



This presentation is part of an educational modular program designed to provide new and beginning farmers and ranchers with relevant information to initiate, improve and run their agricultural operations



United States Department of Agriculture
National Institute of Food and Agriculture

**This program is funded by the
Beginning Farmer and Rancher
Development Program (BFRDP)**

USDA-NIFA-BFRDP 2010-03143



Financial Record Keeping

WHY AND HOW TO KEEP FINANCIAL RECORDS



Financial record keeping



- For years farmers have been reporting financial information on a variety of forms for various reasons:
 - For example for taxes, for loan management, etc.
- However, record keeping is also a very important tool for making informed decisions about the everyday workings of the farm and to make plans for the future



Objectives



In this presentation we will talk about the importance of keeping a good record system and compare different systems for keeping records

Then we will compare some cash vs. accrual accounting, and finally we will review some recommendations of things to do (and not to do) about farm record keeping



Why keep records?



1. Proof

- The IRS can ask for proof of income, expense and inventory items reported on tax returns

2. Decision-aids

- Farm managers use records to construct balance sheets, balance flow and income statements and other financial aids for making more informed decisions in areas such as machinery purchases, adding or deleting enterprises, size expansion and others



Why keep records?



3. Institutional requirements

- Some lending institutions and government bodies require financial and/or production records be maintained over a number of year.
- For example, the government farm program requires certain production and acreage records be reported and maintained. Also, planning for conservation compliance and other aspects of soil and water management essentially become historical records over time

4. Environmental regulations

- Increasingly, farm owners are being asked to keep records about chemical use, livestock waste applications and irrigation water use on their farms



Why keep records



- Plus,

1. Lenders and leasers may require up-to-date financial records as a condition of an operating or getting a loan or lease
2. It will help you evaluate over time the progress and changes of your farm

Plus, it is always a good business practice!



What kind of records do I need to keep?



The minimum list of records are:

- 1. Inventory of assets and liabilities**
- 2. Transaction journal listing income and expenses**
- 3. Copies of tax forms filed**
- 4. Employment records**



Financial records needed

A reliable financial record keeping system needs to have:

- The minimum requirements, plus:
 1. **Balance sheet**
 2. **Income statement**
 3. **Cash flow statement**
 4. **Enterprise budgets**



These 4 requirements should be timely, accurate and complete

Financial statements

Balance sheet

- Presents a snapshot of the state of the business at one point in time
- It must be done at the beginning of each financial period
- The balance sheet shows 3 things:
 - Assets
 - Liabilities
 - Net worth



Financial statements

Income statement:

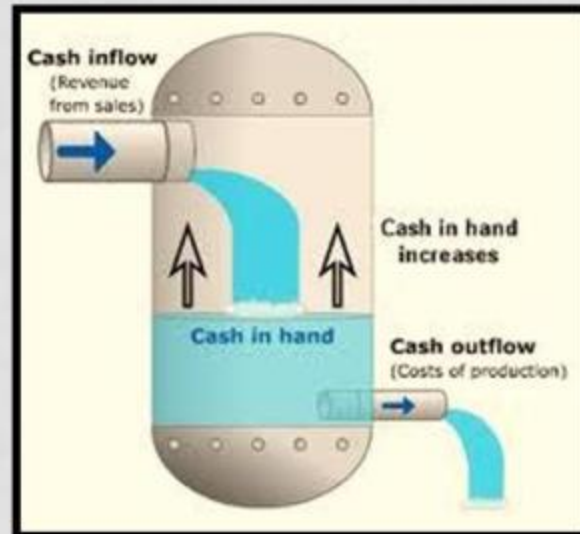
- It shows how the business performed in the period between two different times (such as, beginning and end of a season, beginning and end of the year)
- It uses the information from 2 different balance sheets filled at different times of the year
- The income statement shows 3 things:
 - Outputs
 - Costs
 - incomes



Financial statements

Cash flow statement:

