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**Penn State  
FARM AND DAIRY  
Business Seminar of the Week**

**The Whys And Hows Of Setting  
Up A Good Farm Record System**

**BY VIRGIL E. CROWLEY**  
Professor of Farm Management

Since many of you have recently gone through the process of filing your income tax returns it probably isn't necessary to remind you how important records are.



This is especially true if you have just discovered that your record system is not as complete as you thought it was.

While everyone recognizes how important records are at tax time, too many people keep only the records that are required for filing a tax return. Unfortunately many people still believe that the only use of farm records is for tax purposes. Of course that isn't the case, there are many other uses for farm records.

If your farm record system isn't meeting your needs or if you are keeping your records in a shoe box it isn't too late to set up a good

farm record system and really keep track of what happens on the farm in 1987. While I have been using the term farm records I should point out that I am using that term to refer to both the financial and production aspects of the farm business. A more accurate description would be to call it a farm account and record system.

If you are just setting up a record system or are planning to improve on the one you now have, your first step is to select the accounting method you want to use. There are two principal accounting methods in use and they are the cash and the accrual method. There are major differences between the two methods.

The cash method does not require the use of inventories and entries are made in the cash receipts and cash expense sections of the record book only when cash is actually received or paid out. The accrual system requires beginning and ending inventories and a purchase or sale is recorded

in the income or expense sections of the record book at the time the transaction takes place even if no cash is received or paid out.

Many farmers use what is called a combination method, that is they use the cash method of accounting, but they also use inventories and keep a credit account. This permits them to determine net farm income with the same accuracy as with the accrual method and to use the cash method for tax filing.

Regardless of which accounting method you select your second step is to decide if you are going to do your own recordkeeping or hire a professional recordkeeping service. Many farmers would find it to be a worthwhile investment to hire the services of a professional. If you hire a professional recordkeeping service they will supply the account book. If you keep your own records you will have to obtain a record book. A good place to obtain one is your local county Cooperative Extension Service office. Other possible sources of account books would be your farm supply dealer or your bank.

The foundation of any good record system is the inventory. Once you have selected an account book the next step is to take a complete inventory. Part of this will have already been done and is found in the depreciation schedule listing those depreciable items of machinery, equipment and buildings you have. A complete inventory not only includes all depreciable items, it must also include the farmland and the operator's home (for sole proprietorships). Since a complete inventory includes all assets of the farm business it also includes all feeds on hand and all farm supplies, plus any grain and/or forages being held for sale.

Accurately accounting for the

amounts of feed on hand when inventory is taken is one of the problems encountered. For example, how many bushels of ear corn are in the cribs, how many tons of silage and haylage are in the silos? How many tons of hay are in the stored bales, etc., in addition to determining the quantities of feed and supplies on hand?

Taking an inventory is not an easy task, and it is especially difficult the first time you do it. There are three basic problems associated with the inventory, and these problems may help explain why a limited number of farmers take a complete inventory annually.

The first problem is that taking inventory is time consuming and demands careful attention to detail to insure accuracy.

The second problem is determining the actual physical quantities of grain, hay silage and farm supplies on hand. Silage and/or haylage amounts stored in silos must be estimated as does the grain in bins and the ear corn in cribs. Often the amounts of some of the purchased farm supplies must also be estimated. For example, how many gallons of herbicide remain in the 50-gallon barrel that has been partially used.

A third problem is placing values on the items in the inventory. This is most difficult for some of the major items in the inventory such as land and raised livestock. Also how do you deal with the prices of grain and hay in the beginning and ending inventories. This is a critical question when change in inventory is used to calculate net farm income as with the accrual accounting method; or the combination cash and accrual method. This is because the change in beginning and ending inventories

is calculated on the basis of dollar values for nondepreciable items such as feeder livestock, raised dairy livestock, raised feeds and purchased farm supplies.

For example, suppose on Jan. 1, 1986 a farmer had 10,000 bushels of shelled corn in inventory which had a market value at the farm of \$2.65 per bushel, an inventory value of \$26,500. Now that same farmer has 10,000 bushels of shelled corn in inventory on Dec. 31, 1986 only now the market value is \$1.35 per bushel and the inventory value is \$13,500. If there were no other changes in inventory values this farmer has lost \$13,000 in inventory.

To further complicate the question of evaluating inventory suppose this same farmer has 100 raised dairy cows that are valued at \$1,000 per head on Jan. 1, 1986 and that on Dec. 31, 1986 those cows are worth \$1,100 per head. Does the farmer reflect this \$10,000 increase in value as income or are values for the dairy cows kept constant. Also what about land values which also may change from the beginning of the year to the end.

A convincing argument could be made for adjusting the values of the cows and the land to market values for both the beginning and the end of the year. However valuing dairy cows and land is quite different from valuing corn which has an established market where prices are given daily, based on established standard measures of grain quality. The values of the dairy cows and land are usually estimated values which are not actually established until the cows and/or the land are actually sold. In the final analysis the value of land and cattle is determined by the price that a

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