

Sunland Company Sells Merchandise On Account For \$5100 To Wildhorse Company With Credit Terms Of 1/10,

Sunland Company sells merchandise on account for \$5,100 to Wildhorse Company with credit terms of 1/10, initiating a transaction that has important implications for both companies' accounting records, cash flow management, and credit policy enforcement. This transaction exemplifies typical credit sales in business-to-business (B2B) commerce, involving key concepts such as sales recording, credit terms, potential discounts, and subsequent collection procedures. Understanding the details of this sale provides insight into how companies manage receivables, apply discounts, and ensure accurate financial reporting.

Overview of the Transaction: Sale on Credit

Details of the Sale

- Seller: Sunland Company
- Buyer: Wildhorse Company
- Sale Amount: \$5,100
- Payment Terms: 1/10, net 30
- Transaction Type: Sale on account (credit sale)

Understanding Credit Terms: 1/10, Net 30

The credit terms specify the conditions under which Wildhorse Company can pay for the merchandise:

- 1/10: A 1% discount is available if the invoice is paid within 10 days from the invoice date.
- Net 30: The total amount (\$5,100) is due within 30 days if the discount is not taken.

This structure incentivizes early payment, improving Sunland Company's cash flow and reducing the risk of bad debts.

Accounting for the Sale

Recording the Sale in Sunland Company's Books

When Sunland Company makes the sale, it must record the revenue and the corresponding accounts receivable. The journal entry typically involves:

- Debiting Accounts Receivable for \$5,100 to recognize the amount owed by Wildhorse Company.
- Crediting Sales Revenue for \$5,100 to record the sale.

Journal Entry:

Accounts Receivable \$5,100

Sales Revenue \$5,100

This entry reflects the company's expectation to collect \$5,100 from Wildhorse and recognizes the revenue earned from the sale.

Impact on Financial Statements

- Income Statement: The sale increases revenue by \$5,100.
- Balance Sheet: Accounts receivable increases by \$5,100, representing the amount owed by Wildhorse.

Applying the Credit Terms and Discount Policy

Potential for Early Payment Discount

Wildhorse Company has an opportunity to reduce its payable amount if it pays within 10 days:

- Discount Amount: 1% of \$5,100 = \$51

- Discounted Payment: \$5,100 - \$51 = \$5,049

If Wildhorse pays early, Sunland will receive less cash but benefits from quicker collection.

Recording the Discount When Taken

Suppose Wildhorse pays within the discount period; Sunland must record the receipt of cash and the discount allowed:

Journal Entry Upon Payment:

Cash \$5,049
Sales Discounts \$51
Accounts Receivable \$5,100
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This entry reduces accounts receivable by the full amount and recognizes the discount as a reduction in sales revenue.

## **If Payment Is Made After the Discount Period**

If Wildhorse pays after 10 days but within 30 days:

- No discount applies.

- Journal Entry:

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Cash \$5,100
Accounts Receivable \$5,100
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This reflects full collection without any discounts.

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## **Implications for Wildhorse Company**

### **Recognition of Accounts Payable**

Wildhorse must record the purchase as an account payable:

- Initial Entry:

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Inventory (or relevant asset) \$5,100
Accounts Payable \$5,100
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This increases liabilities, reflecting the company's obligation to pay Sunland.

### **Payment Timing and Discount Utilization**

- If paying early: Wildhorse benefits from a 1% discount, reducing its payable to \$5,049.
- If paying late: It pays the full amount of \$5,100 after 30 days.

### **Effect on Cash Flow and Budgeting**

- Early payment with discount reduces cash outflow slightly.
- Proper management of payment timing can improve Wildhorse's liquidity management.

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## **Cash Collection and Follow-Up Procedures**

### **Monitoring Receivables**

Sunland must track outstanding accounts receivable to ensure timely collection:

- Use aging reports to monitor overdue accounts.
- Send reminders or collection notices as needed.

### **Enforcing Credit Terms**

- Implement policies for late payments, possibly applying penalties or interest.
- Decide whether to offer discounts as an incentive for early payment.

### **Handling Bad Debts**

- If Wildhorse defaults or cannot pay, Sunland may need to record an allowance for doubtful accounts.
- Write-offs are made when collection is deemed uncollectible.

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## **Financial Impact and Reporting Considerations**

### **Revenue Recognition**

- The sale is recognized at the point of sale, based on the invoice date.
- Discounts are accounted for when applicable, reducing sales revenue accordingly.

