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## **UNIT-1 LEASE FINANCING AND HIRE PURCHASE FINANCING FOR ENTREPRENEURS**

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### **1.0 LEARNING OUTCOME:**

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After completing this module the students will be able to:

- Understand the Meaning of Lease Financing
- To have the knowledge of Types of Leasing
- Describe the Advantages and Disadvantages of Leasing
- Understand the Role of Hire Purchase Financing for the Entrepreneurs
- Know about the statutory Limit in Hire Purchase Charges
- Understand the rules of Termination of the Agreement

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### **1.1 LEASE FINANCING**

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Lease contracts have long been an important alternative to direct ownership of an asset. One may opt to take a building on a lease or rent a car, rather than owning them outright. Thus assets can easily be acquired with lease finance and while the owner (Lessor) enjoying the tax benefits which are passed on to the tenant (Lessee) in the form of lower rent. Lease companies play a role of financial intermediaries who encourage investments by making funds available in an easy way. Leasing is now being considered as another alternative to financial instrument. Of late there has been a remarkable growth in the leasing business. The rapid growth of leasing business has resulted in competition which in turn has reduced the lease rentals significantly. In

fact leasing business has contributed economic growth and financial efficiency in a big way. In the changing economic and financial environment with global competitors, the lease financing has assumed a significant role as an alternative source of financing or a close substitute for debt financing.

### **1.1.1 Meaning of Lease**

A lease is contract between a lessor who is the owner of the asset and a lessee who is a user of the asset whereby the lessor (owner) gives the right to use the asset to the lessee (user) over an agreed period of time for a consideration called the lease rental either on monthly, quarterly, half-yearly or yearly basis. And some cases it may be weekly, daily or hourly basis.

According to AS-19, “A lease is an agreement whereby the lessor conveys (transfers) to the lessee the right to use an asset for an agreed period of time in consideration for a payment or series of payments.”

The lessor as a legal owner is entitled to claim depreciation on the leased asset. The lease contract may be a short term lease contract which provides recovery of the cost of the asset and profit through lease rentals during a period of less than five years whereas under long term lease contact (called perpetual lease) the lessee is generally given an option to buy or renew the lease on a nominal lease rentals.

### **1.1.2 Classification of Lease**

According to AS-19 the lease may be of two types:

- Operating Lease
- Financial Lease

**Operating Lease:** A lease is classified as an operating lease if the lessor does not transfer all risks and rewards incidental to ownership of the asset. The lessee acquires rights to use the assets on a period to period basis. In other words, operating lease covers the period which is much shorter than the economic life of the asset. The lessor may lease the asset to different lessees one after another throughout its useful life. The rent payable by any one lessee during the lease period is not sufficient to cover cost of the asset fully. At the expiry of term of lease, the asset reverts back to the lessor. Hence, such leases are called short term leases. An operating lease is also termed as “Service Lease” because lessor also provides necessary services relating to insurance, repairs and maintenance of the leased asset. Therefore, the lease rentals of an operating lease also include for such services in respect of leased asset.

The operating lease is generally cancelled by either party. Because of provisions of services along with the risk of obsolescence, the operating lease is more expensive as compared to other form of lease as the lessee has to compensate to the lessor for both- the instant services and the risk of obsolescence.

***Salient features of an operating lease are:-***

1. It is a short term and cancellable lease.
2. The period covered by any one lease agreement is much shorter than the economic life of the leased asset. The lease period may vary from an hour to five years.
3. There are series of lease agreements one after another throughout the useful life of the leased asset.
4. Operating lease usually contains a maintenance clause.
5. Convenience and prompt service is the very basis of operating lease.
6. Rentals are usually higher as compared to other lease.

***Some examples of operating lease are:***

1. Renting a car, truck or a hotel room including the provision for petrol, diesel, driver or services of waiters in case of hotel rooms.
2. Hiring of a marriage hall including provision for food, drinks and bearers.
3. Chartering a plane or ship including provision of crew and other staff.
4. Hiring computers and office equipments with operators including provision for repairs and maintenance.
5. Hiring crane services with operators.

**Finance Lease:** According to AS-19, a finance lease is a lease that transfers substantially all the risks and wards incidental to ownership of an asset. It usually covers the full useful life of the asset or a period which is closer to its economic life. Such lease are termed as long-term or non cancellable lease contract during which the lessor receives rental that covers not only the cost of the asset but a reasonable return on the funds invested to acquire the asset. The repairs and maintenance of the leased asset is undertaken by the lessee. Hence, such leases are also known as capital or full pay out leases. At the end of lease term, the asset may be returned to owner (lessor) or handled as per lease terms.

