

craftybase - a guide for bookkeepers

A summary of Craftybase features for bookkeepers and accountants.



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Introduction

Craftybase is an inventory and bookkeeping software package designed specifically for small manufacturers.

We help thousands of craft businesses to track their inventory and calculate their COGS using our industry standard perpetual inventory application. In this guide we'll cover the basics around inventory bookkeeping and how our system can help your clients with their financial reporting requirements.

Why do small manufacturers need to track inventory?

One of the most misunderstood areas of manufacturing is how to track and cost inventory. Our system takes much of the hard work out of calculating unit costs and applying to sold products.

Some believe that if their clients have a small turnover or act like a "hobby" that inventory for tax isn't required. This isn't true - it is an essential obligation for all small manufacturing businesses. If your client is based in the US, manufacture their own products and gross (before expenses) revenue is at least \$400 a year, they are obligated to file a Schedule C before April each year including Part III inventory values. To do this, it's vital that your client is accurately recording the costs of material purchases and manufactured products.

For extremely small businesses with low sales and inventory activity, a spreadsheet may suffice for this in the immediate term, however once sales are growing and inventory is being purchased regularly these types of systems quickly get hard to maintain. Craftybase is designed specifically for these business situations by providing a cost effective, easy to use way to monitor and calculate inventory usage. As we are a perpetual inventory system, we are designed to track inventory constantly during the year - this leads to less last minute end of year rushes and reduces stress on both you and your clients.

Outside of tax and financial obligations, there are many other reasons why small manufacturers should use a dedicated perpetual inventory system:

Accurate Pricing

Without understanding exactly how much it costs to make each product, it is almost impossible to set prices that achieves the client's profit margin requirements. Craftybase calculates material costings to 5 decimal places and constantly updates based on material vendor price increases and decreases.

Anticipating Demand

Without knowing previous sales and manufacturing history, it's impossible to predict different sales patterns to account for seasonality, holidays and weather. Keeping track of manufacturing activities can lead to insight as to when the busiest periods are so that your clients can better prepare for them.

Shrinkage and loss control

By tracking where stock is being used, your clients can then start to see opportunities for improvement - they might find that they have a certain product which is now clear produces a large amount of unusable scrap. This can lead them to relook at their entire manufacture process to see if any changes can be made.

Insurance

Think about what sort of information and records your clients' insurance companies will want to know if disaster strikes. Given that your inventory is one of their biggest assets, they'll be wanting to provide detailed records to prove what they had on hand.

What is Craftybase?

Craftybase is a perpetual inventory and bookkeeping system designed for small handmade manufacturers.

Software that provides automatic real-time inventory calculations are called *perpetual inventory systems*. This effectively means that stock levels will be constantly recalculated as your clients change them throughout the year - this is done by logging expenses, orders and manufactures. This is in contrast to periodic systems (like ones built in Excel) that calculate stock only via undertaking huge stocktakes at the end of the year.

As perpetual systems allow for the ability to update stock levels in real time, your clients will be building a picture of their inventory throughout the year: this means that they can make better decisions for their business as they'll have the information needed at their fingertips: sales and expense figures, low stock alerts, profit margin changes, pricing guidance, estimated tax liabilities and more. Perpetual tracking can also remove the necessity for a large scale End Of Year (EOY) stocktake as they have been logging and checking stock all year. This can result in huge time savings for their business and a more streamlined, calmer tax filing time for you and your clients.

Accrual Method

Craftybase uses the Accrual Method for all reporting which is the recommended method for businesses with significant inventory.

Significant inventory is defined as the value of inventory relative to revenue, which is generally the case for most small manufacturers regardless of actual turnover.

The Accrual Method essentially means that the revenue or expense is reported when generated, as opposed to the Cash Method which reports on orders and purchases when they have been paid.

The IRS expects businesses that report inventory to be using the Accrual method of accounting, other than in exceptional circumstances regardless of turnover.

As part of your client's tax obligations, all inventoried goods must be accounted for at the start and end of the tax year - without tracking purchases and sales both on an accrual basis, using cash-basis principles can lead to discrepancies between inventory accounting and reported expenses and income.

