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EC71-847 Revised Your Balance Sheet

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YOUR BALANCE SHEET

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YOUR BALANCE SHEET

by

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WHAT IS IT?

Your balance sheet is a "photograph" — a picture of your financial position at a specific point in time. The two parts of your financial position are assets and liabilities.

Your assets include everything you own that could be sold or liquidated to generate actual dollars. Each asset is valued at estimated market value, assuming a reasonable amount of time could be allowed for liquidation.

You probably have certain obligations. Other people and institutions have certain claims against your assets. Liabilities are the **total** claims on your assets — first, the claims by others; and second, **your** claim which is the difference between the value of total assets and the claims by others. Your claim against the assets is called "Net Worth." This is your equity in the business. Your "equity" plus the total dollar claims by others will always equal total assets.

Since most of what a farmer owns is tied up in his farming operation, his balance sheet will include primarily assets and liabilities relating to the farm operation. The balance sheet form (EC 71-853), however, is designed to allow showing the full financial picture for an individual, which might include non-farm items such as marketable securities, non-farm real estate, etc.

As a farm business increases in complexity, and as the financial interest of the farmer extends beyond the farm, it becomes increasingly desirable to do a balance sheet on the farm business alone, along with balance sheets on each of the other businesses. These separate statements can then be combined into a master balance sheet.

Note that both assets and liabilities are subdivided into current, intermediate, and fixed or long term categories.

Current assets designate cash, savings, cash value of life insurance, marketable bonds, prepaid expenses, notes and accounts receivable, and the value of other assets that will likely be converted to cash under normal operation within 12 months or be used up in the production process during the year.

Intermediate assets are those not expected to be converted to cash during the year, but which contribute to and are used up by the business over a 5-10 year period. Securities not readily marketable also seem to best fit this category. Intermediate assets can be converted to cash easier than those fixed in nature, but their liquidation would normally hinder the business operation.

Fixed or Long Term assets are those used in production 1) which you would not expect to sell during the life of the operation, e.g. land, or 2) which have a life expectancy of more than 10 years but would eventually have to be replaced, e.g. buildings and fences.

As you move from current to fixed assets, an increasing amount of time is required for sale of the asset to yield full market value.

On the liability side, all obligations are itemized according to the final due date of the obligation, assuming a normal on-going business operation. A useful criteria in determining whether something is really an obligation on a given day, is to answer the question: Would this item have to be paid if the business was liquidated today?

Current liabilities are those obligations existing today, which likely will have to be met within 12 months.

Intermediate liabilities include obligations existing today but which have a final due date sometime between 1 and 10 years from the date of the balance sheet.

Long term or Fixed liabilities are existing obligations that have a final due date beyond 10 years. Real estate mortgages are typical fixed liabilities.

PURPOSE OF A BALANCE SHEET

The purpose of the balance sheet is to show your financial position (net worth and the supporting asset and liability structure) at a specific point in time. A single balance sheet indicates a specific financial position, without evidence as to how you arrived at this position.

By using balance sheets for successive periods, it is possible to determine the extent to which financial position is being changed. For comparisons to be meaningful, the balance sheets must be completed at the same time each year, preferably December 31. If a series of income statements is used along with the

balance sheets, it is possible to determine the actual net income from year to year and how this income relates to changes in net worth.

Another use of the balance sheet is to reveal how critical a financial loss would be. For example, a man with a \$200,000 net worth might be able to undertake a project that had a possibility of a \$10,000 loss. If the loss occurs, he could stand the shock without serious disruption. But such a loss would force a young farmer with an \$8,000 net worth completely out of business. The balance sheet helps you keep a proper balance among current assets vs. current liabilities, and current liabilities vs. intermediate and/or fixed liabilities.

A note of caution: the balance sheet is for a point in time. To determine how income and expenditures will compare with respect to timing and amount, a projected cash flow is needed.

A third specific use of the balance sheet is to show what collateral you have available to support loan requests. By analyzing both the existing assets and the claims already against such assets, it becomes clearer as to what future potential exists. Both you and your creditor are interested in what assets are available in relation to debts owed.

