UNDERSTANDING FINANCIAL STATEMENTS

Presenter: Melanie De Jong, CPA





BEHIND THE SCREEN



➤Dordt grad \geq 3 years in public accounting ➢Originally from Washington



There's more.

OUR TEAM







FS FUNDAMENTALS





OBJECTIVES

- ► Understand the 3 main financial
 - statement reports and their
 - importance
- >Understand the difference between
 - cash and accrual reporting





WHO CARES?

➤Tool for management

≻Lenders

➢Estate/Retirement Planning





Basics

➤3 main reports

➢Balance Sheet → Value

➢Income Statement → Profitability

Statement of Cash Flows → Cash in/out

➢ Recordkeeping

➢FS are only as valuable as info used to prepare them





BALANCE SHEET





BALANCE SHEET OVERVIEW

- ➢Financial position at a specified date
- ➢Reflects all past transactions
- ≻Purpose
 - ➢ Financial health
 - ≻ Own vs. owe

Assets = Liabilities – Owners Equity

Difference in assets & liabilities indicates solvency at a certain date





ASSETS

- Owned resource with economic value that is expected to produce a future benefit
- ➤ Asset vs. Expense
 - ➤ Timing
 - > The full cost of an asset is **not** written off immediately in period purchased
 - Depreciated or expensed over a defined period of time
 - Expenses have a direct effect on taxable income, assets have an indirect effect on taxable income
- ➤ Asset Classes
- ➤ Valuation





ASSETS

>Current (Live < 1 Year)</pre>

➤ Cash

≻A/R

➤ Inventories

➤Investment in Growing Crop

>Noncurrent (Life > 1 Year)

➤ Machinery, Equipment, Livestock

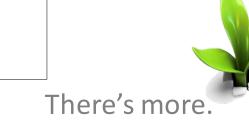
≻Real Estate

➤ Coop Stock/Retains





SAMPLE	DAIRY	
BALANCE : DECEMBER		
ASSE	TS	
CURRENT ASSETS, pledged:		
Cash and cash equivalents	\$ 45,36	
Accounts receivable, Dairymans Cooperative Inc. Inventories:	463,17	3
Hay - 3,016 tons	\$ 238,440	
Silage - 35,783 tons	1,206.507	
Investment in growing crops	38,723	
Total inventories	1,483,67	0
Prepaid expenses	190,89	5
Total current assets	2 192 10	
1 otal current assets	2,183,10	Ø
DAIRY HERD, pledged: 2.544 Cows	3,945,744	
2.041 Heifers	1,696,071	
Total	5,641,815	
Accumulated depreciation	(1,429,728)	
Dairy herd, net	4,212.08	7
DAIRY FARM AND EQUIPMENT, pledged: Land - 325 acres Buildings and improvements Machinery and equipment Autos and trucks Total Accumulated depreciation	1,446,4877,261,7951,823,488166,83110,698,601(5,788,995)	
Dairy farm and equipment, net	4,909,60	6
OTHER ASSETS:		
Cooperative retains	26,907	
Total other assets	26.90	7
		_
Total assets	S 11,331,70	6
See accompanying notes and independent - 2 -	dent accountants' Review report.	





LIABILITIES & EQUITY

≻Liabilities

➤ Classes

➤ All claims against the business

Equity (Net Worth)

- Equity = Total Assets Total Liabilities
- Reflects money that would be returned to shareholders/members if all assets were liquidated and debts paid
- Net income is reflected in OE section





EQUITY

- Components: Beginning equity, Net income, owners contributions (cash/property), owner distributions (dividends, cash, property, etc)
- Increases when a profit is generated and retained (rather than distributed to owners)or money contributed
- Decreases when a loss is generated and cash/property is distributed to owners





LIABILITIES & EQUITY

- Current (Due within 1 year)
 - ► AP
 - ≻Line of Credit
 - ➤Current portion of LT debt
- Noncurrent (Due beyond 1 year)
 - ➤Term loans (portion due after one year)

There's more



SAMPLE DAIRY

BALANCE SHEET DECEMBER 31, 2018

LIABILITIES AND PARTNERS' CAPITAL

CURRENT LIABILITIES:		
Accounts payable, feed dealers	S	555,738
Other trade payables		465,086
Accrued interest payable		18,803
Wages and payroll taxes payable		52,146
Farmers Bank, line of credit, secured by invventories and dairy herd,		
variable payments monthly plus 4.7% interest, matures September 2019		2,414,350
Estimated current portion of long-term debt	_	286,000
Total current liabilities		3,792,123