### **Accounts Receivable Management**

- The balance of accounts receivable reflects the total amount owed by all customers.
- Efficient collection practices improve cash flow and reduce bad debt risk.

### **Impact on Financial Ratios**

- Accounts receivable turnover ratio indicates how quickly receivables are collected.
- The discount policy can influence profitability and cash flow metrics.

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## **Conclusion: Strategic and Practical Considerations**

Managing credit sales transactions like the sale from Sunland to Wildhorse involves careful accounting, strategic credit policies, and diligent receivables management. Offering credit terms such as 1/10, net 30 encourages early payment, which benefits Sunland's cash flow, but also requires robust procedures to ensure collection and minimize bad debts.

Effective communication of credit terms to customers, timely recording of sales and receipts, and vigilant monitoring of receivables are essential for maintaining healthy financial health. Additionally, understanding the implications of discounts and payment timing helps both companies optimize their cash flow and profitability.

In summary, this transaction underscores the importance of precise accounting practices, strategic credit policies, and efficient receivables management in successful business operations. By adhering to these principles, companies like Sunland and Wildhorse can foster mutually beneficial relationships while maintaining strong financial positions.

## **Frequently Asked Questions**

### **What is the total amount Sunland Company will record for the sale to Wildhorse Company on account?**

The total amount recorded will be \$5,100, which is the sale price before any discounts.

### **What does the credit term '1/10' mean in this transaction?**

It means that Wildhorse Company can receive a 1% discount if they pay within 10 days of the invoice date.

### **If Wildhorse Company pays within the discount period, what amount will they pay to Sunland Company?**

They will pay \$5,100 minus 1%, which is  $\$5,100 - \$51 = \$5,049$ .

### **What journal entry should Sunland Company make to record this sale on account?**

Debit Accounts Receivable \$5,100 and credit Sales Revenue \$5,100.

### **How will Sunland Company record the receipt if Wildhorse Company pays within the discount period?**

They will debit Cash \$5,049, debit Sales Discounts for \$51, and credit Accounts Receivable \$5,100.

## **What is the purpose of offering credit terms like '1/10' in sales transactions?**

To incentivize early payment by offering a discount, thereby improving cash flow and reducing credit risk.

## **How does the '1/10' credit term impact Sunland Company's revenue recognition if the discount is taken?**

If the discount is taken, Sunland Company records revenue at the discounted amount of \$5,049, reflecting the actual cash received.

## **Additional Resources**

Sunland Company Sells Merchandise On Account For \$5,100 To Wildhorse Company With Credit Terms Of 1/10

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### **Introduction**

In the world of business transactions, understanding the mechanics behind sales on account and related credit terms is crucial for both financial management and strategic planning. Today, we delve into a specific case: Sunland Company's sale of merchandise valued at \$5,100 to Wildhorse Company, under the credit terms of 1/10, n/30. This example provides a comprehensive view of how credit sales are recorded, the significance of credit terms, and the financial implications for both companies involved. Whether you're an accounting professional, a business owner, or a student, this detailed analysis aims to clarify the nuanced processes that underpin such transactions.

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## **Understanding the Basics: Sale on Account and Credit Terms**

### **What is a Sale on Account?**

A sale on account, also known as a credit sale, occurs when a company sells goods or services to a customer without receiving immediate payment. Instead, the customer agrees to pay within a specified period. This practice facilitates business growth by allowing customers to acquire goods without immediate cash outlays, fostering long-term relationships and increasing sales volume.

### **The Significance of Credit Terms**

Credit terms define the conditions under which a customer must settle their outstanding balance. They specify the timeframe for payment and any discounts available for early payment. Proper

understanding and management of these terms are vital for maintaining healthy cash flow, minimizing bad debts, and optimizing profitability.

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## Details of the Transaction Between Sunland and Wildhorse

### The Sale Transaction

- Seller: Sunland Company
- Buyer: Wildhorse Company
- Product/Service: Merchandise (unspecified in the scenario)
- Sale Price: \$5,100
- Payment Terms: 1/10, n/30

The sale indicates that Wildhorse Company has purchased merchandise from Sunland with a total invoice amount of \$5,100. The terms, 1/10, n/30, are standard in many industries, offering a potential discount to encourage early payment.

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## Decoding the Credit Terms: 1/10, n/30

### What Do These Terms Mean?

- 1/10: The buyer can take a 1% discount if the invoice is paid within 10 days of the invoice date.
- n/30: The net (full) amount is due within 30 days if the early payment discount is not taken.

These terms are designed to incentivize prompt payment, thereby improving the seller's cash flow and reducing the risk of bad debts.

