

University of Missouri Extension

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Home-Based Business — Keeping Records

Department of Consumer and Family Economics

A good recordkeeping system is essential to operating a successful home-based business. Would you believe you could save more than \$112 an hour by keeping good records? Suppose you had a \$20 business expense that you forgot to record. This oversight, in effect, raises your business's net income by \$20. Using 1988 figures, overstating net income by \$20 causes

- Your social security tax to go up \$2.60 (\$20 times 13.01 percent for a self-employed person)
- Your federal income tax to go up \$5.60 (assuming you were in the 28 percent federal income tax bracket)
- Your state income taxes to go up \$1.20 (assuming a 6 percent state tax).

The \$20 expense not recorded will cost you \$9.40 more social security, federal income tax, and state income tax. If you had recorded this expense in five minutes or 1/12 of an hour, you would have saved \$9.40 in 1/12 of an hour or \$112.80 per hour. That is a pretty good use of your time.

Although this example may at first glance seem complicated, the \$20 forgotten expense would not happen with even the simplest record keeping system.

In addition to avoiding costly errors, good records tell you if you are making a profit or losing money, provide you with accurate tax information and give you the information needed to see if and where improvements can be made.

The following are guides to help you develop a simple set of records for your business. It is important that you change your procedures to fit your particular needs as your business expands or when you want your records to tell you more about your business.

Start keeping records

If you are already in business and not keeping records, start immediately. After you get your system set up, you might want to work backwards to the first of the year so that you have as complete information as possible for your year-end records.

If you are starting a new business, you will need an estimate of income and expenses to secure financing if needed; or, if your own resources are adequate, you will still want to know how you are doing financially. To determine profitability, you'll need to figure your start-up costs and your operating costs. Start-up costs are the one-time expenses necessary to starting your business, such as equipment expected to last a long time. Operating costs are those that keep recurring, such as purchasing materials needed for making the product.

Once your recordkeeping system is set up, record all transactions promptly. Set aside a certain time each day, or at least each week, to update income, expenses and other items of importance. It is also a good idea to establish a definite time each month to pay bills, reconcile the bank statement and do other monthly tasks.

Records are much easier to maintain if they are easily accessible. Provide yourself with a space to use as an "office." It need not be large, but should have good lighting, a comfortable chair, a surface for writing and some storage space for supplies and records. An inexpensive box or cabinet for filing and some file folders would be adequate in most cases. Also have a place to keep incoming mail, and be sure to have a wastebasket handy.

Your business "office" might be a part of your home "office" where bills are paid, letters written and incoming mail sorted. The other option is for the transactions of the business to be in a separate location away from the family business center.

Figure out a system

The key to an effective, efficient bookkeeping system is to get it set up right. It should be adequate to meet your current needs and be expandable as your business grows. You do not need an elaborate system for a small business, but you must have a system.

The simplest system is to just use your business checkbook. It is recommended that your business account be separate from your personal account. Record on each check and deposit slip the details of the transaction. All transactions must go through the checkbook and you need to reconcile it monthly. At the end of the year, you can summarize your profit picture. This system is suitable only if you have a few transactions.

A more complete system uses the checkbook plus a cash receipts journal and a cash disbursements journal. Simple journals or ledger paper that fits into a notebook are available in most stationery departments and office supply stores. All transactions are recorded in one of the journals. The cash receipts journal has columns for various categories of receipts with a line for each receipt, including date, source of cash, and total amount. The column categories may be types of merchandise, types of service, place of sale or whatever classification makes sense in your business. It is helpful to record sales tax in a separate column.

The cash disbursements journal has columns for various categories of expenditures with a line for each expenditure, including date, check number, payee, description of expense, and total amount. The column categories may be merchandise for resale, supplies, interest, utilities, loan payments, salaries or whatever classifications make sense in your business.

All columns in both the cash receipts and cash disbursements journal should be totaled each month with year-to-date totals after each month. You can then quickly determine your financial status at the end of any month and make your annual income statement.

In addition to entering all transactions into cash receipts or cash disbursement, you need to keep all receipts, invoices and order forms. You may want to put all of them for one month in one envelope. Or, keep all receipts in one envelope or file folder and all invoices in another. The important thing is to decide how you're going to do it and then keep consistent.

Place these in the file storage in your business "office." Keep your filing system simple. Decide what you want to file and set up a system that makes sense to you. Label your folders so they can be easily read. If two or more people are in business together, it usually works best if one person is in charge of bookkeeping. The other should, however, be familiar enough with the system to be able to take over if necessary.

Keep all financial records for at least six years after tax returns are filed.

If your business requires, or if you decide to use a more elaborate recordkeeping system, you should consider consulting an accountant. An accountant can help you set up a system specifically tailored to your needs. You might also consider taking a bookkeeping or accounting class through adult education opportunities in your community.

Records other than financial records that would be helpful to you are an inventory of supplies and equipment, mailing lists and personal time log. It is up to you to decide what information is important to have and to keep.

Checklist for good records

Open a business checking account

Don't use your personal checking account for your business. The cost of another account is minimal compared to the

confusion of business matters in your personal account.

Pay all bills by check

On each check, note what was purchased with that check. This is your record of having paid bills and enables analysis of expenditures.

Use petty cash sparingly

Only when absolutely necessary should you make payments from petty cash and then be sure you have a receipt including the purpose of each expenditure. Then write a check to petty cash to keep the checkbook complete.

Record all sales

Use sales tickets, duplicate receipts, copies of invoices, cash register tape or some other system that itemizes each sale. This enables analysis of sales and provides a record of who has paid or not paid.

Endorse all checks immediately

Endorse checks "for deposit only" to your account in your bank.

Deposit receipts often

Don't keep cash or checks around your place of business. They invite theft, they can get lost and the money should be put to work for you immediately.

Label bank deposit slips completely

They provide a good record of sources of income and back up sales records.

Balance bank account monthly

Do it when the statements come from the bank.

Inventory all items regularly

Count all items in inventory and include the purchase cost of each item. At the very least, take inventory once a year. A good business practice is to take inventory twice a year and a better practice is quarterly inventory.

Practice good record hygiene

Keep clean, neat and regular records.

It would be unusual if you set up a perfect record keeping system on your first try. Modify these suggestions for your system if you currently are keeping some records but feel they are not adequate. Incorporate the ideas that apply to your situation if you are beginning a record keeping system. But do it now.

References

- Hammond, David H. and Hergatt, Jane Ann. *Record Keeping for Profit*, Cooperative Extension Service, Iowa State University, Pm-1149e, April 1984.
- *Marketing Crafts*, North Central Regional Extension Publication 177, January 1982.

Related MU Extension publications

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