***Salient features of finance lease are:***

1. The lessor transfers ownership of the asset to the lessee by the end of lease term.
2. The lessee has the option to purchase the asset at a price which is expected to be

sufficiently lower than the fair value of the asset.

3. The lease term is for the major part of the economic life of the asset even if the asset is not transferred.
4. The leased asset is of a specialized nature such that only the lessee can use it without major modification being made.
5. In the event of cancellation of lease by lessee, lessor's losses due to cancellation are borne by the lessee.
6. Gains or losses from the fluctuation in the fair value of the residual value fall on to the lessee.
7. The lessee can continue the lease for a second term at a rent which is substantially lower than the market rent.
8. The risk of obsolescence, repairs, maintenance and insurance rests with the lessee.

***Examples of finance lease are:***

The fixed assets such as land and building, plant & machinery, ships & aircrafts which are usually taken for use for their major or whole economic useful life or on perpetual basis.

### **1.1.3 Advantages of Leasing**

The following are the main advantages of leasing for the entrepreneurs:

- **No Sunk Cost:** Lease finance makes huge sum available for land and building, plant & machinery and other fixed assets thus averting a large sum to be blocked in fixed assets. One may start business with necessary amount of working capital. Thus it serves as an additional source of long term finance for the lessees.
- **No Cost of Raising Capital:** The cost of raising long term finances through issue of shares & debentures is totally avoided. The underwriter's commission, the cost of issue of prospectus and other incidental charges has not to be incurred.
- **Simplicity, Convenience and Flexibility:** Lease finance arrangements are easy and simple to make and flexible & convenient to operate as far as compliance of formalities are concerned. If an asset is required for short period, buying an asset and resale thereof may be time consuming, inconvenient and costly affair.
- **No Obsolescence Risk:** The lessee is always free to replace the outdated asset with new one whenever there is a technological change is brought about. Computers are usually subject to rapid and unpredictable changes, hence lessee will always prefer for short-term cancellable lease.

- **Tax Shield:** The lease rentals can be adjusted so as to provide maximum tax benefits. The lease rentals may be enhanced to avail tax concessions by lowering the taxable income and on the contrary, lease rentals may be lowered to pass on the tax benefits for future if current income is already low.
- **Maintenance and Specialized Service:** The lessor is always better equipped to provide best possible maintenance and specialized services at low cost which cannot be provided by any other agency.

#### 1.1.4 Limitations of Lease Financing:

The following are the limitations of lease financing for the entrepreneurs:

- **Restricted Use:** An asset taken on lease has to be used in accordance with terms of agreement. Alteration or modification to suit the lessee's requirements cannot be made. Further, any other condition, such as of compulsory insurance, may be of the terms of the lease contract.
- **Default:** In case of default, the lessee usually loses the right to use asset in case of finance lease, whereas he is required to pay damages in case of an operating lease.

Despite these limitations, a large number of companies are being created with the object of exploiting tax shield and other benefits. Such companies do boost investment and productivity for leasing being an alternative to financing. Since lease rentals are similar to payments of interest on debt, leasing in essence is an alternative borrowing. Thus lease essentially involves a choice between debt financing and lease financing. Leasing companies play a role of financial intermediaries by encouraging investment by making funds available for leasing business purposes in a simplest way to achieve financial efficiency and to accelerate economic growth.

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## 1.2 HIRE PURCHASE FINANCING FOR THE ENTREPRENEURS

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Hire Purchase is a system of selling goods whereby risk involved in transaction is kept to the minimum. It has the advantage of credit sale and ensures regular and periodical recovery of money through installments while keeping the title of goods safe.

According to Pickles, "Hire Purchase is a system under which the property is acquired by payments made in installments, during the period of which the title in the property remains with the Hire Vendor. The payments prior to the final are regarded as being purely in respect of hire and title of the property does not pass to the hire

purchaser until such final payment or some other consideration provided for in the contract has been fulfilled.”

**Hire Purchase Act 1972 section 2 (c) states:**

“Hire Purchase Agreement means an agreement under which goods are let on hire and the hirer has an option to purchase them in accordance with the terms of agreement.”

It includes an agreement under which:

- Possession of goods is given by the owner to a person on a condition that such person will pay the agreed amount in periodical installments,
- The property in goods is to pass such person on the payment of the last of such installments and
- Such person has the right to terminate the agreement at any time before the property in goods so passes.

