

Information Pamphlet



**A GUIDE TO
KEEPING BUSINESS RECORDS**

Inland Revenue Department,
Hong Kong

A GUIDE TO
KEEPING BUSINESS RECORDS

This pamphlet is issued for the general information as a introduction to the record keeping requirements of the Inland Revenue Ordinance in Hong Kong. It is not a legal document and is intended only as a guide to the law. Being a guide, it can only cover the subject very broadly. Further details may be obtained from the relevant legislation or from this Department.

Anthony AU-YEUNG
Commissioner of Inland Revenue

August 1995

CONTENTS

PART ONE - GENERAL

Introduction	1
Why keep records?	1
Some Ideas for record keeping	2
Retention of your records	2
Records that must be kept by all businesses	3
Additional records - businesses dealing in goods	3
Additional records - businesses providing services	4
How to keep your records	5
- The paper based method	5
- The computer method	5

PART TWO - BANKING RECORDS

Bank accounts	7
Cheque books	7
Bank deposits	7
Bank statements	8
Cash book	8

PART THREE - RECORDS OF INCOME

Cash register tapes	10
Receipts	10
Invoices issued	11
Other methods for recording cash sales	11
- Cash sales transaction record	11
- Counting system	12
- Calculator with tape	12
Stock taken for private purposes	12
Returned sales	12

PART FOUR - RECORDS OF PURCHASES AND EXPENSES

Recording purchases	13
Cash purchases	13
Receipts obtained	14
Credit card purchases	14
Invoices	15
Recording business expenses	15
Log books	16
Diaries	16
Petty cash system	16

PART FIVE - KEEPING RECORDS OF YOUR ASSETS

Acquisition of assets	17
Fixed asset register	18

PART SIX -CASH RECEIVED AND EXPENDED

Need to record all money received and expended	19
--	----

PART SEVEN - END OF THE ACCOUNTING PERIOD

Stocktake	20
What is trading stock?	20
Valuation of trading stock	20
List of debtors and creditors	21
Depreciation	22

PART ONE - GENERAL

Introduction

This Information Pamphlet is designed primarily to assist small businesses in preparing and keeping their records. The guidelines explain the minimum records required to be kept to comply with the Inland Revenue Ordinance (IRO). After reading these guidelines you will be in a better position to gauge the nature of the records you need to maintain to satisfy your record keeping obligations and provide you with an accurate picture of your financial affairs.

Business records are important - they help you and they help the Inland Revenue Department (IRD). If, after reading this information pamphlet, you are in doubt on how you should maintain your business records, it may be useful to seek the opinion of your accountant or financial adviser.

Why Keep Records

The IRO requires you to keep sufficient records (in English or Chinese) to enable your assessable profits to be readily ascertained. All records must be retained for seven years from the transaction date. It is an offence not to keep adequate records. You can be penalised for not doing so by being fined up to \$100,000.

There are also many other sound reasons why you should keep accurate business records. Here are some:

- accurate records allow you to be in better control of your business by helping with financial planning and decision making
- you portray a more professional image that makes it easier to deal with your bank
- appropriate records enable you to file an accurate profits tax return
- the costs to you of an IRD audit are reduced if all of the necessary records are readily available

- compliance costs are less
- losses and theft in your business may be detected
- you are in greater overall control of your business.

Some Ideas for Record Keeping

Business records which must be kept include documents which provide a record of your business transactions, or which enable these transactions to be traced and verified through the accounting system from start to finish. These include invoices, receipts, cash register tapes, banking records, cheque books. The essence of good record keeping is good book keeping. Efficient bookkeeping will save you time and money in the long run.

Here are some tips to help improve the efficiency of your bookkeeping:

- make bookkeeping part of your regular routine. Once you've established a routine, you'll find that you work through your books more quickly
- keep your bookkeeping up to date
- keep your books in an organised manner - you'll work quicker if you can easily access the information you need
- look for ways to improve your bookkeeping
- don't leave things until the last minute.

Retention of Your Records

Don't forget that having taken the time and effort to prepare your business records, you must keep them for at least **seven** years after the date of the transactions concerned. Even after you cease trading, your record keeping obligations continue until the seven year period has expired.

