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LAWS AND HIRE PURCHASE ACCOUNTING IN NIGERIA

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ABSTRACT

Accounting is a profession that is highly guided by Laws, Principles, concepts and conventions. Hire Purchase Accounting which is one of the notable topics in accounting indisputably operates within the frame work of the Laws. In other to review and reassess Hire Purchase Accounting in line with the Hire Purchase Laws, the topic, 'Laws and Hire Purchase accounting in Nigeria was framed. To build-up from a good foundation, the paper started by having a look at some definitions of the key variable, Hire Purchase and interestingly, most of the definitions highlighted similar key features, such as; the right to the title of the goods on hire purchase which invariably belongs to the seller (which on one hand means that the hirer cannot pass good title to a third party while the hire purchase contract lasts), if the hirer wishes to end the hire purchase contract, he can do so subject to certain conditions, and the property in goods passes to the last instalment and after exercising the option conferred on him under the agreement. But where default occurs, the owner could repossess the hire purchase item. The Hire Purchase Laws in Nigeria are contained in the Hire Purchase Act of 1965, which stated amongst others, that the subject-matter of a hire purchase agreement can be goods (other than motor vehicles) whose value are not in excess of ₦2,000 and motor vehicles. Based on the unambiguous fact presented in this presentation, conclusion was drawn that Hire Purchase Laws doubtfully affects the preparation of accounts for Hire Purchase. On the whole recommendations were made which include; that the Hire Purchase Act should be carefully and thoroughly amended or replaced with a new one totally, to suit present day realities and that there is an essential need for a comprehensive Statement of Accounting Standards (SAS) for Hire Purchase Accounting.

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INTRODUCTION

Accounting is the language of business. It is a profession that is being guided by principles, concepts, conventions, laws, etc. All these fundamental building blocks serve as common and general compasses to all practitioners of the profession. In some cases, they are nation-wide tailored, while in other cases, they are universally tailored. Accounting as a living, practical, dynamic and realistic professional covers so many areas of social, economic (business), and governmental activities. Surely, any endeavour that involves monetary and material activities create a room for the services of Accounting. Many of the human endeavours for which the accounting profession plays significant (sometimes inevitable) roles include; Banking, Insurance, Manufacturing, Farming Contracting, Oil and Gas, Mining, Transportation (Air, Land and Sea), Educational Institutions, Churches, Ministries, ICT, Hire Purchase, Local Government Authorities, Estate Businesses, Export and Import Businesses, Bill of Exchange Transactions, Royalties Transactions, Consignment Transactions, Stock Market Transactions, Sports, Entertainment, Hospitals and Hospitality Industry, etc.

Amongst these activities where the role of the Accounting Profession has been recognized, the very one that enjoys the focus of this presentation is Hire Purchase. There are various definitions of Hire Purchase, but one main meaning. These definitions include:

A contract of hire-purchase is one under which an owner of goods lets them out on hire to another person called the hirer in consideration of periodic or instalmental payments called hire-rent and on condition that the hirer may at any time return the goods and terminate the hiring, or continue the hiring until the hire-rent reaches a stated sum, in which event either the property in the goods passes to him, or he will exercise an option to purchase the goods by paying a small (usually nominal) option fee (Ezejiofor et al: 1982).

Another definition of Hire Purchase is;

A hire purchase transaction involves an agreement for the delivery of goods under which the recipient of the goods pays a certain sum as deposit to the owner of the goods while promising to pay a certain sum as instalments at agreed intervals (for example, monthly) in consideration of being granted possession and use of the goods and an option to purchase them after a stipulated period, having paid the stimulated total sum.

Section 20(1) of the Hire Purchase Act 1965, defines Hire Purchase as “the bailment of goods in pursuance of an agreement under which the bailee may buy the goods or under which the property in the goods will or may pass to the bailee”.

All the above definitions have some features that are common in them, which are:

- a. Right of the goods still belongs to the seller. The hirer cannot pass a good title to the third party.
- b. The buyer will be informed of the cash price. If he however, wants to buy on Hire Purchase, then he will make payment over an agreed period of time in installments.
- c. Cash deposit will always be made when the Hire-Purchase agreement is signed.
- d. Interest rate will be changed on outstanding balance of the amount over the agreed period of time.