Fourth, a year end balance sheet provides an annual inventory of assets that is basic for preparation of the income statement and the cash flow projection. For example, inventory changes in the income statement require both the beginning and ending inventories for several items. By comparing the values of grain, livestock, supplies and other items at the end of last year with those from the current balance sheet, you have inventory changes.

In preparing a cash flow projection, you need to know what feed, seed, and supplies are on hand at the beginning of the year as this affects what you must buy and when grain and livestock sales will occur. Such information can be taken from the year end balance sheet. These are only examples of how details on the balance sheet become inputs for other "tools" of financial management.

FILLING OUT THE BALANCE SHEET (EC 71-853)

Balance sheets are most useful when completed annually over a period of years. To be meaningful, they should be completed at the same time each year, preferably December 31. You might record a minimum of details on December 31 and actually wait a few weeks to physically complete the form. But, you would use quantities and prices as of December 31. The form provides a space at the top for you to indicate the date to which the balance sheet applies, and a spot at the bottom to indicate the date when you are completing the form.

Comparisons based on balance sheets taken at different times of the year can be very misleading since the nature and amount of both current assets and current liabilities can change substantially from one season of the year to another. The preceding discussion relating how balance sheet information is helpful to completing income and cash flow analysis, requires annual balance sheets as of December 31. Otherwise, much multiple use of the balance sheet is lost.

The example shows how completed form might look. The discussion which follows will deal with the asset side and then the liability side, referring you to the example when appropriate.

Current Assets

Dollars in cash, checking and savings should be inventoried and recorded. Schedule B2 on the reverse side of the balance sheet allows for itemizing marketable securities. To be considered in current assets, a security should be mature and payable within the next 12 months or one which can be cashed in without disrupting the operation of the business. Otherwise, it will be recorded in the "not readily marketable" section and entered under intermediate assets. Prepaid expenses should cover all items or services that have been paid for but have not yet been received, for example, fertilizer paid for in November but not yet delivered. Once the item is delivered, it will appear in inventory if unused. Notes and accounts receivable should include the dollar value of what other people owe you, and which you expect to receive. It is possible that you might have a receivable that you would not expect to receive within 12 months. In that case, simply put it in either the intermediate or fixed asset section, depending on how soon you expect to receive it.

Livestock to be sold includes all feeder animals on hand and the breeding stock which will be marketed within 12 months. Females being kept for replacement purposes should be sorted out and inventoried under breeding livestock in intermediate assets. Animals should be grouped by kind, and then divided according to weight, sex, etc. Valuation should be based on market value as of the date of the statement and adjusted to an on-the-farm basis.

BALANCE SHEET

As of 12/31, 1971

Name John Farmer Age 40 Address Central Nebraska
 Spouse Mary Farmer Age of children at home Boy 15, girl 13 Phone Central 759-3682