Section 4 of Hire Purchase Act 1972 states that Hire Purchase Agreement contains:

- The hire purchase price of goods to which agreement relates.
- The cash price of goods.
- The date on which the agreement shall be deemed to have commenced.
- Number of installments by which the hire purchase price is to be paid, the amount of each of these installments, and the date, upon which it is payable and the person to whom and the place where it is payable.
- The goods to which agreement relates.
- Where any part of hire purchase price is to be paid otherwise than by cash or cheque, the hire purchase agreement shall contain a description of that part of price.

Thus, hire purchase transactions involves an agreement between hire vendor and hire purchaser whereby hire vendor gives the delivery of goods to the hire purchaser on signing of an agreement and after down payment, if any. The hire purchaser undertakes to pay the cash price/balance in agreed number of installments together with interest. The property in goods shall be transferred from hire vendor to the hire purchaser only when the last installment is paid. This is due to the fact that every installment is treated as hire and consequently, hire vendor has a right to repossess the goods on the failure of hire purchaser to pay any installment.

**1.2.1 Statutory Limit on Hire Purchase Charges**

The difference between hire purchase price and the cash price represents hire purchase charges. It is, in fact, the total amount of interest to be paid by hire

purchaser to hire vendor. To avoid higher rate of interest charged by hire vendor section 7 puts the maximum limit of 30 per cent of such installment or the charges as may be ascertained with the help of following formula:

$$SC = \frac{CI \times R \times T}{100}$$

Where,

SC = Stands for statutory charges

CI = The amount of cash price installment

R = Rate as determined by Central Govt. in consultation with RBI

T = Time Period

### **1.2.2 Right of Hire Purchaser to Purchase Goods Taken on Hire**

In case a hire purchaser intends to make outright purchase of the goods taken on hire after the agreement has been signed and delivery taken he can do so by giving 14 days prior notice to the hire vendor as required under the Hire Purchase Act u/s 7. He shall be required to pay the amount due to hire vendor after deducting the rebate under the act. The rebate can be worked out as under:

$$\text{Rebate} = \frac{2(\text{Hire Purchase Charges} \times \text{No. of Installments due})}{3(\text{Total No. of Installments})}$$

### **1.2.3 Hire-Purchase Installment Sale and Lease**

Under Hire-Purchase system the property in goods (ownership) is transferred from hire vendor to hire-purchaser only when last installment is paid. Every installment paid by the hire purchaser is treated as hire and the hire vendor has the right to repossess goods in case of any default. The hire-purchaser cannot temper or transfer the goods until the payment of final installment. However, he has right to terminate the agreement at any time before the transfer of ownership. The hire-purchaser is entitled to claim depreciation and how t he hired asset in the Balance Sheet alongwith the amount due to hire vendor. The interest is charged to P & L A/c.

Whereas, an installment is a credit sale and the property in goods is transferred immediately on the signing of agreement. Every installment paid is treated as part of price. The vendor has no right to repossess the goods, but can sue for the amount due. The buyer has the right to sell, transfer or dispose off the goods at any time but cannot terminate the agreement and return the goods to the vendor. The balance due is shown as secured loan on which interest is payable.

On the other hand, under lease system the entire rental is charged to P & L A/c. The lessee (user) is not treated as owner and as such cannot claim depreciation and is not allowed to show the asset in the balance sheet.

#### **1.2.4 Termination of Agreement**

The Hire Purchase Act gives the hire purchaser the right to terminate agreement at any time by giving 14 days notice to the hire vendor. However, he shall be required to pay a sum as stipulated in the agreement or as per the provisions of the Act, whichever is less. The Hire Purchase Act provides that:

- Where total sum paid and due in respect of hire purchase price immediately before termination exceeds one half of the hire purchase price the hire purchaser is not required to pay any amount on termination.
- Where total sum paid and due in respect of hire purchase price immediately before termination does not exceed half of the hire purchase price, the hire purchaser shall be liable to pay the difference between half of the hire purchase price and amount already paid or the amount so stipulated in the agreement whichever is less.

#### **1.2.5 Explanation of Certain Important Terms**

Some of the importance terms are discussed as follows:

1. **Cash Price:** It is the actual price of goods charged under normal cash sale or the amount paid for outright purchase.
2. **Hire Purchase Price:** The total amount payable under the terms of hire purchase agreement in the form of down payment and installments. It consists of cash price plus interest.
3. **Down Payment:** It is the amount paid by hire purchaser to hire vendor at the time of signing of agreement or at the time of delivery of good.
4. **Hire Purchaser:** Also known as hirer, the one who purchases goods under hire purchase agreement.
5. **Hire Vendor:** The person who sells goods under hire purchase agreement.

