



Discounts and Allowances for Pledges Receivable

Both *Allowance for Doubtful Accounts* and *Discount on Pledge Receivable* are balance sheet accounts which assist in more accurately presenting pledge receivables on the statement of financial position (balance sheet), allowing users of the financial statements to see a more accurate picture of the organization.



What is an allowance for doubtful accounts?

When an organization receives promises to give, revenue and a pledge receivable are recorded in the general ledger. Unfortunately, not all receivables will likely be collected. Management should review gross pledge amounts annually to determine collectability.

The allowance method presents an organization's receivables with a reduction ("contra-asset") account called allowance for doubtful accounts. The allowance for doubtful accounts is used to reduce the amount of receivable to what is expected to be collected.

When an organization waits to recognize a bad debt until the account is determined to no longer be collectible, it is called the direct write-off method. This causes an organization to recognize expenses a year or two after revenues have been recorded — significantly impacting budgets and bottom lines! The allowance method gives a more accurate representation.



...And how is an allowance calculated?

The allowance for doubtful

accounts is not formula based, but should take into consideration many different factors such as the age of the receivable, the history of collectability of the donor and the overall amount promised. Additionally, management may note that collectability is not an issue based upon the organization's historical experience in the collection of balances due, and this is an acceptable accounting policy, as well.

What are the related journal entries?

The following example details how to record the allowance:

In 2017, multiple organizations have promised \$100,000 to ABC Organization. Historically, ABC organization has collected 87% of promises in the past. ABC's management has determined this is an appropriate estimation of collectability on the pledges. So 13%, or \$13,000, is allocated to the allowance for doubtful accounts.

DR: Bad Debt Expense	\$13,000
CR: Allowance for Doubtful Accounts	\$13,000

One of the organizations which pledged \$6,000 has been determined as uncollectible. The following journal entry is recorded to write off the amount.

DR: Allowance for Doubtful Accounts	\$ 6,000
CR: Accounts Receivable	\$ 6,000

As debts continue to be written off, the allowance account balance decreases. At the end of each accounting period, bad debts are estimated again, and the balance is adjusted as needed.

What is a discount on pledge receivable?

When an organization receives notice of significant long-term pledges, management should consider the related time value of money discount. Accounting principles state that a pledge must be recognized at present value, which is the current worth of cash to be received in the future, discounted at a market rate of interest. Pledges that are to be collected in a year or less can be recorded at full value. Discounts are also set up as contra-asset accounts, but separate from the allowance.

...And how is the discount calculated?

Excel has a present value (PV) calculation formula that will do the calculation for you. Three pieces of information are needed: discount rate, length of pledges from current year, and pledge amount.

The discount rate used should be a rate commensurate with the risk involved. Most organizations use the US T-Bill rate, which is a considered a risk-free rate of return.

What are the related journal entries?

In 2017, ABC Organization receives notice of a \$1,000,000 pledge to be paid out evenly over the next four years, starting in 2018.

	2018	2019	2020	2021	Total
Amount	\$250,000	\$250,000	\$250,000	\$250,000	
Formula	NONE – Recorded in full	=250000-PV (2%,2,,250000)	=250000-PV (2%,3,,250000)	=250000-PV (2%,4,,250000)	
Discount	\$ -	\$ 9,708	\$ 14,419	\$ 19,039	\$43,166

To record the discount in 2017:

DR: Pledge Receivable	\$1,000,000
CR: Pledge Revenue	\$ 956,834
CR: Discount on Pledge Receivable	43,166

In 2018, the organization should recalculate the amount of discount and take into consideration new pledges in the current year. For ease of example, in 2018, the Organization received an additional pledge of \$100,000 to be paid evenly in 2019 and 2020. The following entry recognizes the discount in future years:

	2019	2020	2021	Total
Amount	300,000 = 250,000 + 50,000	300,000 = 250,000 + 50,000	\$250,000	
Formula	NONE – Recorded in full	=300,000-PV (2%,2,,300000)	=250000-PV (2%,3,,250000)	
Discount	\$ -	\$ 11,649	\$ 14,419	\$26,068

2018 Journal Entry: $(\$43,166 - 26,068 = 17,098)$

DR: Discount on Pledge Receivable	\$17,098
CR: Pledge Revenue	\$17,098

At the end of each accounting period, the discount on pledge receivable should be adjusted as needed.

Additional resources

[Use the accrual method with an A/R contra account](#)
[Accounting 101: Adjusting Journal Entries](#)
[Allowance For Doubtful Accounts](#)



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