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What Financial Records Do You Need to Keep?

The IRS requires you to have written evidence to demonstrate that the statements on your income tax returns are true and accurate.

The rules for what kind of evidence you need to have include general rules and special rules for certain types of transactions.

You must keep business records related to all items of income and expense for any business or rental income reported on your federal income tax return.

You must be able to show evidence that: 1. The transaction actually occurred, 2. It was for the amount claimed, and 3. That it was for the business purpose claimed.

Income Records

You are required to report all income related to your business. Income records serve to prove that you have not over- or under-reported your income.

The following are examples of minimum required documents to prove **income items**:

- Checking and savings account statements
- Receipts from sales showing if the sale was paid in cash or “on account” (meaning the customer will pay later)
- Records showing amounts received from sales made “on account”
- Records of bad debts or amounts sold on account but never paid

Expense Records

You may, and in fact you *must* deduct expenses that are ordinary and **necessary and reasonable** for your business. Ordinary expenses are defined as “customary or usual” and “common or frequent” in the taxpayer’s business and businesses like the taxpayer’s. Necessary expenses are defined as being “appropriate and helpful for development of the business.”

To prove **expense items** you must be able to show evidence that: 1. The transaction actually occurred, 2. It was for the amount claimed, and 3. It was for the business purpose

claimed. Some expense items have additional special requirements. Examples of expense items with additional special requirements are: asset purchases, vehicle use, travel, meals, gifts, and events. Materials on each of these items are below.

At a minimum your supporting documents for business expenses should identify the payee, the amount paid, proof of payment, the date incurred, and if needed, include a description of the item purchased or service received that shows the amount was for a business expense.

You may need a combination of records to do this, including:

- Checking and savings account statements
- Credit card account statements
- Physical receipts
- Additional notations made on the receipts to explain how the purchase relates to the business

It is a good practice to make a note on a receipt as soon as you can, but most receipts fade out within a few months. The best practice is to take a picture of the receipt - with the note on it - or make a copy of the receipt.

Exceptions to General Records Requirements:

You have the right to take deductions based on a "reasonable reconstruction of expenditures" if your original records are lost due to circumstances beyond your control such as theft, fire or flood.

If records are incomplete due to the taxpayer's own negligence but the taxpayer can demonstrate that some expenses were actually incurred the taxpayer is entitled to some amount of deduction, but the amount will be limited to the smallest amount reasonable.

This resource is derived from materials developed by the University of Arkansas School of Law Agricultural Tax Training as part of the Agricultural Financial, Tax and Asset Protection (AgFTAP) partnership with the University of Arkansas Southern Risk Management Education Center and others.