6. **Hire:** Each installment paid by hire purchaser is treated as hire. It includes part of cash price (principal) and interest rate.
7. **Hire Purchase Charges:** The difference between hire purchase price and cash price.
8. **Net Hire Purchase Charges:** It is the difference between net hire purchase price and cash price.
9. **Net Cash Price:** It is the total cash price less deposit, if any.
10. **Net Hire Purchase Price:** The total amount of hire purchase price s reduced by:
  - Delivery Expenses
  - Insurance Charges, if any, and
  - Registration Fees of Agreement etc.

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### 1.3 SUMMARY

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Although leasing business has been growing very fast, recently there has been a shift to hire purchase as a popular means of financing assets to the entrepreneurs. Many entrepreneurs prefer hire purchase because of flexibility in terminating a hire purchase contract as compared to a leasing contract. In this module lease financing has been discussed in detail. This shows the clear difference between the lease financing and hire purchase financing with particular examples in each case. For the growth and expansion of the business activities, the entrepreneurs try to raise the finance from these two sources.





























**Solution**

Let us first find out all the information required.

- 1) Date of Purchase – January 1, 2016; No down payment.
- 2) Date at which the instalments become due – December 31, 2016, 2017 and 2018.
- 3) Date of closure of accounts – December 31.
- 4) Cash Price – Rs. 6,000.
- 5) Hire Purchase Price – Rs. 2,412 x 3 = Rs. 7,236.
- 6) Number, amount and mode of each instalment – 3 instalments of Rs. 2,412 each payable annually.
- 7) Rate of Interest – 10% p.a.
- 8) Rate of Depreciation – 20% p.a.
- 9) Method of Depreciation – Straight Line.

**Journal Entries in the Books of ABC Ltd**

Date	Particulars	Amount (Dr.)	Amount (Cr.)
2016		Rs.	Rs.
Jan. 1	Machinery A/c                      Dr. To XYZ Ltd. (Being a machine purchased on hire purchase)	6,000	6,000
Dec.31	Interest A/c                      Dr. To XYZ Ltd. (Being the charge of interest @ 10% on Rs. 6,000)	600	600
Dec.31	Depreciation A/c                  Dr. To Machinery A/c (Being the charge of depreciation)	1,200	1,200
Dec.31	XYZ Ltd. A/c                      Dr. To Bank A/c (Being the payment of annual instalment)	2,412	2,412
Dec.31	Profit & Loss A/c                  Dr. To Interest A/c To Depreciation A/c (Being the annual charges transferred to Profit & Loss A/c)	1,800	600 1,200
2017			
Dec.31	Interest A/c                      Dr. To XYZ Ltd. (Being the charge of interest @ 10% on Rs. 4,188)	418	418

**Hire Purchase and Inland Branches**

Dec.31	Depreciation A/c	Dr.	1,200	
	To Machinery A/c			1,200
	(Being the annual charge of depreciation)			
Dec.31	XYZLtd. A/c	Dr.	2,412	
	To Bank A/c			2,412
	(Being the payment of annual instalment)			
Dec.31	Profit & Loss A/c	Dr.	1,618	
	To Interest A/c			418
	To Depreciation A/c			1,200
	(Being the transfer of annual charges to Profit & Loss A/c)			
2018				
Dec.31	Interest A/c	Dr.	218	
	To XYZ Ltd.			218
	(Being the charge of interest @ 10% on Rs. 2,194)			
Dec.31	Depreciation A/c	Dr.	1,200	
	To Machinery A/c			1,200
	(Being the annual charge of depreciation)			
Dec.31	XYZ Ltd. A/c	Dr.	2,412	
	To Bank A/c			2,412
	(Being the 3rd and final instalment paid)			
Dec.31	Profit & Loss A/c	Dr.	1,418	
	To Interest A/c			218
	To Depreciation A/c			1,200
	(Being the transfer of annual charges to Profit & Loss A/c)			

