



FARM CREDIT EAST



Financial Statements and the Business Plan

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What is a Balance Sheet?

- A balance sheet shows the value of the items owned (assets) and all debts owed (liabilities). The difference between these is Net Worth or Equity.
- Shows a snapshot in time (i.e. 12/31/2010)

Assets

- What you “own”
- Organized on a balance sheet in the order of ease of conversion to cash
- Typically broken down in to 3 categories
 - Current Assets
 - Intermediate Assets
 - Long Term Assets

Current Assets

- Easily converted to cash in less than 1 year
- Examples:
 - Cash, checking and savings accounts
 - Accounts Receivable
 - Feed/Supplies
 - Products and livestock raised for resale

Intermediate Assets

- Can be liquidated but requires more time to sell at a fair price
- Examples:
 - Breeding Livestock
 - Machinery, Equipment and Vehicles
 - Coop Stock

Long Term Assets

- In most cases these assets could not be liquidated without the business being terminated
- Examples
 - Land and Buildings

Liabilities

- What you “owe”
- Categorized by the term of the loan, not life of the asset
- Classified into 3 categories
 - Current Liabilities
 - Intermediate Liabilities
 - Long Term Liabilities

Current Liabilities

- Obligations that are likely to be repaid within 1 year
- Examples
 - Accounts Payable
 - Operating Loans
 - Current Portion of Intermediate and Long Term Liabilities

Intermediate Liabilities

- Obligations that are repaid within 2-7 years
- Loans for the purchase of
 - Machinery, Equipment and Vehicles
 - Breeding Livestock
- Leases

Long Term Liabilities

- Obligations with repayment terms longer than 7 years
- Most commonly Real Estate Mortgages

Why is it called a balance sheet?

- Because it must balance!
- $\text{Assets} = \text{Liabilities} + \text{New Worth}$

Types of Balance Sheets

- Market Value: Current Value of the asset if it were to be sold
- Book Value: Cost of the Asset- Accumulated Depreciation
- Which one is used more in farm operations?
 - Market Value

What increases Net Worth?

- Profitable Production
 - Increases in Inventory
 - Accounts Receivable
 - If item is sold, increase in checking and savings accounts or decrease of debt
- Increase in Price of Asset
- Infusion of Cash from Other Source- Gifts and Inheritance
- Forgiveness of Liability

What decreases Net Worth?

- Non-Profitable Production
 - Decrease in inventory, accounts receivable, cash or savings, increase in debt
- Decrease in Price of Assets
- Depreciation
- Family Draws
- Lost Capital

Analyzing a Balance Sheet

- Refer to Handout

What is an income statement?

- The goal of an income statement is to determine the profitability of your business
 - Profitability = value of farm production (receipts) – cost of farm production (expenses)
- Can be prepared on “Cash Basis” or “Accrual Basis”

Cash Basis Income Statement

- $\text{Cash Receipts} - \text{Cash Expenses} = \text{Net Cash Farm Income}$
- Entries are made when cash actually trades hands
- Ignores accounts receivable/payable, inventory changes and sometimes depreciation

Accrual Income Statement

- Accrual is more Accurate
- In addition to cash income and expenses, an accrual income statement takes in to account accounts receivable and payable and inventory changes

SCHEDULE F
(Form 1040)

Department of the Treasury
Internal Revenue Service (99)

Profit or Loss From Farming

▶ Attach to Form 1040, Form 1040NR, Form 1041, Form 1065, or Form 1065-B.
▶ See instructions for Schedule F (Form 1040).

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2010

Attachment
Sequence No. 14

Name of proprietor

Social security number (SSN)

A Principal product. Describe in one or two words your principal crop or activity for the current tax year.

B Enter code from Part IV

C Accounting method:

(1) ☐ Cash

(2) ☐ Accrual

D Employer ID number (EIN), if any

E Did you "materially participate" in the operation of this business during 2010? If "No," see instructions for limit on passive losses. ☐ Yes ☐ No

Part I Farm Income—Cash Method. Complete Parts I and II (Accrual method. Complete Parts II and III, and Part I, line 11.) Do not include sales of livestock held for draft, breeding, sport, or dairy purposes. Report these sales on Form 4797.

1	Sales of livestock and other items you bought for resale	1	
2	Cost or other basis of livestock and other items reported on line 1	2	
3	Subtract line 2 from line 1	3	
4	Sales of livestock, produce, grains, and other products you raised	4	
5a	Cooperative distributions (Form(s) 1099-PATR)	5a	
5b	Taxable amount	5b	
6a	Agricultural program payments (see instructions)	6a	
6b	Taxable amount	6b	
7	Commodity Credit Corporation (CCC) loans (see instructions):		
a	CCC loans reported under election	7a	
b	CCC loans forfeited	7b	
7c	Taxable amount	7c	
8	Crop insurance proceeds and federal crop disaster payments (see instructions):		
a	Amount received in 2010	8a	
8b	Taxable amount	8b	
c	If election to defer to 2011 is attached, check here <input type="checkbox"/>	8d	Amount deferred from 2009
9	Custom hire (machine work) income	9	
10	Other income, including federal and state gasoline or fuel tax credit or refund (see instructions)	10	
11	Gross income. Add amounts in the right column for lines 3 through 10. If you use the accrual method to figure your income, enter the amount from Part III, line 51	11	

Part II Farm Expenses—Cash and Accrual Method.

