

Hire Purchase System

To facilitate the buyers to purchase articles of larger value many businessmen introduce the scheme of purchasing their products on installment basis. Under this scheme, goods are delivered to the purchaser immediately on signing the contract and he is called upon to pay the purchase price in easy periodic (weekly, monthly, quarterly, half – yearly or annual installments).

Features

Hire purchase system is a special system of credit purchase and sale of goods. Under this system a written agreement is entered between buyer (called as hire – purchaser) and the seller (called as hire - vendor) for the purchase and sale of certain goods (necessarily durable goods) whereby goods are delivered to the hire – purchaser immediately on his signing the agreement on the condition that he will pay the purchase price by means of specified periodical installments. According to J.R. Batliboi, **“Under this system, goods are delivered to a person who agrees to pay the owner by equal periodical installment, such installments are treated as the hire of those goods until a certain fixed amount has been paid, when those goods become the property of hirer.”**

The main feature of this system is that though the purchaser takes delivery of the goods immediately on signing the agreement and acquires right to use the goods but he acquires the title or ownership in the property only when all the installments have been paid. Thus, till the last installment is paid, the title in the goods still remains with the hire vendor. The effect of the arrangement is that in the event of default by the hire purchaser in the payment of any installment, the vendor can take back the goods into his possession. The hire purchaser has a right to terminate the agreement at any time before the final installment is paid but he loses his claim on the amount of installment already paid. In fact till the last installment is paid the installments paid by the hire purchaser to the vendor are treated as hire charge. This is why this system of payment is called as hire purchase system. Here, it is to be remembered that after the return of goods by the hire purchaser, he will not be liable to pay the installments falling due in future.

Characteristics of Hire Purchase System

- 1- Credit Sale of Goods – The sale of goods is on credit.
- 2- Payment in installments – Some amount is usually paid on signing the agreement and the balance is paid in periodic installments.
- 3- Total payments being more than cash price – the Total sum payable by the purchaser known as hire purchase price is always more than cash price (I.E. the amount for which the article can be purchased on full payment) of the goods, the excess is the interest for deferred payment and hire purchase charge.
- 4- Possession of Goods – The hire purchaser acquires the right to use the goods immediately on signing the hire purchase agreement.
- 5- Right to use the Goods – The Purchaser acquire to right to use the goods immediately after taking them in his possession.
- 6- Title of Goods – The Title (I.E. ownership) of the goods remains with the vendor till the last installment is received from the purchaser.

Advantage to the Purchaser

- (I) A person of limited financial resources can purchase costly articles.
- (II) Due to pressure of periodic payment of installment he is bound to check his extravagances and to be economic.
- (III) Due to payment being made in installments payment of purchase price of the goods becomes easier.
- (IV) If the vendor has given guarantee for the free repair and maintenance of the goods, he can get his article easily repaired during guaranty period because the vendor has to realize from him his payment.

Difference between Hire Purchase and credit sales

1- **Nature** – Hire Purchase is a contract of hiring coupled with a option to purchase whereas in the contract of credit sale there is no element of hire.

2- **Right of Ownership**- Under hire purchase the purchaser acquires ownership right over the goods after payment of final installment whereas in credit sales ownership right is transferred to the purchaser immediately on getting possession of the goods.

3- **Right of Repossession**- In case of hire purchase, the vendor can be repossess the goods on default by the purchaser in payment of any installment whereas in case of credit sales, the vendor can only sue for the recovery of unpaid installment.

4- **Method of Payment**- In hire purchase system, the purchase price is paid in installments whereas in credit sale, the sum due is usually paid in one lump sum.

5- **Time of Payment** - Under hire purchase, the payment is made at specified intervals whereas in credit sales payment can be made at any time.

Journal Entries

Sr. No.	Transaction	First Method	Second Method
1.	On signing the agreement	No entry	Asset a/c Dr. To Vendors a/c (with Cash price of the asset)
2.	On cash down payment	Asset a/c Dr. To Bank / Cash a/c (with cash paid on delivery)	Vendors a/c Dr. To Bank/Cash a/c (with cash paid on delivery)
3.	On first Installment becoming due	Asset a/c Dr. (with Cash price Portion) Interest a/c Dr. (with Interest Portion) To Vendors a/c (with amount of installment)	Interest a/c Dr. To Vendors a/c (with Interest Portion of Installment)
4.	On payment of the first Installment	Vendors a/c Dr. To bank/ cash a/c (with the amount of installment)	Vendors a/c Dr. To bank/ cash a/c (with the amount of installment)
5.	For depreciation charge	Depreciation a/c Dr. To asset a/c	Depreciation a/c Dr. To asset a/c