

Early payment discount (Skonto): leveraging payment terms and managing liquidity

An early payment discount (Skonto) is a price reduction granted by a supplier if the invoice amount is settled within a short period, typically 8 to 14 days. For buyers, it is a central instrument for managing payment capability and liquidity in the procurement process. This article explains the definition, calculation, negotiation of terms, controls and typical pitfalls from the perspective of DACH industry.

Key facts

- An early payment discount is a rebate for early payment, typically 1 to 3 per cent of the invoice amount within a period of 8 to 14 days.
- The annualised effective interest effect often lies between 15 and 60 per cent in practice, and therefore typically significantly exceeds short-term borrowing costs.
- Legally, the discount is treated as remuneratory, i.e. as consideration for early payment, and is not an obligation of the supplier.
- The decision on taking the discount rests with the finance department, but the terms are negotiated in procurement and belong on the purchase order.
- Clean approval processes, mandatory fields for discount terms and functioning deadline tracking of discount periods are essential.

Definition: early payment discount

An early payment discount denotes a price reduction granted by the supplier that applies only on condition that the invoice amount is paid within the agreed discount period. The terms are usually stated on the invoice and in the terms and conditions, for example "3 per cent discount for payment within 14 days".

Distinction from bonuses and rebates

An early payment discount should not be confused with volume rebates, volume bonuses or annual discounts. Volume rebates apply regardless of the payment date, whereas the discount is linked to payment behaviour. An annual bonus is granted retrospectively on annual volumes and acts as a retroactive rebate; the discount takes effect directly at the payment date and immediately reduces the liquidity requirement.

Legal classification

According to the general view in case law, it is a remuneratory claim, i.e. consideration for early payment. The supplier is not obliged to grant a discount, and there is no automatic entitlement to it without an express agreement. If the invoice amount is paid late, or only after the discount period, even without a deduction, the reduction is in principle forfeited. Whether notification obligations or goodwill arrangements apply should be examined on a case-by-case basis.

Calculation and economic assessment

From the buyer's perspective, the discount is usually assessed as a return on the capital employed. The question is: is it worthwhile to pre-finance the invoice in order to receive the reduction?

Formula and typical magnitudes

The effective interest rate is frequently estimated using the formula $(\text{discount percentage} \times 360) \div (\text{payment term} - \text{discount period in days})$. With 2 per cent discount within 10 days and a 30-day payment term, this gives around 45 per cent p. a. In practice, common discount terms range from 1 to 3 per cent, usually with periods of 8 to 14 days. Even 1 per cent over a short period can mean a double-digit effective interest rate and thus exceed the return on equity of many investments.

Liquidity versus interest advantage

The effective interest rate is only one side of the coin. Drawing the discount ties up liquidity earlier and can disrupt supplier adjustments when payment peaks arise. A comparison with short-term financing costs and the planned liquidity line is sensible. In times of higher interest rates, the discount becomes more attractive for solvent buyers; with tight cash flow, however, forgoing the discount may be the right decision.

Early payment discount from the supplier's perspective

For suppliers, the discount is an instrument for rapid cash conversion and for reducing receivables risk. Anyone wishing to make their own liquidity planning more reliable can consider lower discount scales instead of drawing more expensive overdraft facilities. Buyers who understand their supplier's payment behaviour negotiate realistic terms and strengthen the partnership.

Negotiating and managing discount terms

Discount terms are negotiable and belong in the contract and purchase order documents. The better your own solvency and payment behaviour are evidenced, the stronger your negotiating position.

Negotiating levers in procurement

Key levers are a clean negotiation protocol, a documented award note and the link to volume or framework agreements. Buyers should actively incorporate the terms into tenders and framework agreements rather than letting the supplier unilaterally determine them on the invoice. Tiered models are also common: for example 2 per cent at 8 days, 1 per cent at 14 days and 0 per cent at 30 days. Procurement should segment terms, i.e. differentiate according to commodity group, supply criticality and the supplier's margin situation.

Anchoring in purchase order and invoice processes

To ensure the discount is not lost in practice, the terms must be captured in a structured way. Mandatory fields for discount percentage and discount period in the ordering system are useful, as is a check of whether the invoice matches the purchase order. Purchase order process optimisation and automatic account assignment reduce manual friction losses and ensure that discount periods are taken into account in the payment run in good time. Deadline tracking and dunning processes on the supplier's receivables management side support timely settlement.

Role of the finance department

The decision on whether to take the discount is usually made by the finance department, often jointly with the buyer. Clear internal rules are important: from what effective interest rate is the discount taken? Who approves payments with a deduction? How are complaints, debit notes or requests for additional documents that blow the deadline handled? A joint workflow avoids conflicts and prevents the discount from lapsing despite valid terms.

KPIs and reporting on early payment discount

Without key figures, the discount remains a side issue. Discount rate, realised reduction and the effective interest rate of the terms used become measurable.

Key performance indicators

Typical key figures are the discount utilisation rate (proportion of invoices where the discount was taken), the discount amount realised per period and the average effective interest rate of the terms taken. Also useful: the lost discount on invoices that contained terms but were paid too late or without a deduction, as well as the average duration between invoice receipt and payment. These figures feed into the reporting of procurement and the finance department.

Reporting practice

In practice, monthly reporting showing discount utilisation by commodity group and supplier has proven its worth. The figures can be readily linked to payment behaviour and the supplier scorecard. Those working in category governance use the figures to renegotiate terms per category. Supplementary risk analysis of supplier financing shows whether discount draws place a heavy burden on individual suppliers.

Risks and controls

Early payment discounts carry economic and process risks if deadlines, review processes or data quality fail. Controls should be preventive in approach.