- e. If the hirer wishes to end the agreement, he can do so subject to certain conditions.
- f. The property in goods passes to the Hire Purchaser on the payment of the last installment and after exercising the option conferred on him under the agreement. But where default occurs, the owner could re-possess the Hire Purchase item.

BENEFITS OF HIRE PURCHASE

Most of the benefits of Hire Purchase transaction to both the seller and the hirer are embedded in the features enumerated above, while other benefits include; higher turnover for the seller through hire purchase sales, and opportunity to use (enjoy) product(s) that the hirer does not have the cash for.

TERMS THAT ARE ASSOCIATED WITH HIRE PURCHASE TRANSACTION:

- a. **Hire Vendor:** This is the owner of the goods that is sold under Hire Purchase terms.
- b. **Hire Purchaser:** This is the buyer of the Hire Purchase item.
- c. **Cash Price:** This is the normal selling price of the product without any interest added to it
- d. **Hire Purchase interest:** This is an additional amount to the cash price paid by the Hirer as compensation to seller who allows him to take possession of the goods without complete payment for the product. It is a recovery of cost of capital by the seller.
- e. **Hire Purchase Price:** This is made up of the cash price plus the hire purchase interest.
- f. **Deposit:** This is the initial payment made by the Hirer to the seller before taking possession of the Hire Purchase item. It is also called down payment.
- g. **Installment:** This is the agreed fraction of the Hire Purchase Price that is paid at different agreed intervals over agreed period of time to liquidate the Hire Purchase Price.

A MODEL HIRE PURCHASE AGREEMENT:

Hire purchase agreement on

Machinery/Equipment/Vehicle, etc No:

This hire purchase agreement is between Mr. Resident at No: (the owner of the product (Machinery/Equipment/Vehicle, etc), and Mr. Resident at No: (the hire purchaser).

The terms of the hire purchase are as stated hereunder:

- (1) That Mr. is the owner of the product.
- (2) That the owner allows Mr. to take possession and operate the product on hire purchase.
- (3) That the owner and the hire purchaser hereby agree that the hire purchaser will make daily/weekly/monthly/yearly returns of ~~₦~~..... to the owner for a period of Months/years, excluding/including Sundays/holidays. This sums up to a total return of ~~₦~~.....
- (4) That the hire purchaser takes care of all risks and liabilities associated with operating the machinery/Equipment/Vehicle, etc. Such risks and liabilities include, but not restricted to, general maintenance/fueling, costs of accidents to him and to third parties, government levies, police cases, and other incidents.

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- (5) The ownership passes to the hire purchaser on completion of the stated amount in (3) above.
- (6) That this agreement takes effect as from the and is expected to be completed on the if the hirer purchaser however completes the payment of the agreed sum before the expiration of the agreed Weeks/months/years, ownership certainly passes to him on the day of the payment completion.
- (7) That if the hire purchaser fails to make usual returns to the owner for a maximum of weeks/months/years, the owner will automatically re-possess the product.

Signed By:

- 1. Name: (Owner)
Address:
Signature:
Date:
- 2. Name: (Hire Purchaser)
Address:
Signature:
Date:
- 3. Name: (Hire Purchaser's Guarantor)
Official/ Residential Address:
Signature:
Date:
- 4. Name: (Witness)
Address:
Signature:
Date:

HIRE PURCHASE LAWS IN NIGERIA:

Hire Purchase Laws in Nigeria are contained in the Hire Purchase Act of 1965. Some of the highlights of the Act include:

- i. That the subject-matter of hire-purchase agreement can be goods (other than motor vehicles) whose value are not in excess of ₦2,000 and motor vehicles.
- ii. The seller of a Hire Purchase item remains the owner until the Hire Purchaser has fully paid for the price of the item and the Hire Purchaser has fully paid for the price of the item and the Hire Purchase interest.
- iii. If the Hire Purchaser has paid up-to-half of the price of the product (item), he can return the product to the owner, and the contract terminates. Otherwise, he (the hire purchaser) will be compelled to pay the balance to make-up the required one-half of the product price. When the Hirer returns the product and terminates the contract, he gets no refund of any amount already paid by him of any amount already paid by him.
- iv. Ownership of the Hire Purchase item passes to the Hire Purchaser as soon as he completes the payment of the price of the Hire Purchase item and interest.
- v. When the Hirer has paid up to one third of the price of the product, the owner cannot re-possess the product except through the decision of the court.
- vi. Only products that are durable in nature are usually considered normal for Hire Purchase transactions.
- vii. The Hirer is not under obligation to purchase the product unless he wishes to, as the owner can still re-possess the item, subject of compliance to the requirements of the law.
- vii. The Hirer cannot pass good title to a third party within the period of the Hire Purchase contract.

