

Vendor Prepay for Product that has Decreased in Price

Last Modified on 04/27/2022 9:08 am CDT

If the prepay Purchase Order was created and paid in the prior year and it is preferred to recognize the loss in the prior year, set up a new general ledger account in the current year and the prior year called *Recognized Inventory Value Loss of Prepaid Purchases* and set it as a liability account. Speaking with an accountant is recommended before deciding what type of account should be selected.

1. In the prior year, make a Journal Entry debiting the cost of goods associated with the product(s) on the Purchase Order and credit the new general ledger account for the value of the inventory write down. Allow that Journal Entry to post forward to current year beginning balances.
2. In the current year, set up a new Purchase Add-on Charge. It should post to the new general ledger account.
3. When the Purchase Invoice is processed, add the negative add-on charge for the difference between the prepaid cost and the actual cost. The total of the add-on charge will be the difference between the prepaid cost and the Purchase Invoice cost multiplied by the quantity on the Purchase Invoice and should be entered as a negative amount. This way, the vendor is receiving the cost agreed upon when the prepay was paid but the inventory cost is being reduced by the negative add-on charge.

If the issue does not cross years or it is preferred to not affect the prior year, only enter the new general ledger account in the current year and make the Journal Entry in the current year as well. In either case, when the Purchase Order has been fulfilled, that newly added account should be zeroed out.

Example: A prepaid Purchase Order has been entered in the prior fiscal year for product at \$1000/ton, but the product is now only worth \$800/ton. In the current year, the Purchase Order will pull into the Purchase Invoice at \$1000/ton, but the difference must be offset with a purchase add-on of -\$200/ton. The cost of the product will be \$800/ton for that Purchase Invoice and the vendor prepay amount used will be \$1000/ton as it was entered on the prepaid Purchase Order.