Typical sources of error

Common errors: the invoice contains no discount terms although they were negotiated; the discount period expires before the invoice is approved; payment is made without a deduction because the accounts payable account does not automatically recognise the terms; the invoice is paid later due to open complaints or requests for documents and the discount lapses. Additional interest costs from unnecessary pre-financing are also possible if the portfolio of discount terms is not checked for effective interest rate.

Controls and internal processes

Effective controls: mandatory fields in the ordering system, automatic deadline monitoring, a four-eyes principle for payments with a deduction, and a documented process that interlinks invoice receipt, approval and payment run. Sanctions list screening and KYC in procurement when onboarding new suppliers are important, as the payment terms form part of the contractual relationship. The question of whether a discount is taken in the event of complaints about deviating performance should also be recorded in the negotiation protocol.

Tax and accounting notes

In accounting, the discount is typically treated as a reduction of revenue for the supplier or as a reduction of expense for the buyer. In practice, VAT is often calculated on the discounted amount; whether input tax must be adjusted if the discount is not taken depends on the individual case and should be examined from a tax perspective. These statements are general in nature and do not replace advice in individual cases.

Current developments: dynamic discounting and digital processes

Discounting is being digitalised and increasingly designed dynamically. New instruments combine classic discount terms with supply chain finance.

Dynamic discounting and supply chain finance

With dynamic discounting, the reduction adjusts to the actual payment date: the earlier payment is made, the higher the deduction. Such models can be combined with supply chain finance, in which a bank or financing partner pre-finances the supplier. For buyers, this creates a continuum between pure discounting and classic factoring or reverse factoring. Transparency about costs, posting logic and balance sheet effects on both sides is important.

Automation in the invoice workflow

Digital invoice workflows, OCR capture and automatic account assignment shorten the time between invoice receipt and approval. This is a prerequisite for being able to use short discount periods at all. The supplier onboarding process with D-U-N-S number (DUNS) and risk screening also makes it easier to store discount terms consistently in the master data. Purchase order process optimisation and the linking of purchase order, goods receipt and invoice reduce queries and defuse short deadlines.

Interest rate environment and negotiating logic

In phases of higher market interest rates, the return on taking the discount rises from the buyer's perspective, while suppliers come under pressure as liquidity is tied up. The negotiating logic shifts accordingly: suppliers demand larger reductions for early payment, and buyers examine whether they can exploit the advantage. Risk scenario planning helps to adapt the discount strategy to interest rate and economic cycles.

Typical metrics

Discount utilisation rate: > 80%

Proportion of invoices with terms where the discount was taken

Forfeited discount: < 2%

Proportion of potential discount lost through missed deadlines

Effective interest rate on discount terms: > 20% p. a.

Benchmark above which taking the discount is generally sensible

Lead time from invoice to payment: < 10 days

Prerequisite for being able to use short discount periods

Practical example

A medium-sized mechanical engineering company sourced sheet-metal cuttings from around 40 suppliers. Discount terms had partly been agreed verbally, did not appear on the purchase order and were lost in the payment run. Following a process review, four measures were implemented.

- Introduction of mandatory fields for discount percentage and discount period in the ordering system and updating of supplier master data.
- Linking of invoice receipt, goods receipt and approval, so that invoices with short discount periods enter the payment run with priority.
- Renegotiation of discount scales with the most important sheet-metal suppliers and documentation in the negotiation protocol.
- Monthly reporting on discount rate and forfeited discount to procurement and the finance department.

Conclusion

An early payment discount is more than a reduction on the invoice: it is a liquidity and negotiation instrument with a measurable effective interest effect that in practice often significantly exceeds short-term financing costs. What is decisive is the process anchoring: clear terms on the purchase order, mandatory fields, automatic deadline tracking and clean reporting. Anyone managing discounts systematically improves liquidity and earnings at the same time and creates a solid foundation for dynamic payment models. Forgoing the discount is economically sensible only in cases of tight cash flow or unfavourable terms.

Frequently asked questions

What does early payment discount (Skonto) mean in simple terms?

An early payment discount (Skonto) is a price reduction granted by a supplier if the invoice amount is paid within a short period. Typical terms are 1 to 3 per cent within 8 to 14 days. The deduction applies only if payment is made on time.

How high is the effective interest rate on an early payment discount?

The effective interest rate is approximated as $(\text{discount percentage} \times 360) \div (\text{payment term} - \text{discount period})$. With 2 per cent discount for payment within 10 days and a 30-day payment term, it comes to around 45 per cent p. a. In practice, the annualised effective interest effect usually lies between 15 and 60 per cent.

May a supplier refuse an early payment discount?

Yes, a supplier is not obliged to grant an early payment discount. Without an express agreement, there is no entitlement to the deduction. It is advisable to contractually fix the terms and include them on the purchase order.

What happens if the discount deadline is missed?

As a rule, the discount lapses and the full invoice amount becomes due. Some suppliers grant a reduction as a gesture of goodwill, but this is not enforceable. Good processes with deadline tracking largely prevent this loss in practice.

When is an early payment discount not worthwhile?

An early payment discount is not worthwhile if the effective interest rate is below your own financing costs, or if forgoing liquidity would be business-critical. It can also make sense to withhold the deduction when there are open complaints or unclear deliverables, until the matter is clarified.

How does an early payment discount differ from supplier credit?

Under supplier credit, i.e. a normal payment term, the buyer uses the supplier's liquidity free of charge. With an early payment discount, the buyer pays earlier and receives a price reduction in return. Both instruments can be combined, for example via graduated terms.