**Ledger Accounts in the Books of ABC Ltd  
Machinery Account**

Dr.					Cr.
2016		Rs.	2016		Rs.
Jan. 1	To XYZ Ltd	6,000	Dec. 31	By Depreciation A/c	1,200
			Dec. 31	By Balance c/d	4,800
		6,000			6,000
2017			2017		
Jan. 1	To Balance b/d	4,800	Dec. 31	By Depreciation A/c	1,200
			Dec. 31	By Balance c/d	3,600
		4,800			4,800
2018			2018		
Jan. 1	To Balance b/d	3,600	Dec. 31	By Depreciation A/c	1,200
			Dec. 31	By Balance c/d	2,400
		3,600			3,600

**XYZ LTD (Hire Vendor) Account**

**Hire Purchase Accounts-I**

Dr.					Cr.
2016		Rs.	2016		Rs.
Dec.31	To Bank A/c	2,412	Jan. 1	By Machinery A/c	6,000
Dec.31	To Balance c/d	4,188	Dec. 31	By Interest A/c	600
		6,600			6,600
2017			2017		
Dec.31	To Bank A/c	2,412	Jan. 1	By Balance b/d	4,188
Dec.31	To Balance c/d	2,194	Dec. 31	By Interest A/c	418
		4,606			4,606
2018			2018		
Dec.31	To Bank A/c	2,412	Jan. 1	By Balance b/d	2,194
		2,412	Dec. 31	By Interest A/c	218
					2,412

**Working Notes :**

	Rs.
Cash Price	6,000
Add : Interest on Ist Instalment $(\frac{10}{100} \times 6,000)$	600
	6,600
Less : Ist Instalment	2,412
Amount outstanding at the time of 2 <sup>nd</sup> Instalment	4,188
Add : Interest on 2 <sup>nd</sup> Instalment $(\frac{10}{100} \times 4,188)$	418
	4,606
Less : 2 <sup>nd</sup> Instalment	2,412
Amount outstanding at the time of 3 <sup>rd</sup> instalment	2,194
Add : Interest on 3 <sup>rd</sup> Instalment	218
	2,412

**2.5.2 When the Asset is Recorded at Cash Price Actually Paid**

You know that in case of hire purchase, the ownership of the goods passes to the hire purchaser after the last instalment has been paid. Since the goods do not become the property of the purchaser, he does not have any right to debit the asset at its full price. Hence, no entry is passed when the asset is purchased unless it involves down payment. The entries are passed as and when the instalments become due and the amount is paid towards the price of the article. The journal entries are as follows :

1. **When the asset is purchased**  
No entry
2. **When the down payments is made**  
Asset A/c                      Dr.  
                                            To Bank A/c
3. **When the instalment becomes due**  
Asset A/c                      Dr. (cash price part of instalment)  
Interest A/c                    Dr. (interest on instalment)  
                                            To Hire Vendor
4. **When instalment is paid**  
Hire Vendor                    Dr.  
                                            To Bank A/c
5. **When depreciation is charged**  
Depreciation A/c              Dr.  
                                            To Asset A/c
6. **When interest and depreciation accounts are closed by transfer to Profit & Loss A/c**  
Profit & Loss A/c              Dr.  
                                            To Interest A/c  
                                            To Depreciation A/c

It should be noted that though the asset account is debited with the amount of the cash price paid (not full cash price), the depreciation is charged on the full cash price. The Balance Sheet will reflect the amount of cash price debited to the asset account minus depreciation charged.

Look at the illustration 6 and see how accounting records are maintained in case the asset is recorded at cash price actually paid.

**Illustration 6**

Solve illustration 6 by debiting the asset account at cash price actually paid.

**Solution:**

**Journal Entries in the Books of ABC Ltd.**

Date	Particulars	Amount (Dr.) Rs.	Amount (Cr.) Rs.
2016 Dec. 31	Machinery A/c                      Dr. Interest A/c                              Dr. To XYZ Ltd. (Being first instalment due)	1,812 600	2,412
Dec. 31	XYZ Ltd Dr. To Bank A/c (Being first instalment paid)	2,412	2,412
Dec. 31	Depreciation A/c                      Dr. To Asset A/c (Being annual depreciation charged)	1,200	1,200