ASSETS		LIABILITIES AND NET WORTH	
Current Assets		Current Liabilities	
Cash (on hand) or in checking	\$ <u>500</u>	Open or charge acc'ts.:	
Savings accounts & time certificates		Feed \$ <u>1000</u> Seed \$ _____ Fertilizer \$ _____	
Cash value of life insurance	<u>5,000</u>	Fuel & Oil \$ _____ Repairs \$ _____ Other farm \$ _____	\$ <u>1,000</u>
Marketable bonds and securities (Sched. B2)		Medical & other personal	<u>100</u>
Prepaid expenses (for items not yet received)		Estimated accrued interest on:	
Notes & accounts receivable (good)	<u>500</u>	Open acc'ts. \$ _____ Notes \$ _____	<u>1,415</u>
Livestock to be sold		Intermediate notes <u>Cows, windrower, storage</u>	<u>355</u>
<u>247</u> Steers Ave. wt: <u>475</u> Value/hd. <u>180</u>	<u>44,460</u>	Long term liabilities	<u>2,410</u>
<u>249</u> Steers <u>875</u> <u>289</u>	<u>71,899</u>	Estimated tax liability (accrued):	
<u>2</u> Heifers <u>500</u> <u>324/16</u>	<u>320</u>	R.E. <u>\$2626</u> ; Pers. <u>\$1741</u> ; Income <u>\$1770</u>	<u>6,137</u>
<u>10</u> Cows <u>1000</u> <u>250</u>	<u>2,500</u>	Accrued cash rent	
<u>150</u> Hogs <u>100</u> <u>25</u>	<u>3,750</u>	Notes payable within 12 mo. (To whom, maturity,	
<u>150</u> pigs <u>20</u> <u>1250</u>	<u>1,875</u>	purpose)	
<u>1</u> Boar <u>400</u> <u>60</u>	<u>60</u>	<u>Bank - Apr 1 - Yearlings</u>	<u>56,000</u>
<u>20</u> sows <u>400</u> <u>60</u>	<u>1,200</u>	" <u>Oct 1 - Calves</u>	<u>34,400</u>
Grain, Feed, Seed, & Supplies		" <u>Apr 1 - Feed</u>	<u>3,000</u>
<u>26,810</u> Bu. corn @ <u>1.30</u> <u>1180</u> bu. gr. sorgh.	<u>36,198</u>	That portion of longer term debts due	
<u>160</u> T. hay (<u>1</u> alf. <u>22</u> pr. <u>32</u> other)	<u>3,520</u>	within next 12 months (Sched. B4)	
<u>600</u> T. silage; _____ T. haylage; _____ T. straw @ <u>7.00</u>	<u>4,200</u>	Intermediate	<u>6,240</u>
Supplies (Sched. B3)	<u>728</u>	Long term	<u>5,715</u>
Cash Investment in Growing Crops		Judgments & mechanic liens	
_____ ac. wheat; _____ ac. rye; _____ ac. _____		CCC loans: _____ bu. _____, _____ bu. _____	
TOTAL CURRENT ASSETS	\$ <u>176,710</u>	Other (including relatives)	
Intermediate Assets		TOTAL CURRENT LIABILITIES	\$ <u>116,782</u>
Machinery, equipment, cars, trucks (Sched. B1)	\$ <u>56,059</u>	Intermediate Liabilities (Sched. B4)	
Breeding or work animals not to be sold within 12 mo.		(Show only balance due beyond 12 mo.)	
<u>40</u> Beef cows; _____ dairy cows; <u>2</u> bulls	<u>10,960</u>	Notes payable <u>cows and windrower</u>	\$ <u>13,240</u>
_____ 2 yr. old hfrs.; <u>10</u> yrlg. hfrs.	<u>1,500</u>	Sales contracts	
_____ Ewes & rams; <u>1</u> horses	<u>300</u>	Life insurance loans	
<u>20</u> Gtrs; _____ sows; _____ boars	<u>1,700</u>	Other intermediate term liabilities	
Securities not readily marketable (Sched. B2)	<u>300</u>	TOTAL INTERMEDIATE LIABILITIES	\$ <u>13,240</u>
TOTAL INTERMEDIATE ASSETS	\$ <u>70,819</u>	Long Term Liabilities (Sched. B4)	
Fixed Assets		(Show only balance due beyond 12 mo.)	
Farm real estate (Schedule B 5)		Mortgages on farm real estate	\$ <u>22,000</u>
Gross value \$ <u>157,000</u>		Land contracts	<u>75,600</u>
less: estimated cost of selling \$ <u>9,420</u>		Mortgages on other real estate	
est. capital gains tax \$ <u>2,000</u>	<u>145,580</u>	Other <u>Father</u>	<u>20,000</u>
Net value		TOTAL LONG TERM LIABILITIES	\$ <u>117,600</u>
Non-farm real estate (Schedule B 5)		TOTAL LIABILITIES	\$ <u>247,622</u>
Household goods		PRESENT NET WORTH	\$ <u>145,487</u>
TOTAL FIXED ASSETS	\$ <u>145,580</u>	TOTAL LIABILITIES AND NET WORTH	\$ <u>393,109</u>
TOTAL ASSETS	\$ <u>393,109</u>		

Insurance on crops Hail on corn \$ 80/ac Do you carry: medical insurance? Yes; accident insurance? Yes
 Insurance on bldg. (fire, ext. cov.) \$ 25,000 disability insurance? No; life insurance? \$40,000
 Insurance on mach., equip., & livestock \$ 56,000 Are any suits pending against you? No
 Liability insurance coverage \$ 150,000
 List notes co-signed for other people None

I certify that the above statement and the schedules on the reverse and attached are correct.