### Practical Example

Suppose the invoice date is October 1, 2023:

- If Wildhorse pays by October 11, 2023, they are eligible for a 1% discount.
- If they pay after October 11 but before October 31, they must pay the full amount of \$5,100.

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## Recording the Sale in Sunland's Books

### Step 1: Recognize the Revenue

Upon delivery of goods, Sunland records the sale:

- Debit: Accounts Receivable \$5,100
- Credit: Sales Revenue \$5,100

This recognizes the revenue earned from the sale and the receivable owed by Wildhorse.

Step 2: Consideration of Cost of Goods Sold (if applicable)

If Sunland maintains inventory accounts, it should also record:

- Debit: Cost of Goods Sold (COGS) — based on the cost of merchandise sold
- Credit: Inventory — to reduce inventory by the cost of the merchandise

This aligns with the matching principle in accounting, matching expenses with revenues.

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## Handling the Discount When Payment Is Made

Scenario 1: Payment Within Discount Period

Suppose Wildhorse pays within 10 days, on October 8, 2023:

- Calculate the discount: 1% of \$5,100 = \$51
- Amount payable after discount: \$5,100 - \$51 = \$5,049

Recording the receipt:

- Debit: Cash \$5,049
- Debit: Sales Discounts Forfeited (or similar account) \$51 (if tracking discounts separately)
- Credit: Accounts Receivable \$5,100

Alternatively, the entry might be:

- Debit: Cash \$5,049
- Debit: Sales Discounts Allowed (as an expense or contra-revenue account) \$51
- Credit: Accounts Receivable \$5,100

This reflects the early payment with discount and settles the receivable.

Scenario 2: Payment After Discount Period

If Wildhorse pays on October 20, 2023, beyond the discount window:

- Amount payable: \$5,100

Recording the payment:

- Debit: Cash \$5,100
- Credit: Accounts Receivable \$5,100

No discount applies here, so the full invoice amount is collected.

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## **Implications for Wildhorse Company**

Wildhorse's decision to pay early or late impacts its cash flow and financial statements.

- Early Payment Benefits:
  - Savings of 1% on purchase price
  - Strengthening of supplier relationships
  - Potential to negotiate better terms in future transactions
- Late Payment Risks:
  - Missing out on discounts
  - Possible late fees or penalties (if applicable)
  - Strain on supplier relationship

Wildhorse must evaluate its cash position and operational needs to determine the optimal payment timing.

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## **Financial Impact and Analysis**

For Sunland Company:

- Revenue Recognition: The sale increases sales revenue and accounts receivable.
- Cash Flow: Early payments improve cash inflow, reducing receivables.
- Discounts Given: If Wildhorse pays early, Sunland records a sales discount, decreasing net revenue but encouraging early payment.

For Wildhorse Company:

- Cost Management: Taking advantage of discounts reduces purchase costs.
- Cash Flow Planning: Timely payments help maintain liquidity and supplier relationships.
- Financial Metrics: Discounts can improve gross profit margins on purchases.

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# Best Practices for Managing Such Transactions

1. Clear Documentation: Ensure invoices clearly specify credit terms and due dates.
2. Timely Reminders: Send payment reminders close to the discount window.
3. Accurate Record-Keeping: Maintain detailed records of receivables, payments, and discounts.
4. Cash Flow Forecasting: Incorporate expected early payments and discounts into cash flow projections.
5. Credit Analysis: Evaluate customer creditworthiness to mitigate the risk of non-payment.

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## Conclusion: Strategic Significance of Credit Terms

The transaction between Sunland Company and Wildhorse Company exemplifies fundamental principles of credit management, revenue recognition, and cash flow optimization. The 1/10, n/30 credit terms serve as a strategic tool—balancing the incentives for early payment against the risk of delayed settlement.

For businesses, understanding these terms and their implications is vital. Properly managing discounts, receivables, and payment timings can impact profitability, liquidity, and supplier relationships. As demonstrated, the straightforward transaction of selling merchandise on account involves a series of carefully coordinated accounting entries and strategic decisions that ripple across financial statements and operational performance.

By mastering the nuances of such transactions, companies can foster healthier financial practices, enhance profitability, and build stronger partnerships, ultimately contributing to sustained business success.

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In summary, the sale of \$5,100 on credit with 1/10, n/30 terms reflects a common yet strategically significant practice in commerce. It underscores the importance of precise accounting, effective credit management, and the proactive optimization of payment behaviors to maximize benefits for both seller and buyer.

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