HIRE PURCHASE VERSUS CREDIT SALES: DIFFERENCES, AND SIMILARITIES.

- a. Differences between Hire Purchase and credit sales:
 - i. Hire Purchase sales attract interest, which is paid to the seller, while credit sales do not usually attract additional interest.
 - ii. In the accounting treatment of Hire Purchase, the nominal interest rate could be converted to the rate of interest, while this may not happen in conventional credit sales.
 - iii. When the hirer purchaser defaults in making the agreed payment, the seller has the right to repossess the item(s) under hire purchase, but in the conventional credit sales, the seller may only have to sue for the unpaid balance.
 - iv. In the Hire Purchase, any profit or loss made from the repossessed item will have to be reflected in the seller's Statement of Profit or Loss, while such is not the case in normal credit sales.
 - v. In most hire purchase Statement of Profit or Loss, profit is not assumed on any unpaid amount of the hire purchase, hence the calculation of unrealized profits and interests on hire purchase, but under the conventional credit sales, profit is assumed on the total amount of sales immediately the item is sold to the customer.

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- vi. In credit sales, the buyer can sell the item to a third party and title lawfully passes to him (the third party), but in hire purchase, the hire hirer cannot sell the item to someone else, since he is not yet the owner of the product.
- vii. Initial deposit (payment) will always be made at the beginning of the hire purchase transaction; while this may not be required in credit sales.
- viii. In hire purchase, the seller retains the ownership of the goods, while in credit sales, the buyer becomes the owner.
- ix. The product is usually acceptable in hire purchase transaction is a durable products, while any product can qualify for credit sales.
- b. Similarities between Hire Purchase and credit sales:
 - i. In both transactions, the buyer takes the possession of the product.
 - ii. The buyer in both cases pays for the price of the product.
 - iii. If the hirer purchaser all the conditions as agreed with the seller, then ultimately in both cases ownership passes to the buyers.
 - iv. In both cases, payment for the product is differed.

ACCOUNTING PRINCIPLES, CONCEPTS AND CONVENTIONS THAT AFFECT THE PREPARATION OF ACCOUNTS IN HIRE PURCHASE

The generally acknowledged Principles, Concepts and Conventions on which the practice of accounting is based, inevitably guides the preparation of accounts in Hire Purchase. These principles and concepts include:

Business entity concept, Money measurement concept, Going concern concept, Cost concept, Matching concept, Realization concept, Accruals/Prepayment concept, Dual aspect concept, Materiality convention, Convention of Prudence and Conservation, Consistency convention, Convention of Periodicity, and the Principle of objectivity.

ACCOUNTS THAT ARE NORMALLY PREPARED FOR THE HIRE PURCHASE TRANSACTIONS:

- a. Certain Accounts are normally prepared for Hire Purchase transactions in the Books of the Hire Purchaser. They include;
 - i. **Cash and bank account:** A cash or Bank Account (depending on the mode of payments by the business) is likely to be opened to take care of periodic payments of the instalments to the Hire Purchase seller. Other payments and receipts by the hirer will also be accommodated in this account.
 - ii. **Asset Account** (e.g. Motor Vehicle Account Machinery Account, Equipment Account, etc.): Normally, the hire purchase item will always be durable in nature and becomes or forms part of the Fixed Assets of the hirer purchaser. So, a Fixed Asset Account will usually be opened for it. This Fixed Asset Account will be debited in the name of the seller with the cost of the item, while it will be credited in the name of Asset Disposal with the same amount any time it becomes sold.
 - iii. **Provision for Depreciation Account:** Since the Hire Purchase item is a fixed Asset which the Hirer uses in running his business, it therefore enjoys periodic depreciation provision, and a depreciation account is hence opened. The depreciation Account will be

