Money, money,

All very well if you're a rich man, but most of us are not. So, if you're after a few access platforms, or maybe a couple of cranes, you'll be looking around for some finance options. **Simon Wilkinson** advises.

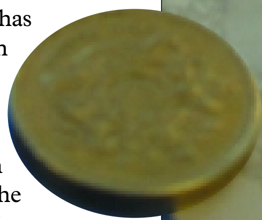
Many companies will have seen opportunities to develop business, but lack the cash resources to complete the purchase without compromising working capital.

In the crane and access industries there is one key element that works in your favour: you are dealing with long-life, slow depreciating assets which are regarded as good security by the finance industry.

Obtaining finance for equipment is relatively simple, but critical to your business is obtaining the right facility with a structure and term that is matched to your cashflow. It is in this area that there is usually a disparity between the borrower, who wishes to borrow as much as possible for as long as possible in order to preserve cashflow, and the lender who wants to lend as little as possible over as short a term as possible, in order to preserve security.

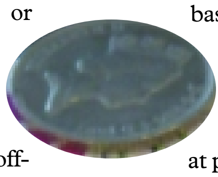
Having identified the equipment you wish to purchase, it is now time to approach the finance market. There are some basic guidelines that you should bear in mind when undertaking this exercise:

- Always obtain quotations in writing
- Do not put all of your eggs in one basket, spread your risk among different lenders
- If you have a facility with your bank and then use their asset finance arm to finance your equipment, you may experience difficulties at a later date over 'Group Exposure'
- Always check for any fees or insurances that are to be charged in addition to the basic finance costs
- Ensure that your accounts are up to date and that the projected income and outgoings associated with the acquisition of the equipment have been well thought through
- It is worth taking some independent advice before committing to a finance contract



The finance industry has become more innovative in recent years, with a number of major finance companies employing specialists working specifically in the construction equipment market. Whilst the basic facilities available to finance equipment have not changed, there have been more variations in structures with stepped repayments, VAT deferrals, seasonal payments and balloon payments all of which are designed to structure the repayments to match your cashflow. It remains true, however, that the stronger your balance sheet the more flexible the facility and the weaker your balance sheet the more rigid the facility as the lenders eye is drawn closer towards their exposure to the asset.

Hire purchase



At the end of the three, five or seven years it generally takes to pay off on a hire purchase agreement, you will own your machine. You will be able to claim capital allowances to be offset against your profit, and benefit from a smaller tax bill at the end of the year. Hire Purchase repayments are usually monthly or quarterly and can be variable or fixed rate.

Finance Companies normally require a deposit of 10% or more, plus the full VAT attracted by the purchase price. Many lenders have now realised that payment of the VAT on large items of equipment can put an enormous strain on working capital and will consider deferring the VAT until it has been reclaimed. Many companies can offer payment holidays, stepped payments and can set things up to allow the equipment to start generating money before you start payments but remember that there is always a cost in using these structures that put off the evil day of having to meet the regular monthly repayments.

A couple of points worth considering are that fixed rates are currently very good value but, in entering into a fixed rate agreement, early settlement can be an expensive option with the interest penalties charged by all lenders. A fully variable rate facility usually avoids this problem, but then you are risking your interest costs rising when base rates rise. There are also compromise arrangements with some lenders where your repayments will be fixed but the transaction tracks changes in base rates, either reducing the period of finance if rates come down or extending the period should rates increase.

Fixed rates are the most popular at present but do not finance equipment over a longer term than you expect to keep it, otherwise you will pay the penalty.

Finance lease

The Finance Lease has become a less popular option for buyers of large capital plant, because many of the tax benefits have been eroded in recent years. Did you realise that a finance company cannot claim the same capital allowances that you are entitled to when you purchase equipment? They are entitled to a maximum 25% first year allowance which is time apportioned over their financial year.