**Hire Purchase Accounts-I**

Dec. 31	Profit & Loss A/c To Depreciation A/c To Interest A/c (Being annual charges transferred to Profit & Loss A/c)	Dr.	1,800		
				1,200	
				600	
<b>2017</b>					
Dec. 31	Machinery A/c Interest A/c To XYZ Ltd. (Being third instalment due)	Dr. Dr.	1,994 418		
				2,412	
Dec. 31	XYZ Ltd To Bank A/c (Being third instalment paid)	Dr.	2,412		2,412
Dec. 31	Depreciation A/c To Asset A/c (Being annual depreciation charged)	Dr.	1,200		1,200
Dec. 31	Profit & Loss A/c To Depreciation A/c To Interest A/c (Being annual charges transferred to Profit & Loss A/c)	Dr.	1,618		1,200 418
<b>2018</b>					
Dec. 31	Machinery A/c Interest A/c To XYZ Ltd. (Being third instalment due)	Dr. Dr.	2,194 218		2,412
Dec. 31	XYZ Ltd To Bank A/c (Being third instalment paid)	Dr.	2,412		2,412
Dec. 31	Depreciation A/c To Asset A/c (Being annual depreciation charged)	Dr.	1,200		1,200
Dec. 31	Profit & Loss A/c To Depreciation A/c To Interest A/c (Being annual charges transferred to Profit & Loss A/c)	Dr.	1,418		1,200 218

**Note:** Depreciation has been charged on straight line method @20% p.a. at the full cash price of Rs. 6,000.

## 2.6 ACCOUNTING RECORDS IN THE BOOKS OF VENDOR

So far as the vendor is concerned, a hire purchase sale is just like an ordinary sale with the exception that payment is deferred over a period of time for which the vendor charged interest. He debits the Hire Purchaser's A/c with full cash price and credit is given to Sales A/c. The interest amount is debited to Hire Purchaser's A/c as and when the instalments become due. Instalment amounts received are credited to the Hire Purchaser's A/c and debited to Bank A/c.

The journal entries passed are as follows:

- 1 **On sale of goods under hire purchase**  

Hire Purchaser A/c	Dr	
To Sales A/c		(with full cash price)
  
- 2 **On receiving cash price down payment**  

Bank A/c	Dr	
To Hire Purchaser A/c		
  
- 3 **On instalment becoming due**  

Hire purchaser A/c	Dr.	
To Interest A/c		
  
- 4 **On getting payment on the due instalment**  

Bank A/c	Dr.	
To Hire Purchaser A/c		

With the help of above entries, you can easily prepare the Hire Purchaser's A/c and Interest A/c. Look at illustration 7 and see how accounting records are maintained in the books of the vendor.

### Illustration

On January 1, 2017, IFB Ltd. acquired machinery from JK Ltd. for Rs. 1,886 (cash price) under a hire purchase agreement where Rs. 400 was the initial payment and two instalments of Rs. 800 each would be paid. Interest @ 6% p.a. would be charged. Prepare the ledger accounts in the books of J.K. Ltd., assuming rate of depreciation @ 10% (straight line).

**Solution:**

### In the books of JK. Ltd. IFB LTD.

Dr.					Cr.
2017		Rs.	2017		Rs.
Jan. 1	To Sales A/c 1	1,886	Jan. 1	By Bank A/c	400
Dec. 31	To Interest A/c	89	Dec. 31	By Bank A/c (1st Inst.)	800
			Dec. 31	By Balance c/d	775
		1,975			1,975
2018			2018		
Jan. 1	To Balance b/d	775	Dec. 31	By Bank A/c (2nd Inst.)	800
Dec. 31	To Interest A/c	25			
		800			800

**Interest Account**

**Hire Purchase Accounts-I**

2017		Rs.	2017		Rs.
Dec. 31	To Profit & Loss A/c	89	Dec. 31	By IFB Ltd.	89
		89			89
2018			2018		
Dec. 31	To Profit & Loss A/c	25	Dec. 31	By IFB Ltd	25
		25			25

**Working Note**

Statement having calculation of hire purchases interest and the amount of principal in each instalment.

	Rs.	Interest Rs.	Cash Price Rs.
Cash Price	1,886	—	400
Less: Down Payment	400		
	1,486		
Add: Interest on 1st instalment to be paid on Dec. 31, 2017 @ 6%	89		
	1,575		
Less : 1st Instalment on Dec. 31, 2017	800	89	711
	775		
Add: Interest on 2nd instalment @ 6%	25		
	800		
Less: 2nd Instalment on Dec. 31, 2018	800	25	775

**Check Your Progress C**

1. Enlist the information required before solving the hire purchase problem.

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2. State whether following statements are **True** or **False**.

- i) When the asset is recorded at full cash price, the hire purchase becomes a method of financing the fixed asset.
- ii) When the asset is recorded at the price actually paid, the Asset A/c is debited and the Hire Vendor's A/c is credited with full cash price.
- iii) The Hire Vendor debits the hire purchaser's A/c and credits the sales A/c on sale of goods with cash price.



















































































































































