- The cash flow **plans the future inflows and outflows of cash** in the business over a specific time period
- It also shows cash in the business at the start of the period and cash left in the business at the end of the period



Financial statements

Enterprise budgets:

- Budgeting is trying to **plan future expenditures** and match these in some ways with future sales and other dollar inflows
- It is one of the most important functions in running a business

No one knows the future, so budgeting results will usually be inaccurate

But it is better to have a bad plan, than to have no plan



Enterprise Budgets



- Enterprise budgets show the estimated returns per enterprise based on the use of a production system, estimated production, and estimated production costs
- Each budget needs to be made for a certain production period for each type of crop, livestock and other goods produced on the farm

These budgets are typically done at the start of each production period for each of the farm's enterprises



Enterprise Budgets

Each enterprise budget must include:

1. Estimated production for each type of merchandise
 - For crops it is an estimated per acre yield multiplied by an estimated selling price
 - For livestock it is an estimated per head yield multiplied by an estimated selling price
2. Operating expenses
 - Such as feed, seed, fertilizers, etc.
 - These are the costs of inputs



Enterprise budgets



3. Fixed costs

- Costs associated with capital assets such as land, machinery, and buildings

4. Total costs

- Combining fixed costs and operating expenses

5. Net Returns over total costs

- Estimated production minus total costs



Where to find Enterprise Budgets and Financial Statements?

- Arkansas Extension has available:
 - Crop and livestock planning budgets
 - Herd inventory record books
- Neighboring states' Extension Services have available:
 - Balance sheet (OK and KS)
 - Cash flow materials (OK and KS)
 - Income statement (OK and KS)
 - Enterprise budgets for non-traditional crops (OK, MO, and KS)



How long should I keep
financial records?

How long should you keep your financial records?



What records to keep and how long

Cancelled checks	3 to 6 years
Investment records	6 years
Loan agreements	Until updated
Receipts for large purchases	Until item is sold
Service contracts and warranties	Until item is sold
Tax returns	6 years from filing date

How do you keep your records?



CASH VS. ACCRUAL ACCOUNTING

How to keep your records?



- One of the first decisions that you need to make is what type of accounting system you will use, that is, how are you going to keep your records?
- In general, there are 2 accounting systems
 - Cash accounting system
 - Accrual accounting system

Cash vs. accrual accounting

Cash vs. accrual accounting



OR



Cash vs. Accrual Accounting



Cash accounting systems

- Expense recorded when the goods and services are actually paid for
- Income recorded when the money is in your possession
- System can not be used when you are selling products on credit and bill buyer at a later date
- System used by many agricultural producers

Example:

You purchase a new printer on credit in May and pay \$1,000 for it in July. Using the cash method, you would record a \$1,000 payment for the month of July, when the money is actually paid.

Cash vs. Accrual Accounting



Accrual accounting systems

- Expenses are recorded when the expense is incurred
- Attempts to match expenses with generated revenue
- Revenue is recorded when the project is completed or the product shipped, we don't care about when received payment
- Generally, used by larger businesses that sell on credit

Example:

You purchase a new printer on credit in May and pay \$1,000 for it in July. Using the cash method, you would record a \$1,000 payment for the month of May, when you become obligated to pay for it

Picking an Accounting system



- Each system requires different level of record keeping by the user
- You will want to pick system that works for your farm. But once you pick a system you should stick to it!



Record keeping Systems



- In general, the law does not require any specific kind of records, so you can choose to keep your records with the cash or accrual system depending on your own business
 - Small businesses usually can operate with a simple record keeping system
 - You want to pick a system that you feel comfortable using

Keep a complete and separate set of records for each business in which you are involved

Record keeping systems

- The next decision that you need to make is how are you going to maintain your records:



vs.