LONG-TERM DEBT: Notes and loans payable: Farmers Bank, secured by real estate and equipment: Payable S15,025 monthly including 3.45% interest, matures January 2021 \$ 360.600 Payable \$4,800 monthly including 3.38% interest, matures December 2023 278,208 Payable \$9,395 monthly including 3.35% interest, matures January 2027 865,840 Payable S10,000 monthly including 3.72% interest, matures January 2030 1,267,200 John Deere Financial, secured by equipment. payable \$5,000 monthly, non-interest bearing, matures February 2020 70.000 GM Financial, secured by equipment, payable \$1,500 monthly including 3.98% interest, matures June 2022 63,000 Estimated current portion (286.000)

See accompanying notes and independent accountants' Review report.

2,618,848

SAMPLE DAIRY, PARTNERS' CAPITAL: Balance at December 31, 2018

Long-term debt, ne

Total liabilities and members' equity

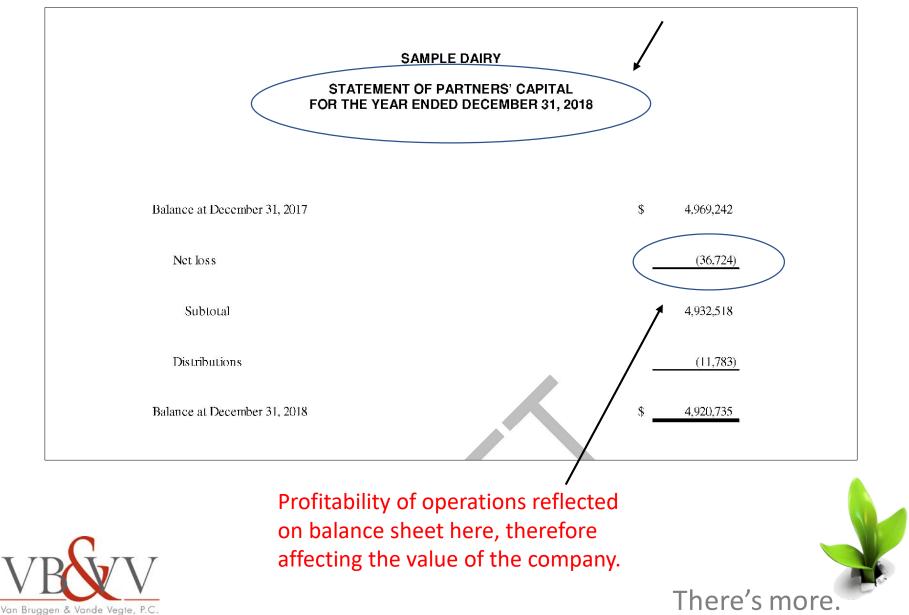
11,331,706

4,920,735

______ There's more.

Not retained earnings because not

a corporation, a partnership.



Certified Public Accountants and Financial Advisors

INCOME STATEMENT





INCOME STATEMENT

Shows income and expenses for a **period of time** (quarterly, monthly, annual)

Purpose

- Lender/investor/management analysis
- Profitability

Components

- ➢ Revenue
- Operating income
- Cost of goods sold
- ➢ Gross Profit
- Operating expenses
- Other income/expenses





SAMPLE DAIRY

STATEMENT OF INCOME FOR THE YEAR ENDED DECEMBER 31, 2018

		PER CWT F	ERCWT	PER
	AMOUNT		ECMILK	COW
INCOME FROM OPERATIONS:				
Milk S	10.439.484	S 15.85 \$	15.52 \$	4.148
Calves	93,444	0.14	0.14	37
Patronage dividends	10,423	0.02	0.02	4
Agricultural program payments	45,240	0.07	0.07	18
Farming, net. Schedule 1	(12,169)	(0.02)	(0.02)	(5)
Other	38,819	0.06	0.06	15
Total income from operations	10,615,241	16.12	15.79	4,217
OPERATING EXPENSES:				
Feed:				
Hay	751,971	1.14	1.12	299
Grain and commodities	3,416,058	5.19	5.08	1.357
Silage	1,100,041	▲ 1.67	1.64	437
Heifer and dry cow raising	1,323,476	2.01	1.97	526
Cost of feeding heifers	(1,540,251)	(2.34)	(2.29)	(612)
Total feed	5,051,295	7.67	7.51	2.007
				2,007
Herd replacement cost:				
Depreciation - cows	901.166	1.37	1.34	358
Loss on sale of cows	162,689	0.25	0.24	65
Total herd replacement cost	1,063,855	1.62	1.58	423
Other operating expenses:				
Interest	206,765	0.31	0.31	82
Labor	1,151,292	1.75	1.71	457
Partners salary	147,150	0.22	0.22	58
Depreciation - other	692,404	1.05	1.03	275
Milkhauling	9,251	0.01	0.01	4
Industry assessments	116,013	0.18	0.17	46
Supplies	550,290	0.84	0.82	219
Bedding	246,851	0.37	0.37	98
Repairs and maintenance	299,859	0.46	0.45	119
Utilities	229,994	0.35	0.34	91
Taxes and licenses	118,884	0.18	0.18	47
Insurance	170,625	0.26	0.25	68
Fuel and oil	151,360	0.23	0.23	60
Professional fees	20,773	0.03	0.03	8
Veterinary and breeding	264,361	0.40	0.39	105
Testing and trimming	104,961	0.16	0.16	42
Miscellaneous	38,830	0.06	0.06	15
Cost of raising heifers	(58,685)	(0.09)	(0.09)	(23)
Total other operating expenses	4,460,978	6.77	6.64	1,771
Total operating expenses	10,576,128	16.06	15.73	4,201
Income from operations	39,113	S 0.06 \$	0.06 \$	16
OTHER EXPENSES:				
Loss on sale of assets	(75,837)			
Net loss S	(36,724)			
	, , = , ,			