Date Jan. 5, 1972 Signature John Farmer Signature Mary Farmer
 Subscribed and sworn to before me this _____ day of _____, 19____, Notary Public in and for the State of Nebraska,
 _____ County. My commission expires _____, 19____ (SEAL)

Schedule B1 - Machinery, Equipment, and Auto Inventory

NOTE: YOU MAY WANT TO SUBSTITUTE LAST YRS. DEPREC. SCHED.

Item	Make & Model	Date acquired	Cost or other basis	Deprec. for past yr.	Current undeprec. balance
Auto	<i>Flem</i>	<i>1969</i>	<i>\$3000</i>	<i>\$270</i>	<i>\$2190</i>
<i>3/4 ton pickup</i>	<i>Ford</i>	<i>1969</i>	<i>2000</i>	<i>180</i>	<i>1460</i>
Truck	<i>2 ton Chev</i>	<i>1960</i>	<i>5700</i>	<i>None</i>	<i>570</i>
Tractor	<i>JD 4020</i>	<i>1969</i>	<i>6108</i>	<i>550</i>	<i>4459</i>
<i>Tractor</i>	<i>JD 3020</i>	<i>1965</i>	<i>3740</i>	<i>337</i>	<i>1384</i>
<i>Windrower</i>	<i>14' S.F.</i>	<i>1971</i>	<i>5125</i>	<i>461</i>	<i>4664</i>
Combine	<i>JD 14'</i>	<i>1969</i>	<i>9100</i>	<i>819</i>	<i>6643</i>
<i>Cornhead</i>	<i>6 row</i>	<i>1969</i>	<i>7525</i>	<i>677</i>	<i>5493</i>
Baler					
<i>Batch dryer</i>		<i>1969</i>	<i>5175</i>	<i>466</i>	<i>3778</i>
Irrig. equip.		<i>1967</i>	<i>30000</i>	<i>3000</i>	<i>15000</i>
<i>Grinder-mixer</i>		<i>1968</i>	<i>2000</i>	<i>180</i>	<i>1280</i>
<i>All other</i>				<i>1590</i>	<i>9138</i>
TOTAL			<i>\$</i>	<i>\$8530</i>	<i>\$56059</i>

Schedule B2 - Securities Inventory

Description and no. of shares	Original cost		Present market value	
	per unit	total	per unit	total
Marketable				
	\$	\$	\$	\$
TOTAL		\$		\$
Not Readily Marketable				
<i>Central Coop</i>	\$ 15-	\$ 300	\$ 15-	\$ 300
TOTAL		\$ 300		\$ 300
Schedule B3 — Supplement, Seed, Fertilizer, Chemical Fuel, etc. Inventory				
Item	Quantity		Value	
<i>Gasoline</i>	<i>600 gal.</i>		<i>\$ 150</i>	
<i>Oil</i>	<i>60 gal.</i>		<i>78</i>	
<i>Soy bean meal</i>	<i>5 tons</i>		<i>500</i>	
TOTAL			\$ <i>728</i>	

Schedule B4 - Inventory - Intermediate and Long Term Liabilities

	To whom	Purpose and/or property mortgaged	Final due date	Interest rate	Payment dates	Current outstanding prin. bal.	Portion of balance	
							due with- in 12 mo.	due beyond 12 mo.
INTERMEDIATE								
Notes	Bank	Windrower	6/1/73	8	6/1	\$3400	\$1700	\$1700
	Bank	Cow herd	11/1/75	8	11/1	14000	3500	10,500
	A SC S	Brain storage	11/1/73	3	11/1	2080	1040	1040
Sale contracts								
Life ins. Co. loans								
Other								
TOTAL						\$19,480	\$6,240	\$13,240
LONG TERM								
Farm R.E. mortgages	F.L.B	Buy land	11/1/95	8 1/2	1/1	\$23,000	\$1000	\$22,000
Land contracts								
	Father	160 ac.	7/1/88	6	7/1	80,325	4725	75600
Non-farm R.E. mortgages								
Other (specify)	Father	Downpayment - note only	None	6	1/1	20,000	-	20,000
TOTAL						\$123,325	\$5725	\$117,600