Computer-based systems



The most important use of a computer on the farm is for



Computer-based systems

- **Advantages of computerized records**

- Easier storage and access to files
- There are many software packages available to help you keep, organize and analyze your financial records
 - Immediate availability of key reports
 - Improved planning and budgeting capabilities
 - Easier detection and elimination of unprofitable enterprises



Computer-based systems



Computer-based systems:

- Increasingly affordable
 - Some software for small business start at under \$100
 - There are many options so ask around to find a system that works for your needs

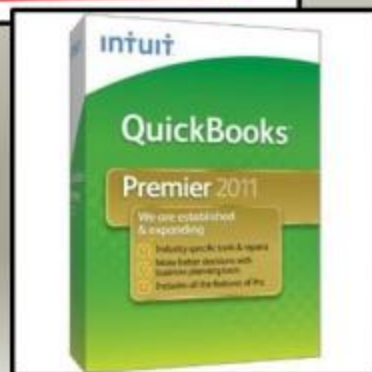
Pros of a computer-based system:

- Eliminates math errors
- Break expenses and revenues down by category
- Interface with computer-based tax software easily
- Easily creates:
 - Cash-flow statements
 - Profit and loss statements
 - Graphs and charts



Examples of available Commercial software products

There are many different software packages available, but these are some of the most commonly used



Commercial software products



Quicken

- Cash accounting program
- User friendly
- Inexpensive and widely available (\$20 to \$70 depending on the version you purchase)
- Can be easily adopted to wide variety of agricultural businesses

www.agecon.okstate.edu/quicken/

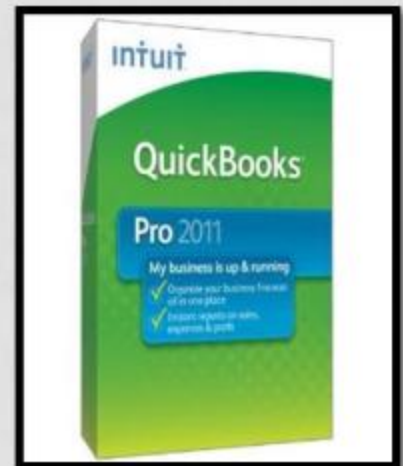


Commercial software products



QuickBooks

- Accrual accounting program
- Double entry accounting
- Handles payroll
- Can be easily adopted to wide variety of agricultural businesses
- Costs between \$190 to \$250 depending on version purchased



Commercial software products

- **Farm Works**

- Software designed specifically for agriculture
- Can integrate the field level and whole farm records

<http://www.farmworks.com/>

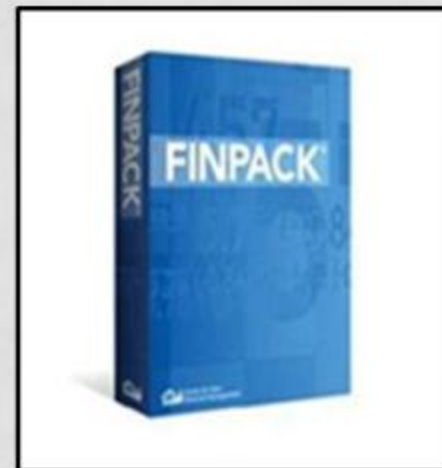


Commercial software products



FINPACK

- System designed specifically for agriculture
 - Excellent tool for developing
 - Balance sheets
 - Budgets
 - Cash-flows
 - Provides key financial measures
 - Costs \$99/annually or \$395 for lifetime subscription
- <http://www.cffm.umn.edu/FINPACK/>



Record keeping alternatives



There are people that like to keep physical and handwritten records of everything

- This is a suitable option for small and beginning operations

"Farm account books"

- Good for small and part-time farmers
- Provides a record of all basic information
- Available through:
 - Cooperative Extension Services
 - Ag Lenders (USDA-FAS)
 - Farm Management firms
 - Several universities have forms and guidelines available to start your own recording system



How to get started



1. Identify your needs

- How big and complex is your business?
- Can you keep up with handwritten financial records or do you need a computer program to help with record keeping?