- Credited with the periodic (annual) depreciation amount in the name of profit or loss although the life of the asset in the business.
- iv. **Seller's Account or Creditors Account:** The seller in Hire Purchase transaction is the creditor. He receives initial deposit and regular installments form the hirer for the hire purchase item. The seller's account is usually credited with the cost of the Hire Purchase item and the due Hire Purchase Interest, while the account becomes debited with any amount (cash or bank) paid by the hirer. This account is updated yearly until the Hire Purchase contract ends.
 - v. **Hire Purchase Interest Account:** The benefit/compensation that the seller receives in Hire Purchase transaction is the interest. The buyer pays the interest to the seller and hence an interest payable account is normally opened in his books. The periodic interest amount will be debited in this account in the name of the seller, and this a will be done throughout the duration of the Hire Purchase contract.
 - vi. **Assets Disposal Account:** When the hire purchase product (Asset) is sold, an account called 'Asset Disposal Account' is normally opened in the books of the hire purchaser. The Asset Disposal Account will usually be debited with the cost of the product and credited with accumulated value for depreciation and proceeds from the disposal. Any Profit or loss on disposal will also be reflected in the Account.
 - vii. **Statement of Profit or Loss:** In the statement of profit or loss of the Hirer, both the Hire Purchase interest and periodic depreciation on the hire purchase asset will appear on the debit side of the account, as the constitute part of the cost (expenses) of running the business.
 - vii. **Statement of Financial Position:** As earlier stated, the hire purchase product will always be a fixed asset item which goes to the Statement of Financial Position under Fixed Assets. In the Statement of Financial Position, accumulation depreciation will normally be deducted from the cost of the item. Another amount that will be deducted from cost after depreciation is any unpaid amount on the hire purchase, after which a final net amount is arrived at and left in the Statement of Financial Position.
- b. In a similar vein, the accounts that can be prepared in the books of the seller that take care of the Hire Purchase Transactions include:
- i. **Cash or Bank Account:** The hirer pays period installments to the seller, and the payment covers amortized (part of the) cost of the hire purchase product and due interest. This payment that the seller receives has to be debited in the seller's cash or bank account amongst other receipts and payments (debited) within the financial period.
 - ii. **Sales (Hire Purchase Sales) Account:** In hire purchase transactions, the seller is seen as a person who engages in buying of goods, so all the sales he makes are usually aggregated (credited) in his sales account which is later posted to the Statement of Profit or Loss.
 - iii. **Hire purchaser's Account:** The hire purchaser or hirer is a debtor to the seller hence he is normally debited with the value of the goods sold to him, including the periodic due interest, while on the opposite side, any amount he pays is credited in his favour until the total amount that is due to the seller is exhausted.

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- iv. **Interest Account:** Earlier, it was stated that the hirer pays Hire purchase interest to the seller, for which he opens Hire Purchase Interest payable account. This Interest Payable shown in the books of the hirer becomes Interest Receivable in the books of the seller; hence an interest Receivable Account is normally opened by him. The period interests due to the seller are always credited in this Hire Purchase Interest Receivable Account, and subsequently posted to the credit side of the seller's Statement of Profit or Loss as an income (gain).
- v. **Statement of Profit or Loss:** The seller of the hire purchase product is a trade who will normally open a Statement of Profit or Loss to ascertain his Gross Profit for the period. All the hire purchase sales (in addition to other sales, if any) go to the credit side of the Statement of Profit or Loss. In some cases also, unrealized profits and interest on hire purchase sales are adjusted against the total sales by debiting it in the Statement of Profit or Loss. Equally, the Statement of Profit or Loss is usually affected by Hire Purchase transactions because periodic Hire Purchase Interest receivable must have to be credited in the Statement of Profit or Loss of the seller, since the interest constitutes part of the seller's gain for the financial period.
- vi. **Statement of Financial Position:** The unrealized profit and interest on sales that is debited in the Statement of Profit or Loss as a deduction from sales also goes to the Current Assets side of the Statement of Financial Position, and it is normally deducted from total debtors in line with the convention of conservation.