Schedule B5 - Real Estate Inventory

Tract no. or descrip.	Acres						Title held in name of	Date of purchase	Purchase Cost	Cost of improvements added	Estimated current market value
	Total	Irrig. crop	Dry crop	Hay- land	Range or past.	Waste					
FARM											
Home place	160	150				10	NW 1/4 Sec 16, T1N, R7E	7/1/68	\$ 104,000	\$ None	\$ 112,000
2	160		75		78	17	SW 1/4 Sec 10, T1N, R7E	11/1/65	37,500	8000	45,000
TOTAL									\$ 141,500	\$ 8000	\$ 157,000
NON-FARM											
TOTAL									\$	\$	\$

Prepared by Philip A. Henderson, Extension Economist (Farm Mgt.), and Thomas L. Frey, Ass't. Professor of Agricultural Finance and Farm Management.



EXTENSION WORK IN "AGRICULTURE, HOME ECONOMICS AND SUBJECTS RELATING THERETO,"
 THE COOPERATIVE EXTENSION SERVICE, INSTITUTE OF AGRICULTURE AND NATURAL RESOURCES,
 UNIVERSITY OF NEBRASKA-LINCOLN, COOPERATING WITH THE COUNTIES AND THE U.S. DEPARTMENT OF AGRICULTURE
 LEO E. LUCAS, DIRECTOR

In the example, two separate groups of steers are shown, differentiated on the basis of weight and/or value per head. Likewise, two groups of hogs are shown. Use the blank lines to write in appropriate designations and values.

In showing the quantities of grain on hand, combine bushels of dry and high moisture grain in the same figure unless you particularly want to keep these amounts and their respective values separate. Include the entire amount you own, including that sealed under CCC loan. You may want to squeeze in notations regarding the prices used in arriving at total values as illustrated in the example. The total tonnage of all hay, straw and silage, and their value should be shown. Again you may want to make pencil notations to denote the kind of hay and whether it's loose or baled.

With today's increasingly complex farm business, you may have a sizeable inventory of supplement, seed, gasoline, etc., on a given day. You will either owe for these supplies or will have already used cash to pay for them. In either case, it is essential that all such items be inventoried and valued at cost (or market value if it is lower). Compile the inventory in schedule B3 on the reverse side of the balance sheet, and transfer only the total to current assets on the balance sheet.

The method of showing a growing crop as an asset has long been debated. In most cases there is nothing marketable until the crop matures; and yet, very sizeable out-of-pocket expenditures may have been incurred. In addition, the crop will normally mature and generate a very real asset within a few months. Therefore, a generally accepted practice is to show the total dollar out-of-pocket investment you have in each crop in the form of seed, fertilizer, chemicals, gasoline, etc. as current assets. With balance sheets prepared at the recommended time of December 31, only the fall annual crops like wheat and rye will be of concern. If a balance sheet is prepared at another time during the year, the investment may be greater.

Intermediate Assets

Schedule B1 on the reverse side of the balance sheet is provided for listing the major pieces of machinery and equipment. Space does not permit a detailed listing of all machinery and equipment so it will be necessary to group a good bit of what you have. The values should be the depreciated values. These can be calculated from your income tax depreciation schedule by subtracting the amount of depreciation allowed in prior years and the amount of depreciation for the immediate past year from the cost or other basis. You may want to attach a copy of your income tax depreciation schedule to the back of your balance sheet.

The number, kind and value of breeding animals should be entered under intermediate assets with the exception of those to be sold within the next 12 months. The latter should be entered in the current asset section. Use current market value on raised breeding animals as nearly as you can estimate them, as well as on purchased breeding animals. Female stock such as heifers or gilts being kept for replacement purposes should be itemized in this intermediate asset section. Saddle horses and work horses should also be included in this section as well as brood mares and stallions.

The value of securities not readily marketable such as coop stock, or Production Credit "B" stock should be listed in schedule B2 on the reverse side and the total value of such stock entered in this section on the line provided.