Do not include personal or living expenses such as taxes, insurance, or repairs on your home.

12	Car and truck expenses (see instructions). Also attach Form 4562	12		25	Pension and profit-sharing plans	25	
13	Chemicals	13		26	Rent or lease (see instructions):		
14	Conservation expenses (see instructions)	14		a	Vehicles, machinery, and equipment	26a	
15	Custom hire (machine work)	15		b	Other (land, animals, etc.)	26b	
16	Depreciation and section 179 expense deduction not claimed elsewhere (see instructions)	16		27	Repairs and maintenance	27	
17	Employee benefit programs other than on line 25	17		28	Seeds and plants	28	
18	Feed	18		29	Storage and warehousing	29	
19	Fertilizers and lime	19		30	Supplies	30	
20	Freight and trucking	20		31	Taxes	31	
21	Gasoline, fuel, and oil	21		32	Utilities	32	
22	Insurance (other than health)	22		33	Veterinary, breeding, and medicine	33	
23	Interest:			34	Other expenses (specify):		
a	Mortgage (paid to banks, etc.)	23a		a		34a	
b	Other	23b		b		34b	
24	Labor hired (less employment credits)	24		c		34c	
				d		34d	
				e		34e	
				f		34f	
35	Total expenses. Add lines 12 through 34f. If line 34f is negative, see instructions	35					
36	Net farm profit or (loss). Subtract line 35 from line 11. Partnerships, see instructions.						
	• If a profit, enter the profit on both Form 1040, line 18, and Schedule SE, line 1a; on Form 1040NR, line 19; or on Form 1041, line 6.						
	• If a loss, you must go to line 37.						
37	If you have a loss, you must check the box that describes your investment in this activity and whether you received any applicable subsidy (see instructions).			37a	<input type="checkbox"/> All investment is at risk and you did not receive a subsidy.		
	• If you checked 37a, enter the loss on both Form 1040, line 18, and Schedule SE, line 1a; on Form 1040NR, line 19; or on Form 1041, line 6.			37b	<input type="checkbox"/> Some investment is not at risk or you received a subsidy.		
	• If you checked 37b, your loss may be limited. See instructions.						

For Paperwork Reduction Act Notice, see your tax return instructions.

Cat. No. 11346H

Schedule F (Form 1040) 2010

FARM CREDIT EAST

Analyzing the Income Statement

- Refer to Handout

Trend Analysis

- A Trend ties the Balance Sheet into the Income Statement
- It also includes:
 - Non-Farm Income
 - Debt Service
 - Family Living
 - Income Taxes
- Represents the discretionary funds of the operation and borrower combined

Trend Analysis

- See Example Handout
 - Cash and Accrual

Summary

- Balance Sheet
- Income Statement
- Trend Analysis

Monthly Cash Flow Budget

- Why is it necessary?
 - Takes into account the seasonality of your business operating cycle.
 - Assists to determine timing and \$ amount of operating infusion.
 - Provides for an opportunity to fine tune your budget for the upcoming season.
 - Provides an opportunity to prioritize capital purchases and identify potential funding sources.

PLUS

Monthly Cash Flow Budget

**BANKERS
LOVE THEM**

Monthly Cash Flow Budget

- Components From Top to Bottom
 - Step 1: Basic Five Line Income Statement

Gross Sales

Less COGS

Equals Gross Margin

Less Overhead Costs

Equals Net Margin

COGS = wholesale cost on items purchased for resale or variable input costs
(feed, bedding, trucking, production labor)

Overhead Costs = DIRT 5 (depreciation, interest, repairs, taxes, insurance)

- Step 2: Add in Net Non Farm Income (after tax)

Monthly Cash Flow Budget

- Step 3: Take out Family Living Expense
- Step 4: Itemize Monthly Debt Payments
 - Operating Lines (Interest Only)
 - Could be supplier credit or credit cards
 - Capital Debt Payments (Vehicles/Equipment)
 - Mortgage Payments (Real Estate)

Monthly Cash Flow Budget

- Step 5: What is Monthly Cash Required?
 - Is it positive or negative?
 - If negative, where fund the short fall?

- Step 6: Determine any other capital needs
 - How funded and when?

Business Plan

- Set the Mission, Values, and Goals:
 - Mission: Reason for existence-what the operation will do
 - Vision: Some desired future state
 - Goals: Measurable desired future state an operation attempts to realize

Business Plan

- Structure of the Company:
 - What type of entity?
 - Who is in charge?
 - Who is responsible for what tasks?

- SWOT Analysis
 - Strengths
 - Weaknesses
 - Opportunities
 - Threats

- Marketing Plan

Business Plan

- Financial Analysis
 - Start Up Costs
 - 3 yrs of balance sheet and cash flow projections
 - Sources of funding and required repayment
- What are your “doors out”?
 - Sell a building lot
 - Borrow from family members
 - Get a part/full time job off the farm
 - Liquidation of farm assets

Business Plan

- Hints and Tips:
 - Build in extra for start up costs
 - Be realistic-a loss the first year is ok
 - Know the industry averages
 - Have others review your plan



FARM CREDIT EAST



Thank You!

Questions?