EFFECTS OF THE HIRE PURCHASE LAWS ON THE ACCOUNTS:

- i) Based on the Hire Purchase Act of 1965, hire purchase transactions and Accounts would have been limited to vehicles only, because of the provision of the Act which says that "the subject-matter of a hire purchase of a hire purchase agreement can be goods (other than motor vehicles) whose value are not in excess of ₦2, 000 and motor vehicles". However, common law is devoid of this impediment.
- ii) As the law vest the ownership right on the seller while the hire purchase contract lasts, the financial statement of hirer is presented in the light of this law, hence any unpaid amount on the hire purchase asset is normally deducted from the total value of the Fixed Asset in the periodic Statement of Financial Position of hirer. In the same manner, by the financial year, year end, unrealized profit and interest on hire purchase sales are deducted from both the gross profit in the Statement of Profit or Loss and from total debtors in the Statement of Financial Position.
- iii) When re-possession of the hire purchase product occurs, it could lead to profit or loss and this becomes part of the contents of the Statement of Profit and Loss in the books of the seller. In this situation also, the re-valued amount of the returned product will be added back to the stock of the seller, and it becomes part of both Statement of Profit or Loss and the Statement of Financial Position for the period.

- iv) Hire Purchase products are always treated as Fixed Assets in the books of the hirer, and periodic provision for depreciation is made for them because the law made it mandatory that hire purchase goods are to be durable in nature.

CONCLUSION

A brief review of certain aspects of the Hire Purchase Laws in Nigeria and Hire Purchase Accounting has been presented in this paper. From the laws (Hire Purchase Act 1965), we are made to understand that the subject-matter of a hire- purchase agreement can be goods (other than motor vehicles) whose value are not in excess of ₦2,000 and motor vehicles, the seller of the hire purchase item remains the owner until the hirer has fully paid for the price of the item and the hire purchase interest, ownership of the hire purchase item passes to the hire purchaser as soon as he completes the payment of the price of the hire purchase product and interest, and only products that are durable in nature are usually considered normal for hire purchase transactions. The law made it crystal clear that hire purchase and credit sales are not the same, even though there are similarities. The preparation of accounts in hire purchase are invariably guided by normal accounting principles, concepts and convention, and such accounts that could be opened in the books of both seller and the hirer include; cash or bank account, Assets Account, provision for depreciation Account, Hire Purchase Interest Account, Hire Purchase Sales Account, amongst others. The Hire Purchase Laws undoubtedly affects the presentation of Accounts for Hire Purchase. It therefore follows that any deficiency or Lacuna in the Hire Purchase Laws will, directly or indirectly, have some impact on Hire Purchase Accounting.

RECOMMENDATIONS

- a. As noted earlier in this presentation, the Hire Purchase Act (1965) limits the monetary value of goods that could be hired out to #2000, except motor vehicles. In the absence of common law, this make very impossible for hire purchase to be in operations in these days for any product (Machinery, Plant, Equipment, etc.) besides motor vehicles. Therefore, the Hire Purchase Act should be carefully and thoroughly amended or replaced with a new one totally, to suit present day realities.
- b. In as much as the preparation of Hire Purchase Accounting is being guided by the prevailing Principle concepts and conventions of accounting, there is still an essential need for Hire Purchase Accounting to be package by the right body (Financial Reporting Council of Nigeria - FRCN), since such as SAS is presently not in existence.
- c. Hire Purchase as a convenient way of funding business (starting and running businesses) should be made more popular by governments at all levels in Nigeria to encourage (as well as stimulate) entrepreneurship, economic empowerment and business/industrial growth
- d. There may be need to always include as one of the ledger account in the books of the sellers, stock (Hire Purchase Adjustment) Account in order to decongest the Statement of Profit or Loss of seller.

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- e. There may need to always include as one of the ledger Accounts in the books of the seller, 'unrealized profit interest on Hire Purchase (Adjustment) account', in order to also decongest the Statement of Profit or Loss of the seller.
- f. In order to decongest the Statement of Financial Position, there may be need to always include in the Ledger Accounts of the hirer, assets (Hire Purchase adjustment) Account.
- g. Finally, in order to decongest the Statement of Financial Position of the hirer, there may be need to always include in the Ledgers Accounts of the hirer, 'debtors (Hire Purchase adjustment) Accounts'.

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