See accompanying notes and independent accountants' Review report.

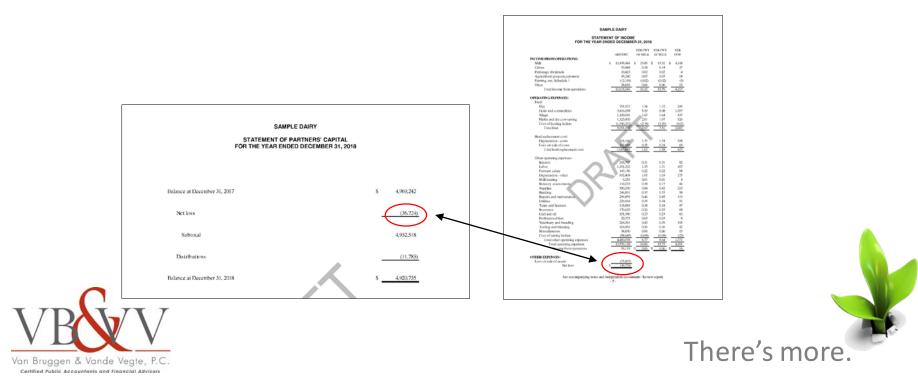




VBCV Van Bruggen & Vande Vegte, P.C. certified Public Accountents and Financial Advisor

INCOME STATEMENT & BALANCE SHEET

- Should be prepared for the same periods because of the link between the two
- > Every period income is closed to **Equity**(a balance sheet account)



STATEMENT OF CASH FLOWS





STATEMENT OF CASH FLOWS

≻Purpose

➤Critical questions

➤ Where did we obtain funds?

Are we expanding faster than we can generate funds?

➤What is our ability to repay our debt obligations (creditors)?

➢Reconcile Net income to cash balance





STATEMENT OF CASH FLOWS

Components

Operating activities

- > Net income/loss
- Increases/decreases in current assets and liabilities
- ➤ Depreciation

Investing activities

- Asset expenditures
- ➤ Coop retains

Financing activities

Changes in long term liabilities(debt) & equity

Beginning/Ending cash balance





SAMPLE DAIRY			
STATEMENT OF CASH FLOWS FOR THE YEAR ENDED DECEMBER 31,	2018		
CASH FLOW FROM OPERATING ACTIVITIES:			
Net loss		S	(36,72
The following is a reconciliation of net loss to net cash provided by operating	ıg		
activities:			
Non-cash patronage dividends	S	(2,545)	
Depreciation		1,625,207	
Loss on sale of cows		162,689	
Proceeds from sale of cows		367,940	
Purchase of heifers		(15,875)	
Purchase of replacement cows and bulls		(10,500)	
Capitalized cost of growing heifers		(1,598,936)	
Loss on sale of assets		75,837	
Increase in accounts receivable		(23,662)	
Decrease in inventories		248,856	
Decrease in investment in growing crops		14.261	
Increase in prepaid expenses		(179,524)	
Increase in accounts payable and accrued expenses		507,422	
Total adjustments			1.171.17
		-	
Net cash provided by operating activities			1,134,44
net each promate of openning activities			1,10 1,11
CASH FLOW FROM INVESTING ACTIVITIES:			
Purchase of fixed assets		(975,936)	
Return of cooperative capital		809	
		0.05	
Net cash used in investing activities			(975.12
			0.00
CASH FLOW FROM FINANCING ACTIVITIES:			
Borrowing of short-termidebi		3,450,367	
Repayment of short-term debt		(3,940,972)	
Borrowing of long-term debt		945,734	
Repayment of long-term debt		(602.665)	
Distributions		(11,783)	
Districtions	-	(11,76.5)	
Net cash used in financing activities			(159.31)
the chan abea in manena, activities			(100,01
Net decrease in cash and cash equivalents			
Cash and cash equivalents balance at December 31, 2017			
Cash and cash equivalents balance at December 31, 2018		S	
See accompanying notes and independent accountants' I	Review re	port.	
- 6 -			





