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How Do Your Records Need to be Organized?

If you just keep bank and credit card statements and receipts, you will not have a system for organizing that information in a way that is required to report meaningful summary information on your tax return, so you also need a system for organizing your individual transactions into meaningful categories of income and expense for each year.

You are required to use a method that **clearly and accurately** reflects your gross income and expenses and allows you to report asset purchase and sales separately from other business transactions.

There is no specific requirement to use a particular method to keep your records, and summarize your individual transactions into the groupings required on the IRS forms, but the method you use must be appropriate for the size of your operation.

Minimal organization is ok for a very small operation in its first year of operations. Here are two common methods for small businesses in their first year of operations:

- Keep sales and purchase receipts, sort them into groups corresponding to categories on the tax return. You can give these receipts to a tax preparer or, total each grouping and report that number if you prepare your own return or use a computer program to help you prepare your own return. Note that if you give receipts to a tax preparer to total they may make mistakes and they will charge you extra.
- Use paper or a spreadsheet program to create a register showing date, payee or payor, amount and purpose of each transaction, and code each transaction to an appropriate category on the tax return. You can total each grouping yourself if you prepare your own return.

Note that these methods are slow and will not be clear and accurate if there are lots of transactions. If you do not have a receipt for something you will not include it and your returns will be inaccurate. There is no built-in way for you to verify that you have correctly recorded each transaction even if you use your bank statement or credit card statement to guide you.

The standard best practice is to use a double-entry bookkeeping system. Double-entry bookkeeping is not required for very small businesses, but it is required for larger and

more complex businesses, and it is the only way to ensure that your records are complete and accurate and easily produce usable reports. Double-entry bookkeeping means that each transaction is recorded according to well-established (literally centuries old) rules, and there are standard methods for verifying completeness and accuracy.

To implement a double-entry bookkeeping system for your business you can:

- Use an online software program such as Quickbooks and learn as you go
- Hire a trained bookkeeper to do all of your bookkeeping
- Use an online software program such as Quickbooks and hire a trained bookkeeper to help you set it up and help you learn the best ways to use the program and manage your documents

For more help setting up a double-entry bookkeeping system see the resources of the FarmLink Bookkeeping Toolshed, particularly the FarmLink Model Chart of Accounts.

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.