If you have losses from earlier years of assessment that have been set off against profits in later years, it is a good idea to keep all of the records until 7 years after the end of the year in which the losses have been fully set off.

Records That Must be Kept by All Businesses

You must keep sufficient records to enable the assessable profits of your business to be readily ascertained. To confirm your calculations, your business records must include -

- the books of account recording receipts and payments, or income and expenditure
- the underlying documentation necessary to verify the entries in the books of account; such as vouchers, bank statements, invoices, receipts and other relevant papers
- a record of the assets and liabilities of your business
- a day by day record of all sums of money received and expended by your trade, profession or business together with supporting details of the receipts or payments.

You must also keep records relating to all your business assets and liabilities at the end of each year, including:

- lists of debtors and creditors
- stocktake figures.

Additional Records - Businesses Dealing in Goods

In addition to the records that must be kept by all businesses, if your business deals in goods, you must maintain records relating to your purchases and sales. This includes full particulars of all goods purchased and all goods sold. Copies of the invoices for the transactions must show goods, and the buyers and sellers, in sufficient detail to enable the Commissioner to readily verify:

- the quantities and values of the goods
- the identities of the sellers and buyers.

In most cases, the relevant purchases and sales invoices issued for the transactions will satisfy this requirement. If, however, the relevant details are either absent from or not clear on an invoice, you may make additional notations on it to clarify any doubtful points.

You may face practical difficulties in complying with this requirement if your business is engaged in retail trade traditionally conducted in cash, particularly as regards recording the identities of all purchasers. A concession therefore exists for those taxpayers engaged in retail trades, professions and businesses which are normally conducted in cash. They are not required to keep the specified details records **of all goods sold**. If the concession applies to you, you must nevertheless keep full records of your purchases and full details, recorded on a day by day basis, of all sums of money received and expended by your business.

The inclusion in your accounts of the correct value of trading stock on hand at the end of the accounting year is essential in determining the correct profit for that year. You must prepare and keep statements (including quantities and values) of trading stock on hand at the end of the accounting year (together with the stocktaking records from which the trading stock statements have been prepared).

Additional Records - Businesses Providing Services

Trades, professions and businesses involved in providing services must maintain records of all services provided in sufficient detail to enable the Commissioner to readily verify the entries in the business's day to day record of all monies received and expended. If you provide services, you must keep a record all services provided. The sums charged and paid for them have to be traceable through the books of account to the statement of income and expenditure.

How to Keep your Records

- **The paper based method**

Paper based record keeping simply means keeping all your invoices for sales and for purchases as well as all your cheque butts, copies of your bank deposit slips and bank statements. These will form the basis of the entries in your cash book.

When you use the paper based method of book keeping you must make sure you keep all your records in a legible and well organised manner.

- **The computer method**

Another way of keeping records is by using a computer. Depending on the type and size of your business, using a computer can simplify and improve your record keeping. Advantages in using a computer to keep records include:

- most computer accounting programs will give you an up-to-date picture of how your business is going, and help you plan and forecast your future situation
- a computer can improve the accuracy of your record keeping, and find recorded information more quickly if you need it later
- lists of items that change from time to time (for example, a register of your fixed assets) can be updated much more easily if they are kept on a computer
- information that may be required by the IRD can be produced by the computer, provided it has been recorded correctly in the first instance
- if IRD decide to audit your records, it can be made a lot easier by using computer-stored information. The audit can be finalised more quickly and this will cause less disruption to your business.

Even if you do keep your records on computer, you must still keep source documents such as cheque butts, invoices, bank deposit slips and bank statements to substantiate your income and expenses.

Make sure that you backup all the information you have on your computer. This means copying the information onto a floppy disk or printing out copies of vital information regularly. These copies must be stored safely. Keeping all your records on computer without proper backup procedures can be disastrous if your system malfunctions.

PART TWO - BANKING RECORDS

Bank Accounts

It is good business practice to maintain separate bank accounts for personal and business purposes. Using your registered business name or business trading name for your bank account will give a clear indication that it is a business account. If separate accounts are not kept it is important to record separately in your cash book any extra money you put into your business and any private expenses you pay from the account.