CASH & ACCRUAL





ADVANTAGES OF CASH REPORTING

➢Simplicity

➤Tax benefit → FS manipulation

➢Prepay expenses

➢Defer income

➤Timeliness





ADVANTAGES OF ACCRUAL REPORTING

≻Why Do It?

➢ More Lenders Are Requiring It

More Accurate-Removes the "Games" We Play to Tax Plan

➤Allows for Benchmarking

➤ Decision Making

>Assessing profitability, risk, cost of production, etc.





CASH METHOD

- Recognizes revenue when payment is received regardless of when the revenue is actually earned
- Expenses cash when paid, regardless of what period it's for
- Doesn't accurately reflect "true" costs of operation





ACCRUAL METHOD

Recognizes revenue when earned rather than when cash is received

Books expenses when incurred rather than when paid

Key concept: accrual accounting seeks to match revenues and expenses



There's more.

SIMPLE EXAMPLE- DECEMBER

➤ Facts:

- Deposited November milk check for \$500 in December, actual revenue for milk shipped in December is \$600, which was deposited in January 2020.
- > Paid feed bill of \$50 for November, December feed bill of \$65 not paid until January 2020.
- Received a bill for \$30 supplies purchased in early December, not due (and won't be paid) until January 2020.

DECEMBER INCOME STATEMENT				
Cas	h Basis	Accru	al Basis	
\$	500.00	\$	600.00	
\$	(50.00)	\$	(65.00)	
	-		(30.00)	
\$	450.00	\$	505.00	
	Cas \$	Cash Basis \$ 500.00 \$ (50.00)	Cash Basis Accru \$ 500.00 \$ \$ (50.00) \$ -	





BEYOND THE BASICS





ACCRUAL ACCOUNTS

 \blacktriangleright New accounts \rightarrow Accrual accounts

➤Accounts Payable

➤Accounts Receivable

➤Inventories

➢Prepaid Expenses

➤Accrued Expenses

➤Investment in Growing Crop





INCOME STATEMENT

Profit & Loss

	Accrual	Тах
Revenue From Operations	5,423,384	5,406,082
Operating Costs & Expenses		
Crop & Other Expense	3,909,926	4,685,587
Depreciation	211,137	667,301
Total Expense	4,121,063	5,352,888
Net Income Before Taxes	1,302,321	53,194
Income Tax Provision	(434,620)	(8,299)
Net Income	867,701	44,895





ASSETS

Balance Sheet

	Accrual	Тах
ASSETS		
Current Assets		
Accounts Receivable	4,084,402	-
Inventory	307,898	-
Income Tax Receivable	4,522	-
Income Tax on Deposit	2,080	-
Prepaid Expenses-Crop Input	788,788	-
Commodity Account	62,412	72,163
Total Current Assets	5,250,102	72,163
Fixed Assets		
Property & Equipment	2,762,417	2,712,770
Accumulated Depreciation	(772,437)	(2,305,701)
Net Fixed Assets	1,989,980	407,069
Other Assets	2,900,699	2,900,699
Total Assets	10,140,781	3,379,931



There's more.

LIABILITIES & EQUITY

Balance Sheet

	Accrual	Тах
LIABILITIES & EQUITY		
Current Liabilities		
Bank Account (Overdraw)	48,762	48,762
Current Notes Payable	2,899,414	2,898,397
Current Deferred Income Tax	1,761,224	
Total Current Liabilities	4,709,400	2,947,159
Long-Term Liabilities		
Notes Payable	353,016	353,016
Non-Current Deferred Income Tax	538,190	
Total Liabilities Equity	891,206	353,016
Stock	3,672,474	36,470
Net Income	867,701	43,286
Total Equity	4,540,175	79,756
Total Liabilities & Equity	10,140,781	3,379,931



There's more.

A FINAL NOTE

► Usefulness of FS

➤Garbage in = garbage out

➤Your Operation





QUESTIONS?