Fixed Assets

Schedule B5 on the reverse side of the balance sheet is provided for a detailed listing of real estate, by "farm" and "non-farm" categories. If you operate more than one tract of land, identify each tract in your record system for ease of reference. The rather extensive detail called for on each tract of land will be especially helpful to anyone else reviewing your balance sheet. You will find the acreage breakdown useful when you are making cash flow projections for the following year. The exact way real estate title is held, i.e. whether title is held by you alone or with your spouse and whether you hold title in joint tenancy, as tenants in common, or in some other way, is information a lender may need. Enter your total current market value of farm real estate in the "Gross Value" blank on the front of the balance sheet. Deduct the estimated cost of selling and the estimated capital gains tax which would result if you were to sell your farm real estate. The result is the "Net Value", which is entered in the asset column. This adjustment is necessary, as you could not convert the current value of your farm into cash without incurring some costs. The amount of capital gain can be estimated by comparing the purchase cost plus the cost of improvements added with the estimated current market value. The capital gains tax will depend on a number of factors, but you can estimate it by taking 10-15% of the gain, if you do not want to make a more accurate estimate by using IRS tax tables.

Now enter the net value of non-farm real estate on the front of the balance sheet from Schedule B5. There is some debate as to whether household goods should be entered on the balance sheet. But, if you are careful to list each debt or other liability, there is a case for listing each and every asset, including your household goods.

Total Assets

Each section (current, intermediate, fixed) should be totaled by itself and the amount shown in the space provided. The sum of the three totals will be the total value of all assets which should appear in the last value space on the asset side.

Current Liabilities

Under "open or charge accounts," include all amounts owed for purchased items which are not backed by notes or mortgages. An obligation is created at the moment of purchase or service rendered. If payment for such items has not been made, the obligation should appear on the balance sheet. This would include amounts payable for feed, fertilizer, seed, fuel, oil, doctor bills, etc.

If such accounts have been outstanding long enough to have accrued an interest charge, the total amount of such accrued interest due should be shown in the space provided under "accrued interest." In addition, show the amount of interest accrued on notes, mortgages, and delinquent taxes as of the date of your balance sheet even though the interest may not be payable until some later date. The detailed listing of intermediate and long term liabilities on schedule B4 on the reverse side of the balance sheet will be useful in computing the accrued interest on intermediate notes and long term liabilities.

Accrued interest assumes that interest becomes an obligation immediately upon use of borrowed funds, even though not yet due. Therefore, interest accrues daily, based on the volume of money borrowed and the interest rate. For those principal amounts where interest has not yet been paid, you will need to determine the length of time the various amounts were outstanding and what the amount of unpaid interest is for each. Your accrued interest entry on the balance sheet would be the sum of these calculated interest charges.

Under accrued taxes, show the amounts which have accrued even though payment is not due until sometime later.

There is a considerable time lag between the time the tax obligation develops and the time payment is due. For example, on real estate taxes, assume a Nebraska farmer's balance sheet as of December 31, 1972. During 1972, on April 1 and August 1, the first and second half respectively of 1971 taxes (covering the period January 1, 1971 to December 31, 1971) would be payable. It is clear that any unpaid balance from the April and August payments would be delinquent on December 31, 1972 and would show in the balance sheet. In addition, on December 31, 1972 he would owe real estate taxes for the entire year 1972, even though he would not yet have received a statement showing the amount of taxes. These should be estimated.

Personal taxes are a little different. Here a farmer is assessed on: 1) property owned on January 1, plus 2) the value of grain produced during the past year. While the tax liability on grain becomes an obligation following harvest and for other personal property on January 1, payment is not required until the following December 1 and the succeeding July 1. So for the balance sheet on December 31, you have an obligation for the second half of property taxes resulting from the previous January 1 assessment (payment of which will be due July 1) plus accrued taxes on your grain production for the past year (4 mills per bushel on corn, soybeans, wheat, dry beans and flax, and 2 mills per bushel on all other grains.)

Income tax is an obligation as of December 31, even though one will not likely know for a month or so the exact amount of the obligation. An estimate is the best one can do here.

Accrued cash rent should include the amount of cash rent accrued (but not yet paid) up to the time of the inventory or balance sheet, for use of corn stalks, buildings, pasture, machinery, etc., even though actual payment is not called for until some later date.

The notes payable section should include a detailed listing of all notes currently outstanding and having a final due date within 12 months. Show the name of the payee, the maturity date, and the purpose as well as the amount.

