



# Five Minute Accounting



## F06410 – Prompt Payment (a.k.a. Sales) Discounts

### The Basics

- Sellers sometimes offer early payment discounts
- A sales discount is not a price reduction, it is a reward/incentive to accelerate customer payment
- Prompt payment discounts are recorded only when payment is received
- Prompt payment discounts accumulate in a separate contra-revenue account

### What is a Prompt Payment or Sales Discount

The idea is simple: A seller's terms allow the buyer to deduct a specified amount from their payment if it is paid within the "discount period" as specified in the terms.

The terms prompt payment and sales discount are interchangeable. Textbooks typically call them sales discounts.

### Terms

Sellers put terms on invoices stipulating the timeframe in which customers must pay. Simple terms look like this:

- N10 – Net due in 10 days
- N30 – Due in 30 days

When discounts are offered terms are expressed like this:

- 2/10, N30 – Pronounced "two ten, net thirty" – it means the buyer can deduct 2% of any amounts paid within 10 days, but 100% is due within 30 days.
- After 30 days the seller has legal recourse for collection.

### Examples

- \$1000 invoice, terms: 1/10, N30
  - Paid within 10 days the buyer can remit \$990 for payment in full
- \$1000 invoice, terms: 2/15, N30
  - Paid within 15 days the buyer can remit \$980 for payment in full
- \$1000 invoice, terms: 1/10, N30 but only \$500 is paid within 10 days; the other \$500 in 30 days
  - \$495 paid in 10 days satisfies \$500 of the amount due. Partial payments within the discount term earn the proportional discount.
  - \$500 of balance must be paid in full



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## Accounting

The sales discount does not affect the sale entry; it only changes the payment entry. For example, a \$1000 sale on account with terms (2/10, N30) is recorded as:

Date	Accounts	DR	CR
6/1/xx	Accounts receivable	1,000	
	Sales		1,000

If payment in full of \$980 is received within the 10 day discount period the following entry is recorded:

Date	Accounts	DR	CR
6/9/xx	Cash	980	
	Sales discounts	20	
	Accounts receivable		1,000

## Financial Statement Presentation

Sales discounts are accumulated in a separate account for transparency, allowing readers to fully understand the nature of the transaction:

Sales	1,000
Less: Sales discounts	<u>-20</u>
Net sales	980

You can see that the above presentation is more informative than simply reducing sales.