Inventory Valuation Method

As you most likely know, there are three ways recognised by the IRS for valuing the cost of inventory: FIFO, LIFO and Weighted Average Cost.

Craftybase uses the **rolling average method** exclusively in all inventory calculations.

The rolling / weighted average method assumes that all inventories are being sold simultaneously from a single "pool". This method is most commonly used in manufacturing situations where materials are piled or mixed together once purchased and thus can no longer be differentiated by their exact unit costs.

From 2008, the IRS has declared that using rolling average costs was an allowable method for calculating inventory.

Cost of Goods Sold

As Craftybase is a perpetual inventory application, inventory valuations and COGS calculations are made in real-time.

Craftybase effectively maintains two inventory ledgers for all stock changes - one for products and another for materials.

Each time a stock change is made that affects materials, this is logged as an inventory adjustment. This adjustment has an associated cost, which is calculated from the rolling average calculations discussed above.

An adjustment for a purchase (expense) of 4 green beads at a \$0.56 unit cost may look like this:

6 Mar 2019 Beads - Green - 5mm +40 \$0.56

An adjustment when 5 of the beads are consumed in the manufacture of a product may look like this:

10 Mar 2019 Beads - Green - 5mm -5 \$0.56

These adjustments are all created automatically based on the action taken by the user so they do not have to be maintained directly. Adjustments can be made manually to each material or product adjustment ledger - this is useful for stocktaking discrepancies, damage or other unexpected loss of stock.

The material adjustment history is used to generate a cost of manufacture for each product made. This is subsequently entered into the product adjustment history like this:

20 Mar 2019 Grey Bag +1 \$19.67

As the stock has been removed from the material adjustment history at the same time, this is how stock value is moved from raw materials to finished product inventory.

When a product is sold and shipped, this triggers a final calculation to remove the material value from inventory. This is again based on our rolling average calculations and results in a posting to the product inventory adjustment history as so:

25 Mar 2019 Grey Bag -1 \$19.67

It is the constant recalculation of all adjustments made via these actions that results in highly accurate, real time stock quantity and inventory valuations.

Schedule C

As seen, the total value of inventory adjustments for any date period can be calculated, making tallying COGS and inventory valuation at end of year much easier than the manual method.

To make things even easier, the Craftybase Schedule C Guidance report brings together all the important inventory tallies that are needed for filing a IRS Form 1040 Schedule C.

The report covers I Income, II Expenses and III Cost of Goods Sold calculations. Expenses in Part II are categorised by the custom categories created by the user for each non-material (indirect) expense logged in the time period.

III Cost of Goods Sold

Inventory at beginning of year: The total value of all materials in stock on this date as calculated via inventory adjustment history, plus the material cost of all unshipped stock.

Purchases less cost of items withdrawn for personal use: The total inventoriable material expenses for the year, minus any material and project inventory adjustments added in the year with a category of "Personal Use".

Inventory at end of year: The total value of all materials in stock on this date as calculated via inventory adjustment history, plus the material cost of all unshipped stock.

This report can be downloaded a print-friendly PDF or a CSV for further analysis in a spreadsheet.

Stocktaking

Perpetual material inventory systems are designed to track the changes in stock levels constantly through the year.

Due to this, if your clients are tracking accurately it's technically not required to request an annual stocktake of their entire material inventory.

The keyword here is “accurately” - if you don’t feel that they yet have a reliable degree of accuracy in your manufacture and wastage measurements by end of year then it is a good idea to schedule in a count regardless to ensure that their records are correct.

The best way to improve their accuracy going forward is to recommend using an approach called the "cycle (or perpetual) count". This method involves regularly counting a small sample of stock and comparing it to current records. Any discrepancies can then be instantly adjusted or investigated to find out the cause.

Summary

Craftybase is a fully featured, industry standard inventory application designed for small scale handmade manufacturers.

Our software is designed to be a perpetual inventory tracker and uses rolling / weighted averaging to calculate inventory valuation and COGS. All of our calculations are based on the accrual system of accounting and follow GAAP / IRS regulations.

If you have any further questions, please do get in touch:

Craftybase Support help@craftybase.com

Craftybase Facebook Community <https://www.facebook.com/groups/craftybase/>