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ITI STRATEGIES, INC

Investment, Tax and Insurance Planners

Record Keeping for Your Own Business

Record Keeping for Your Own Business

Keeping good business records will not only help you stay in business but may also help you increase profits. Your business records let you analyze where your business is and where it's going. They point out potential trouble spots and serve as a guide to where you want your business to be.

Your ideal office manager: criteria for record-keeping systems

Like a valued office manager, your record-keeping system should have good work habits. It should be easy to use. If it's too complicated, it might be neglected, defeating its purpose. It should reflect information accurately, completely, and consistently throughout all of its applications, and it should do so in a timely fashion; you don't want to base important business decisions on partial or outdated information. Finally, it should present results in an easily understandable manner. If you can't comprehend the data that your record-keeping system provides, you might ignore their implications.

Some commercial record-keeping systems are generic in format and applicable to many types of business. Others are designed for specific types of business operations (e.g., retail sales and manufacturing). Most generally will offer the ability to summarize your business activity with appropriate periodic financial reports. Many websites allow you to see a demonstration version of the software before you purchase the software.

You can decide whether to keep your own books or hire someone to do it for you. Your decision depends in part on how much time and ability you have for the task. You can hire a company that specializes in payroll services to handle the paperwork and withholdings for your employees. Most small-business advisors suggest that you have an accountant prepare your tax returns and year-end statements. In many cases, an accountant can also offer advice on various aspects of financial management, such as cash flow analysis, borrowing for the business, tax considerations, and suggestions for which software to buy for record keeping. Whichever way you go, you should stay involved in the record-keeping process. After all, it's your business, and ultimately you are responsible for its success or failure.

What your records should do for you

Like a medical diagnostic tool, your records help you assess the health of your business.

- Bank statements measure cash on hand, and accounts receivable predict future income. Together, these records help determine cash flow requirements and may point to a need for short-term borrowing.
 - In addition to providing income tax information to your employees, payroll records help you determine the appropriateness of your pricing and customer billing policies.
 - If your business keeps merchandise on hand, your records help you manage the size of your inventory, thus avoiding the loss of profits from obsolescence, deterioration, or simply being out of stock.
 - Expense records help you plan to meet obligations in a timely fashion. They also help you assess whether the income generated supports the expense involved.
 - Statements of income, or profit and loss statements, help pinpoint unprofitable departments, products, or services, alerting you to make changes or eliminations if necessary.
 - The balance sheet captures the condition of your business at a given moment in time, allowing you to measure its reality against either your own budget projections or similar businesses.
- **Be prepared: the taxman cometh**
- One of the most important functions of business records is to prepare you (or your accountant) for filing tax returns for the business. Thus, you may want to set up a record-keeping system that captures information in a way that matches the demands of the IRS. If you are a sole proprietor, you'll want to familiarize yourself with the requirements for completing Form 1040, Schedule C.

- Here are some tax considerations to remember in relation to your record-keeping system design (for more information, see IRS Publication 334, "Tax Guide for Small Business"):
- If your small business is one that carries no inventory, then you can generally use the cash method of accounting.
- If you produce, purchase, or sell merchandise, you typically must keep an inventory and use the accrual method of accounting. However, there are exceptions to this rule if you are a "qualifying taxpayer" or a "qualifying small business taxpayer." You are a qualifying taxpayer if your average annual gross receipts are \$1 million or less and your business is not a tax shelter. You are a qualifying small business taxpayer if: your average annual gross receipts are less than \$10 million; you are not prohibited from using the cash method as defined by Section 448 of the Internal Revenue Code; and your business is an eligible business as defined in IRS Publication 538.
- The business-related portion of deductible car or truck expenses may be the actual expenses incurred (including gas, oil, tires, repairs, insurance, depreciation, and rent or lease payments), or you may elect to take the standard mileage rate (53.5 cents per mile for 2017, down from 54 cents per mile for 2016).
- Depreciation may be taken on property that is used in the business or held to produce income, provided it has "substantial" and "determinable" useful life. This means that it has a life beyond the year in which it was purchased but will also become obsolete or wear out over time. Examples include business cars, computers, and office furniture.
- Through 2017, an additional first-year "bonus" depreciation deduction is available, equal to 50% of the adjusted basis of qualified property placed in service during the year. The deduction amount decreases to 40% in 2018 and 30% in 2019. The basis of the property and the regular depreciation allowances in the year the property is placed in service and later years are adjusted accordingly. Alternatively, instead of claiming the bonus depreciation, companies may elect to accelerate alternative minimum tax credits.
- Some businesses may elect under IRC Section 179 to expense the cost of qualifying property purchased and put into use during a designated year, rather than to recover such costs through depreciation deductions. The limit is \$500,000, with a phase-out that starts when purchases exceed \$2,000,000. (Note that since 2016, the dollar limit and phaseout threshold have been indexed for inflation. In 2017, the limit is \$510,000 and the phaseout threshold rises to \$2,030,000.)
- You may deduct any contributions to employee benefit plans (such as health insurance plans and other fringe benefits) or contributions to pension or profit-sharing plans that are for the benefit of employees.
- You may deduct real estate or personal property taxes on business assets, Social Security and Medicaid taxes paid to match required withholdings on employee wages, state disability and federal and state unemployment taxes paid. Sales tax should be treated as part of the cost of goods or merchandise purchased.
- Depending on whether you use your home or other real estate for business purposes, you may deduct some or all of any mortgage interest paid, as well as some or all of the maintenance and repair expenses associated with the property.
- You may deduct the cost of business supplies purchased during the tax year.
- You may deduct the cost of utilities associated with business use.
- Also, if you have a home office used exclusively for business purposes, you may be able to take advantage of a simplified way to calculate the home office deduction. Under this method, instead of determining and allocating actual expenses such as mortgage interest and utilities, you would simply multiply the square footage of the office by \$5.00. The maximum allowed is \$1,500 (or 300 square feet). For more information on this deduction, see IRS Publication 587, "Business Use of Your Home."
- You can deduct professional fees, such as those paid to your accountant.
- You may deduct 50 percent of meal and entertainment expenses directly associated with the conduct of your business. You may be able to deduct the full amount of other travel-related expenses.

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- Remember to save any records and underlying documentation, such as invoices or receipts, relevant to your tax return for at least three years. Ask your accountant how long he or she suggests keeping the documentation.

- **Managing your business records**

- Records management is vital to any business. You should have a good system in place that will ensure that both your paper (physical) records and your electronic or digital records are retained as long as they need to be. Make sure your records are easily identifiable and accessible, and keep them well-organized. Shred (and recycle) paper records that you do not need or no longer need. Keep your electronic records safe and secure by adding a firewall to your computer and using software that provides adequate security. Back up your computer regularly using a CD, external hard drive, or an online remote back-up service (i.e., in the "cloud"), and be sure to use logins and passwords that are secure. Dispose of e-records carefully.

The opinions voiced in this material are for general information only and are not intended to provide specific advice or recommendations for any individual. To determine which investment(s) may be appropriate for you, consult your financial advisor prior to investing. All performance referenced is historical and is no guarantee of future results. All indices are unmanaged and cannot be invested into directly.

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