You should regularly bank all business income into your business bank account. Paying all purchases and expenses by cheque creates a permanent record of each payment that appears in your bank statement.

Cheque Books

Most businesses pay their expenses by cheque. A cheque book provides a record of payments and, if used correctly, can assist in managing your cash flow. Your cheque butts or covering payment voucher should record:

- the date of payment
- the name of the payee
- details of goods or services purchased or account being paid
- the amount of the cheque.

It may be useful to file away your used cheque books in case you need to make reference to them later.

Bank Deposits

Many bank deposit slips contain a self-carboning duplicate which, when machine-imprinted by the bank, is the customer's receipt for the deposit.

Retaining duplicate deposit slips is a good idea as they may assist in reconciling your bank statements.

Bank Statements

Bank statements are the bank's record of the transactions you have conducted with it. The entries on the statement may differ from your cash book entries because direct debits, bank charges and interest may have been deducted from your account. You will not know the amount of these charges until you receive a bank statement.

Comparing the cash book to the bank statement and adjusting for the differences is termed a bank reconciliation.

Bank statements are a vital part of your account keeping and should be safely filed away in date order. Be careful not to lose them as banks may levy a charge to provide you with copies.

Cash Book

This is the book in which you should record all your business transactions involving cash. It is the minimum bookkeeping system for any business. There are a number of important reasons why you should use a cash book:

- a cash book records all receipts and payments whether by cash or cheque
- you can monitor your cash flow - i.e. how much money is coming into your business and how much you are paying out
- it helps you to check that your bank statement is correct
- to know where your receipts have come from, and where your expenses are going to
- preparation of your profits tax return is made simpler, saving you money
- you can provide IRD with a complete record of your business transactions, if necessary

- it provides a convenient way of checking past transactions.

It is good business practice to reconcile your bank statement balance with your bank balance calculated from your cash book on a regular basis - monthly is recommended.

Before you can reconcile your bank statement with your cash book you need to have all your bank statements up to the period you are trying to reconcile. Use your bank statements to record items such as automatic payments, bank fees and interest charges (and anything else not already shown in your cash book) into the cash book prior to reconciling it.

PART THREE - RECORDS OF INCOME

You MUST keep records that record and explain ALL sales transactions

The documents described in this Part are called 'source documents'. They are the documents from which the entries in the 'receipts' section of your cash book are made.

There are a number of ways you can record your sales. These include:

- cash register tapes
- receipt books
- invoices issued
- exercise books or note books
- goods taken for own use diary
- credit notes for returned goods

Cash Register Tapes

Cash registers which have an internal tape to record all transactions provide a good record. If you use a cash register, ensure all sales are put through it. The tapes must be kept with the other business records. Highlighting the date of the tape will assist in any later verification of the recording of the sales in the cash book.

Receipts

Receipts may be used to record all sums you receive. The most suitable type of receipt is one that is pre-printed and consecutively numbered with duplicates. The name of your business should appear on every receipt.

Invoices issued

You should use sequentially numbered invoices for goods or services you supply to your customers. There are many styles of invoices available commercially but regardless of their design, the minimum information they contain should include:

- invoice number
- date of issue
- customer's name and address
- your business's name and address
- date of transaction
- description of goods or services, including quantities and prices
- total price.

Other methods for recording cash sales

If you have a cash retail business, you are required to keep a record of your sales. If you do not use either a cash register, receipt book or invoice to record these transactions any of the following methods can be used:

- **Cash sales transaction record** -This could simply be an exercise book, note book or such to record all sales, including any cheques received. This should record, as a minimum:
 - the date of trading
 - the total taking from the day's trading.

- **Counting system**

In some businesses there will be a number of transactions at the same price e.g. cinemas. These sales can be recorded, for example, by using consecutively numbered tickets and recording the number of tickets issued at each price level. The product of the number of tickets at each price should be recorded in the daily sales transaction record.