2. Commit financially to what you need

- If you go with financial software, buy the one that works for your business
- If you don't have the time to keep up, be willing to pay someone to do it

3. Commit the time

- Don't put it off till next year, always set aside the necessary time. It is an important part of your business!!

Do's and Don'ts for Farm Records



- **DO:**
 - Keep records ALWAYS AND OFTEN!
 - Keep them organized
 - Put someone in charge
 - Preferably someone who likes to do it
 - Provide the right tools
 - Provide dedicated time, space and environment
 - If you don't like it or don't want to do it, maybe hiring somebody to do this part of the job is a good investment



Do's and Don'ts for Farm Records

- **Do:**

- Keep records updated
- Keep business and personal accounts separated
- Consider record-keeping a vital part of your business



Do's and Don'ts for Farm Records



- **DON'T**

- Wait until next season or next year to start recordkeeping
 - You will forget things (and it is a real pain)
- Act like record keeping isn't a REAL job. Often, the success of the business relies on studying your records
- Play with or change balance sheet values
- Ignore balance sheet trends



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Want more information?



- Setting up a record keeping system
 - Ohio State University
 - <http://ohioline.osu.edu/cd-fact/ii52.html>
- Keeping your business on track, part II.
 - University of Maine Cooperative Extension
 - <http://www.umext.maine.edu/onlinepubs/htmpubs/3003.htm>
- Developing a set of financial statements
 - Small Business Notes
 - <http://www.smallbusinessnotes.com/operating/ginmgmt/financialstmts/gettingstarted.html>
- Basic rules for Financials
 - Business Owner's Toolkit
 - http://www.toolkit.com/small_business_buide/sbg.aspx?nid=P06_7025

Want more information?



- Financial Statements
 - Agricultural Marketing Resource Center
 - http://www.agmrc.org/business_development/operating_a_business/finance/financial_statements.cfm
- Cash-flow projection for operating loan determination
 - Kansas State University Extension
 - <http://www.oznet.ksu.edu/library/agec2/MF275.pdf>
- Borrowing in a risky environment
 - Texas A & M University Extension
 - <http://trmep.tamu.edu/cg/factsheets/rm5-9.pdf>
- Cash management.
 - Small Business Notes
 - <http://www.smallbusinessnotes.com/operating/finmgmt/cashmanagement.html>
- Quicken® for Farm and Ranch Financial Records
 - Oklahoma Cooperative Extension Service
 - <http://osufacts.okstate.edu/docushare/dsweb/Get/Document-1799/CR-324.pdf>

Want more information?



- Developing a cash flow plan
 - Oklahoma Cooperative Extension Service
 - <http://osufacts.okstate.edu/docushare/dsweb/Get/Document-1782/AGEC-751web.pdf>
- Developing a balance sheet
 - Oklahoma Cooperative Extension Service
 - <http://osufacts.okstate.edu/docushare/dsweb/Get/Document-1805/AGEC-752web.pdf>
- Developing an Income statement
 - Oklahoma Cooperative Extension Service
 - <http://osufacts.okstate.edu/docushare/dsweb/Get/Document-1789/AGEC-753web.pdf>
- Schedules of Assets
 - Oklahoma Cooperative Extension Service
 - <http://osufacts.okstate.edu/docushare/dsweb/Get/Document-1799/AGEC-791web.pdf>

Want more information?



- Liabilities schedule
 - Oklahoma Cooperative Extension Service
 - <http://osufacts.okstate.edu/docushare/dsweb/Get/Document-1710/AGEC-792web.pdf>
- Using Enterprise Budgets in Farm Financial Planning
 - Oklahoma Cooperative Extension Service
 - <http://pods.dasnr.okstate.edu/docushare/dsweb/Get/Document-1658/AGEC-243web.pdf>
- Arkansas Production Budgets
 - Arkansas Extension Service
 - http://www.uaex.edu/depts/ag_economics/farm_management.htm