



Pros and Cons of Asset Finance

(Principally for the business user)

An asset finance loan can be seen as an alternative to traditional bank lending and has a number of advantages over a bank loan or an overdraft.

There are essentially two forms of asset finance, either Lease (effectively renting or hiring) or Purchase, which allow the business to take advantage of the various 'Capital Allowances' relating to Use of the asset (Lease) or Ownership of the asset (Purchase). An accountant would be best placed to advise which Allowances are available to your business.

Lease Option

Where use, not ownership is important, the user (borrower) makes regular fixed payments (typically monthly) to the lender (who owns the asset) to effectively hire the asset for a pre determined period, normally between 2 & 5 yrs.

At the end of the agreed period the user has a number of options, depending on the type of lease. They can either;

- return the asset and (subject to any conditions) walk away with nothing more to pay, for example Contract Hire
- Sell (with conditions) the asset on behalf of the lender (owner) and receive a proportion of the sales proceeds by way of a refund of rentals, for example Flexi Lease.
- Pay a small 'peppercorn' rent for a set period, say 12 months, to extend the spirit of the lease and continue using the asset.
- A 'Balloon' or 'Final Rental' may be payable at the end of the lease, the effect of this is to reduce the amount paid monthly

VAT is always payable on lease, rent or hiring agreement payments and so leasing is particularly (but not exclusively) appropriate to VAT registered businesses, which can often reclaim the full VAT Cost

Purchase Option

If eventual ownership is important then a form of Hire Purchase would be appropriate. Again, a regular fixed monthly payment is paid by the user to the lender, who retains title (ownership) of the goods until the payments (including any 'Balloon' payment) are all complete. At the end of the term the user has a number of options, depending on the type of Hire Purchase

- Keep the asset and use it in the business or personally as desired
- Sell the asset with no restrictions

Unlike a lease, no VAT is due on the regular payments under a purchase option.

Summary

It is important to note that asset finance is every bit as flexible as a 'traditional' bank loan. Variable rate agreements can be found (though of course less desirable when rates are likely to rise). Virtually any asset can be financed and because in most cases the asset has a strong value, against the amount of the loan, no further security is required from the borrower, though Personal/Directors Guarantees are sometimes a condition depending on the financial strength of the borrower.

Last year, £20 billion worth of asset finance loans were provided to fund everything from vehicles to computer equipment and this form of finance is expected to grow this year, reflecting its suitability to businesses of all sizes.

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