- **Calculator with tape**

A calculator or portable adding machine with tape could be used to record all sales transactions. The total of the daily sales transactions are entered in the cash book.

Stock Taken for Private Purposes

If you take stock from your business for your own private purposes, you should show this in your business records. The value of stock taken for private use should be either added to sales or deducted from the cost of purchases.

Accurate records should be kept of goods taken from stock for private use. In particular, you must be able to demonstrate that the value attributed to goods taken from stock for your own private use was fair and reasonable.

Returned sales

Goods which have been sold but which are returned due to incorrect quantities, defects, damaged or incorrect invoicing need to be recorded because they reduce the corresponding sales figures. It is recommended that you supply your customer with a credit note, which can then form the basis of the adjustment to your sales records.

PART FOUR - RECORDS OF PURCHASES AND EXPENSES

You MUST keep records that record and explain ALL purchase and expense payment transactions.

The documents described in this Part are source documents and are used to make the entries in the 'payments' section of your cash book.

Recording purchases

There are a number of ways of recording your business purchases. Some examples include:

- cheque butts
- receipts issued for payments made:
 - cash register tape receipts
 - account statements
 - diary or day book
- invoices received
- a petty cash system for small cash purchases

Cash purchases

All payments should be made by cheque whenever possible. However, where cash is used for small or sundry purchases, it may be more convenient to account for it through a petty cash system. If you spend any of the cash you have received before banking it, a record of the cash appropriated for cash payments is essential.

Receipts obtained

Wherever possible you should ask for a receipt when paying a business expenses - whether you pay by cash or cheque. Receipts will help you to prove accounts have been paid if queries arise later. The details that should be shown on a receipt are:

- date
- name of supplier or service provider
- amount paid
- description of property, goods or services being paid for.

A receipt issued by a cash register would be generally be sufficient, but it may not always describe the property, goods or services that have been paid for. If it doesn't contain sufficient detail, an additional notation should be recorded on the receipt.

Where receipts are not available, an invoice, account statement or cheque butt may used to provide the necessary substantiation. A diary or similar record should be used only where no other evidence of payment is available.

Credit card purchases

If you pay for goods or services with a credit card, the following records are acceptable as documentary evidence of the payment:

- your credit card docketts,
- payment receipts, and
- monthly card statements.

Invoices

Invoices usually contain more information than a receipt or other docket and provide additional evidence to support the payment or the purchase. All invoices received should be retained.

Recording business expenses

The procedures for recording your business expenses such as rent, electricity, telephone, insurance and motor vehicle expenses are essentially the same as those for recording purchases. Methods of recording business expenses include:

- cheque butts
- receipts obtained for payments made:
 - cash register tape receipts
 - account statements
 - diary or day book
- invoices received
- log books
- diaries
- petty cash payments

Log books

Motor vehicle expenses are an example of expenses that may need to be apportioned by sole proprietors and partnerships when they are not wholly related to business purposes. Motor vehicle expenses are usually apportioned on the basis of the distances travelled for business and non-business purposes. A log book identifying business and private journeys (including kilometres travelled) is an appropriate way of accurately determining the business proportion of the overall expense incurred.

Diaries

At times it will not be possible to obtain receipts for some expenses, such as public transport fares, parking meter fees etc. Recording these types of expenses in a diary is an acceptable method of verifying the expenditure claimed.

Petty Cash System

Where practical, you should make all payments by cheque. However, small spending on small items such as tea, milk, stamps and public transport fares can mean using cash. Many businesses operate a petty cash system to use to pay the small day by day expenses.

Wherever possible, receipts should be obtained from the claimants to support the expenditure incurred. Even if you do not maintain a petty cash system, you must still keep a record of amounts paid in cash.

PART 5 - KEEPING RECORDS OF YOUR ASSETS

You MUST keep records that record and explain all expenditure relating to assets.

Acquisition of Assets

Your business is likely to have a number of assets, such as machinery and plant, land and buildings etc. You will need to keep records of:

- the date you bought each asset, and how much it cost you
- the date you sold the asset, and for how much you received for it
- the date and amount of any other spending incurred in relation to the asset.