You will never own the machine with finance lease, but at the end of it, with the lender's permission, you will usually be able to sell it to an independent third party and retain the majority of the proceeds. Alternatively you will normally be allowed to retain the use of the equipment into a

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secondary leasing term and pay an annual 'peppercorn' rental.

Leases can be structured in a similar manner to hire purchase agreements and over similar periods but the key differences are that you will being paying rentals rather than making repayments and instead of paying the VAT at the start of the agreement you pay VAT only on the rentals as they become due.

Siemens' useful website (www.siemens financialservices.co.uk), which offers a range of financial advice, says "A finance lease is where you pay the full cost of the equipment, plus interest, over the primary term of the agreement via a series of monthly repayments. It's deemed that you are taking the 'risk and reward' in using the equipment, meaning that the asset is treated by you as if it were your own, and the value of the asset is therefore shown on your balance sheet.

"Payments are tailored to match your budget and may be offset against taxable profits.

"At the end of the agreement you can choose whether to continue leasing the equipment at a reduced rate, simply upgrade or sell the equipment as our agent."

Operating lease

Operating lease is the last option of the big three, most commonly chosen routes.

The lender assumes that the asset will have a resale value at the end of the lease period and so the lessee can pay a lower rental over the term of the lease. The resale value is generally termed a 'residual value'.

At the end of the contract term you are required to return the equipment to your lender, who will resell the equipment and expect to generate a profit on sale.

The advantage to this method is that the asset does not show up on your balance sheet – because it is the lender, not the lessee, taking the risk. This is known as 'off balance sheet funding'.

An operating lease is most likely to be used when you don't think you will want to keep the equipment for long. This method is getting more popular now – could this be a reflection of tighter safety regulations meaning that people don't want to take a risk with older machinery? If you do decide to keep the crane or access platform at the end of your rental period, you will have to renegotiate with the finance company, based on their view of the fair market value of the asset at that time.

This facility can be a useful option if you have an opportunity to quote for a specific contract where machines are required for a limited period of perhaps 12 or 24 months and you would be unable to absorb the machines into your fleet at the end of the term. Using an operating lease in this situation would allow you to price the contract and fix your margin knowing that at the end of the term the machines will be returned to the finance company.

Lease purchase

A lease purchase agreement allows you title to your equipment at the end of the lease. After paying your lender a series of instalments over a defined period – normally between 12 and 60 months, at the end of the term you will be given the option to purchase via a single, pre-agreed payment. Before that, the lender has title to the asset. In truth this is a hire purchase agreement dressed up to look a little different!

This is an on balance sheet facility, usually based on a monthly payment profile. Interest charges may be set off against taxable profits and the hirer is entitled to claim the capital allowances

Special packages

Watch out for any special packages offered by lenders aside from the usual offerings. An example of this is 'Business Threeways' at Royal Bank of Scotland, normally an on balance sheet option, where you can buy the asset at the end of the finance term for the balloon payment and option to purchase fee, give back the asset with no further liability (in good condition) or continue the agreement under the terms of an extension agreed at the start.

Manufacturer Schemes

Don't dismiss schemes offered by some manufacturers. These can provide excellent value for money and a degree of flexibility often not available through traditional finance companies. Many of these schemes are backed by finance companies but with recourse arrangements with the manufacturers.

What to choose

"We can give the customer facts and benefits about all the options, but the decision rests with them", says Gary Egerton of Royal Bank of Scotland. "Clients should consider all the options and, if necessary, seek advice from their accountants.

Bill Green of PLC offers advice from personal experience to new kids on the block. "Banks and finance companies do not like to take risks. If they see an area (in your financial credibility) which makes them nervous, they will insist on personal guarantees. It could be your house, or any other tangible asset worth at least the value of your purchase. This will be at risk if you default. Until your company has built up a good trading record, it is most likely that you will have to put up personal guarantees."

It is rare for any new business to be launched without considerable personal investment and risk – a leap of faith is generally required. But remember, 'look before you leap'. ■

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