

[How Contract Hire Works](#)

Contract Hire enables companies to run their company vehicles without the worry and risks of the capital cost and future vehicle values. Perhaps the simplest way to think of a Contract Hire agreement is as long-term car hire.

The contract is for a fixed term, which can be for a period of 12 months to 48 months. Typical terms for contract hire are either two or three years, normally with three monthly payments made in advance. For example if it were a two year contract of say \$200 per month, you would make an initial payment of \$600 and then pay 23 monthly payments of \$200. All payments are subject to VAT, in most cases the company can re-claim 50% of the VAT in the case of cars and 100% for commercial vehicles. Normally the monthly rentals can be off set against profits. At the end of the term you simply hand the vehicle back.

The advantages of Contract Hire to a company are as follows:

- * Off balance sheet funding
- * Fully budgeted costs
- * Maintenance can be included
- * No worries about future values
- * Does not tie up staff time on vehicle disposal

Contract Hire versus Hire Purchase of vehicles.

Many companies are now opting for Contract Hire in preference to Hire Purchase for their company vehicles. The attraction seems to be the ease of acquiring vehicles without the responsibility of ownership or the time and effort involved with eventual disposal. It also appeals to many companies that Contract Hire is off balance sheet and that they have fully budgeted costs.

When companies opt for hire purchase it can be because they plan to keep the vehicle for longer than a typical three year Contract Hire term. Although it is unusual for a company nowadays to keep a vehicle for longer than three years and of course if they do so, they have to consider that most vehicles will then be outside the warranty period.

It can also be because they feel that they may need to exit from the agreement early; although there are penalties payable for early termination with both funding methods, it is generally less expensive to terminate a Hire Purchase agreement. Of course for those who are concerned about this, they could as an alternative opt for a shorter Contract Hire agreement of say two years. Most companies provide the option to extend the agreement at the end of two years, in some cases on a monthly or quarterly basis.

Personal Contract Hire. (Contract Hire for individuals)

Personal Contract Hire is very similar to Contract Hire, detailed above; Contract Hire is designed for businesses and Personal Contract Hire is for individuals who wish to lease a vehicle. The only real difference for the client is the treatment of VAT. In the case of Contract Hire, the client pays a monthly rental to which VAT is added. In the case of Personal Contract Hire the monthly rental is inclusive of VAT.

The other benefits are the same as Contract Hire; fully budgeted monthly cost, maintenance can be included (so even the cost of replacing tyres is included in the monthly cost) and no further worries of disposing your vehicle. For many car owners the worst aspect of acquiring a new car is having to advertise and sell their existing vehicle and discovering that in the time they have owned it, it has dropped dramatically in value. With Personal Contract Hire as with Contract Hire you simply hand the vehicle back at the end of the term.

Personal Contract Hire versus Hire Purchase of vehicles.

Over the past few years many individuals have opted for Personal Contract Hire in preference to Vehicle Hire Purchase. This funding method can be of particular interest to those who are opting out of a company car scheme, or are in receipt of a car allowance. Also the ease of acquiring vehicles without the responsibility of ownership and eventual disposal of the vehicle seems to be an added attraction. Many seem to find the disposal of their vehicle to be particularly onerous; not liking the idea of a stranger turning up at their home to view the vehicle, and also they are often unsure of how best to deal with a test drive, as the prospective purchaser may not be fully insured.

When the vehicle is sold there is then the issue of payment; in general it is not considered advisable to receive large amounts of cash at home. If the

purchaser is paying for the vehicle with a Bankers Draft, as a precaution it's authenticity should be verified with the issuing bank.

For those who opt for Hire Purchase in preference to Personal Contract Hire when acquiring a new vehicle it is often done because they feel that they may keep the vehicle longer than the typical three-year term offered with Contract Hire. Also some feel there may be the possibility of needing to withdraw from the agreement early; although there are penalties for doing so with both funding methods, it is generally less expensive in the case of Hire Purchase. Of course those who are concerned about this, could as an alternative opt for a shorter two-year Personal Contract Hire term.

What to look out for when obtaining a Contract Hire or Personal Contract Hire quote.

Vehicle sourcing and broking is at the moment unregulated. There are government plans that it should become a regulated industry, in the meantime care should be taken when obtaining quotations.

* Advance Payments. A typical Contract Hire or Personal Contract Hire quotation will show three payments in advance, followed by perhaps 23 or 35 payments depending on the term. Some companies will advertise what appears to be a low monthly rental, however on closer inspection, it becomes evident that rather than three payments to be made in advance there are six. On other occasions the rental appears low because a much larger initial payment is required, sometimes running into thousands of pounds (there is an example at the end of this section, as to how a cost comparison can be made between a company quoting six payments and another quoting three payments in advance). In general the most straightforward way to make a cost comparison is to look at companies quoting three payments in advance and 10,000 miles per annum. 10,000 is the mileage companies normally advertise. Should your annual mileage requirements be higher most companies will be happy to provide a quotation at your required level.

* Deposits. If a broker requires a deposit it is very important to establish the terms under which the deposit is paid (a deposit should normally be paid to the supplying dealer). There have been many cases of vehicles not being delivered and the customer being unable to recover their deposit.

* Fees. On occasions there may be a fee payable, this can be unavoidable because some manufacturers charge a documentation fee, of perhaps \$125 - \$150. There are however cases of brokers charging their own fees. This is not necessarily a reason not to deal with a company but it is important to take the cost of the fee into account when comparing costs.

* Vehicle Availability. It is important to establish that a vehicle being advertised by a company is actually available at the price quoted and either in stock, or they are able to quote a delivery date. This can help to avoid the time and sometimes money that can be lost ordering a vehicle that is just not available, or not available at the price advertised.

Should you wish to establish which quote is the most competitive for a similar vehicle advertised, one company offering three and another six payments in advance, the calculation is as follows.

A Contract Hire Quote of \$200 per month over 36 months with three payments in advance.

3 payments in advance \$600
35 monthly payments @ \$200 \$7,000
Total cost \$7,600

The same vehicle quoted at \$189 per month over 36 months with six payments in advance.

6 payments in advance \$1,134
35 monthly payments @ \$189 \$6,615
Total cost \$ 7,749

In this example the vehicle that appears cheaper at first glance, is in practice more expensive. There is also a slight financial disadvantage when making six payments in advance; the extra cost of the three additional payments has to be found at the beginning of the contract, rather than being spread over the term. The difference however is minimal and in the interests of simplicity it is probably best to ignore this factor when making a comparison.

About the Author

Should you have any queries or questions regarding [Contract Hire, Personal Contract Hire or Hire Purchase](#) or any other funding method, please do

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