These records should include:

- copies of contracts of purchase and sale
- market valuations (where the item was acquired or disposed of otherwise than by sale)
- statements of account, invoices and/or receipts for services rendered, (e.g. legal fees)
- agent's commissions and broker's fees
- stamp duty
- any expenditure in improving the asset

Fixed Asset Register

For good record keeping of fixed assets the use of a fixed asset register is recommended. An example of a fixed assets register is shown below.

Description	Item No.	Cost/Value \$	Date purchased	Remarks
Laser printer	651	3,900.00	15/10/94	
Scanner	652	7,500.00	15/10/94	
Computer Monitor	653	2,000.00	15/10/94	
Desk	654	1,500.00	15/10/94	
Chair	655	550.00	15/10/94	
Laptop computer	656	20,000.00	21/06/95	
Fax/Modem	657	1,500.00	21/07/95	
Sofa	658	5,000.00	28/08/95	
Telephone	659	1,000.00	28/08/95	
Fax machine	650	4,000.00	15/10/95	
Reception Desk	651	1,500.00	11/11/95	
Coffee Table	652	1,700.00	12/11/95	
Hot Water Urn	653	1,500.00	12/11/95	

PART 6 - CASH RECEIVED AND EXPENDED

Need to record all money received and expended

You **MUST** keep a daily record of **ALL** money received and expended by your business.

It is probable that if you keep a full set of accounting records and settle small purchases and expenses through a petty cash system, you will already be keeping a daily record of money received and expended. However, if you do receive or expend money that is not recorded anywhere else in your records i.e. as sales, purchases and expenses, or assets you must keep records of the amounts received and expended.

PART 7 - END OF THE ACCOUNTING PERIOD

Stocktake

You **MUST** keep records that record and explain your trading stock on hand at the end of each accounting period. The stock-on-hand at the beginning and end of each year has to be taken into account in working out whether or not a business has an assessable profit.

What is trading stock?

Trading stock is anything produced, manufactured, acquired or purchased for purposes of manufacture, sale or exchange by your business. In certain circumstances, goods are treated as trading stock on hand even though they are not in your or the business' actual possession, such as

- stock held in the hands of an agent
- stock held in an off-site warehouse
- stock held in a bond store
- stock held in transit.

Valuation of trading stock

The cost of trading stock includes not only its purchase cost but also such things as freight costs and manufacturing costs. The portion remaining unsold (including the cost of work in progress and raw materials) or unused has to be taken into account to prevent expenses for the year being overstated. To determine the correct assessable profits of your business, trading stock on hand at balance sheet date has to be valued. This generally involves conducting a physical count of the stock (raw materials etc.) remaining unsold or unused.

Documentary evidence of such a stocktake should be compiled and kept with your other business records. A list describing each article of stock on hand

(including raw materials and work in progress) and the value of the stock etc. should be prepared. This list should also include the following information:

- who did the stocktake
- how the stocktake was done
- the date of the stocktake
- the basis of the valuation.

List of debtors and creditors

You should consult with your accountant or financial adviser as to whether it is appropriate for your business to take account of debtors and creditors in calculating your assessable profits.

If it is appropriate, then at the time of preparing your profits tax return, the following information will be necessary -

Debtors

- customer's (or client's) name
- the amount owed to you by each debtor
- total amount owed to you by all debtors
- length of time each debt has been outstanding
- when you expect each debt to be paid
- what steps you have taken to recoup each debt.

Creditors

- supplier's name

- the amount you owe to each supplier
- total amount you owe to all suppliers.

Depreciation

You are allowed to claim an initial allowance on items machinery and plant and industrial buildings acquired during the year used to produce assessable profits. You are also entitled to an annual allowance for wear and tear on qualifying assets.

You should keep records of depreciation allowances you have already claimed as deductions so that you can calculate your entitlement to depreciation allowances in subsequent years.

FURTHER INFORMATION

Further information on all aspects of your record keeping requirements under the Inland Revenue Ordinance can be obtained from the Inland Revenue Department by telephoning 2594 5400 or writing to GPO Box 11234, Hong Kong.