presentation

Legislative framework relating to Depreciation and Presentation by Karon D'souza & Sharon D'souza

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Advantages of Leasing

To the Lessor

- Full security
- Tax benefit
- High Profitability
- Trading on Equity
- High Growth potential

To Lessee

- Financing of capital goods
- Additional source of finance
- Less costly
- Ownership preserved
- Avoids conditionality
- Flexibility in structuring of rentals
- Simplicity
- Tax Benefits
- Obsolescence risk
- Other benefits

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Problems in Leasing

- Resource constraint
- Risk of obsolescence
- Non availability of sales tax consideration
- Cut-throat competition
- Lack of qualified personnel
- Delay in rental payment
- Attitude of government

Factors influencing buy or borrow decision

- Capital and cost of borrowing
- Availability of freehold or leasehold interest
- Interest on capital employed
- To show increase in capital
- Taxation
- Obsolescence risk
- Future returns
- Depreciable asset
- Non-depreciable asset
- Other factors
    - Operating factors
    - Legal factors
    - Financial factors

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Hire Purchase

A contract of hire between a vendor and a purchaser, with an option to
the asset at the end of fixed term of hire; by the purchaser provided he
rentals regularly.

Terms: Payment will be made in instalments, Possession of the
transferred to the buyer immediately, ownership remains with the ven
payment of last instalment, Seller can repossess the goods if the buyer
the instalment, each instalment is treated as hire charges till the last in
paid.

Features

- Transfer of asset from vendor to hire purchaser immediately at the be
  the contract
- Purchaser pays agreed rentals at agreed intervals to the vendor
- Vendor continues to own the asset till the last instalment is paid by th
  purchaser.
- Hire purchaser may make a down payment upon signing the agreeme
- If the purchaser defaults a payment, even the last one, the vendor has
  take back the asset without having to pay any compensation.

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Contents

- **Nature of agreement:** stating the nature, term and commenceme agreement

- **Delivery/handing over of assets:** place, time of delivery of asset will pay the delivery charges, installation responsibilities etc

- **Location:** place where the asset will be kept during the period of agreement.

- **Inspection:** the hirer has examined the equipment and is satisfied

- **Insurance:** that the hirer will pay for insurance and hand over the the owner.

- **Alterations:** the hirer is not authorised to make any alterations/m to the machinery without prior consent of the owner.

- **Repairs:** the hirer will pay for all repairs required during the cont

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- **Termination:** what conduct of the hirer would lead to a term the agreement?

- **Risk:** risk of damage and loss to be borne by the hirer

- **Indemnity clause:** clause which necessitates the hirer to ma the loss/damage incurred by the lender on the asset

- **Stamp duty**: the hirer will pay the stamp duty

- **Registration and fees:** the hirer is responsible to follow all la necessary registrations and pay the fees

- **Schedule:** schedule of equipment, hire charges etc forming agreement

- **Guarantee:** usually the agreement is accompanied by a bank or a promissory note given by the hirer for the full amount o including interest and finance charges.

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Banks and Hire Purchase

- Banks extend consumer loans and instalment credit to buyers and sel
- Not been able to extend credit to hire-purchasers directly. Hence p credit to owners or refinance financing companies or associate manufacturers against hire-purchase contracts
- In case of commercial vehicles banks extend OD or cash cre hypothecation of first charge of vehicles covered under hi agreements. Also, secured by indemnity insurance policies in favour
- Banks maintain a margin of 25%-30% on instalments due by hirers to
- They usually do not accept hire agreements of amounts exceeding Rs

IDBI

- IDBI indirectly participates in hire-purchase business by way of usance bills/promissory notes arising out of sale of indigenous ma deferred payment basis.
- Under the IDBI scheme bills/pro notes should be drawn in manufacturer who can discount them at banks and other financial who can further re-discount them at IDBI.
- Deferred payment period is generally up to 5 years or 7 years under cases.
- Manufacturers of cotton and sugar machinery, machine tools machinery, oil solvent extraction plants, and some other agro indu use of this facility.

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Difference between Leasing and Hire purchase

- Down payment
- Reporting
- Maintenance of Assets
- Sustainability
- Nature of Assets
- Receipts
- Income

Difference between Installment sale and Leasing

- Nature
- Ownership of the assets
- Tax Benefits
- Appearance in the Balance sheet
- Overall cost of the Asset
- Duration
- Maintenance support of the Asset
- Reduced initial cash outlay

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Comparison of Hire purchase with Credit Sale

- Governing Act
- Ownership
- Payment
- Interest
- Repossession
- Termination of the contract
- Risk of loss
- Sales tax

Link for you tube video

https://www.youtube.com/watch?v=PD8XV8Pvy0E

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