Principal payments on intermediate and long term loans which are due within the next 12 months as shown in the next to the last column of schedule B4 on the reverse side of the balance sheet should be entered as current liabilities.

The dollar value of all judgments and mechanic liens against you, and/or your spouse should be shown in the space provided.

The amounts of CCC loans which you have obtained should also be included, regardless of how you intend to fulfill this obligation. Be sure all grain under CCC loan is shown under assets.

Intermediate Liabilities

That portion of notes or sales contract not due within the next 12 months but due within 10 years should be shown in this section on the appropriate lines. The amount of loans secured by life insurance is included here since such loans do not have specified maturity dates. Any other intermediate term financial obligations should also be shown.

Fixed Liabilities

That portion of long term debt such as real estate mortgages, land contracts, or other long term obligations which is not due within the next 12 months should be shown in this section. The detailed supporting information should be shown in schedule B4 on the reverse side of the balance sheet.

INTERPRETATION OF THE BALANCE SHEET

Two different motives prompt interpretation of the balance sheet. First is the farmer analyzing his own business and trying to draw appropriate conclusions, and second is the creditor attempting to evaluate a man and his business in relation to a loan request.

Skillful use of a balance sheet requires knowledge of both its uses and limitations. In the past, lenders may have placed a heavy reliance on balance sheet analysis of farm loan requests. Current trends show that what may have been sacred ratio analysis guidelines in the past are insufficient today. Details about the profitability of a business and a detailed analysis of anticipated income and expenditures and when such activity will occur are also needed.

The balance sheet reveals the net worth an individual has achieved, and a series of these statements indicates the rate of growth. The absolute size of net worth partially indicates ability to accept risk and the chance of continued operation even in the face of financial setbacks. The ratio of total debt to net worth relates the amount of debt capital to that being supplied by the farmer. As a general statement, lenders prefer that total debt not exceed the net worth. However, farm operations are now requiring increasing amounts of capital, and credit is the major source. As debt to net worth ratios exceed one (for example, a \$160,000 debt in relation to a \$140,000 net worth equals a 1.14 ratio), the importance of further information increases. Payments on debt are fixed obligations and thus one must consider the absolute size of the total liabilities in relation to size of total business as shown by total assets and by the potential for generating income. The current assets to current liability ratio shows a so-called working capital position. When current liabilities exceed current assets, a business may become vulnerable. Again there is no one "ideal" relationship. Creditors find a 2:1 ratio desirable but many good operations fall short of this. Intermediate assets are the "production" assets — machinery and breeding livestock. These assets in conjunction with the fixed assets give a quick indication of potential productivity.

SUMMARY

The balance sheet, sometimes referred to as a financial statement or net worth statement, is probably one of the most commonly used financial management tools. Nearly everyone has used a map to plan travels ahead. In every case, it was essential to know "the starting point." So it is with the balance sheet — it describes in detail where you are financially, and the bases from which future progress can be made. It gives the inventory of assets so basic to financial planning and analysis. With a series of statements, progress as measured by net worth change over time can be described and observed.

Two notes of caution. First, a series of balance sheets does not reflect profitability of an operation, but rather, it shows only the extent to which profits have been used to increase equity in the business. It takes an income statement such as EC 71-854 to examine profitability. Second, the balance sheet should not be used to determine the ability of a business to meet loan repayments — that is the task of a cash flow analysis such as that shown by EC 71-852. The balance sheet is a powerful financial management tool, but must be supplemented with an income statement and a cash flow analysis.

A FINANCIAL MANAGEMENT SERIES FOR NEBRASKA FARMERS & RANCHERS

EC 71-846	YOUR PLANS FOR PROFIT
EC 71-847	YOUR BALANCE SHEET
EC 71-848	YOUR INCOME STATEMENT
EC 71-849	CASH FLOW PLANNING WITH THE AID OF YOUR INCOME TAX RETURN
EC 71-850	CASH FLOW PLANNING WITH THE AID OF YOUR RECORD BOOK AND BUDGETING
EC 71-851	ESTIMATING YOUR FAMILY LIVING EXPENSES
EC 71-852	CASH FLOW PLANNING FORM
EC 71-853	BALANCE SHEET
EC 71-854	INCOME STATEMENT

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