

Part IV Integrating Financial Management & Human Resource Management

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Integrating Finance & Mgmt – 5 Issues

- Role of Chief Financial Officer (CFO)
 - Duties, proficiencies, & performance expectations
 - Who is CFO now...who should be?
- Financial Policies & SOP's
- Building financial management knowledge – owners and management team members
- Use of Peer Groups for Performance Review

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1 CFO Role

- Emerging as **key position** in Ag Businesses
 - Unique skills needed to manage technology, finance, & information management
 - Can't be "jack of all trades" - agronomist, GPS expert, mechanic, marketer, herdsman
- Career Path: Bean counter → Financial Analyst → Strategic Planner → CFO → CEO

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TEPAP Survey Results*

Financial positions staffed in farm business...

Bookkeeper	68%
Office Manager	43%
Controller	20%
Chief Financial Officer	34%

*Based on 44 responses January 2015 TEPAP Year I

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Duties, Skills & Expectations- CFO

- **Primary role:** provide information & analytical services that help others optimize decisions
- **Focus areas**
 - Empower members of management team
 - Administer accounting system & MIS
 - Facilitate/coordinate financial planning and budgeting
 - Capital investment analysis
 - Arrange financing - operating and strategic plans
 - Performance analysis - whole business; management segments; cost of production; ABC's

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Finance (CFO) and Marketing

- Budget preparation and variance analysis
- Maintain records and circulate to management team
- Arranging credit for operating and capital purposes
- Banking responsibilities
- Member of executive committee; key player in strategic planning
- Capital investment analysis; negotiate purchases
- Market grain commodities
- Preparation of tax returns
- Manage insurance & risk management programs
- Liaison with attorney on legal matters

Detailed description www.wittmanconsulting.com

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Challenge: Converting Data to Decisions

- Data - numbers-meaningless by themselves
 - yield data, transaction journals, calving records
- Information - data transformed into medium we can understand
 - color maps, graphs, financial statements
- Knowledge - Human understanding applied to information
 - Ratio analysis, profit/cost center, herd data
- **Better Decisions:** Ultimate payoff → improved profits & financial performance

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Who is CFO now...who should be?

Questions we should ask:

“How much time do I currently spend on each function?”

“...how much time should I spend?”



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Where do you find a good CFO?

- 3 TEPAP alumni – multi-site grain operations and farm supply businesses
 - Hired controller/CFO away from big firm making over “6 figures”/yr ...60 hrs/wk
 - \$75,000/yr for 30 hrs/week
+ \$35,000 secretary/data entry person
 - Formed service bureau with office, computers, accounting systems, 401k
 - Total cost = \$150,000 split 3 ways
- Rent-a-CFO

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Defining Financial Policies and SOPs 4 Sloppy Areas

- Compensation/division of earnings
- Capital contributions/withdrawals
- Inter-entity transactions/transfer pricing
- Intra-family financing practices

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Dividing Returns: Mgmt vs. Owners

Assumptions:

Farm Operating Margin* = \$400,000

Position	Value of Mgt/Labor**	Ownership Share
Sr. Farm Manager	\$60,000	50%
Asst. Farm Manager	50,000	30%
Jr. Farm Manager	40,000	20%

* Margin before management and owners are compensated

** Excluding \$40,000 non-cash employee benefits

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Process for Dividing Returns

Farm Operating Margin		\$400,000
less: Mgmt / Labor Allocation		<u>150,000</u>
Balance to Allocate to Owners		\$250,000
Sr. Farm Mgr	50%	\$125,000
Asst Farm Mgr	30%	75,000
Jr. Farm Mgr	20%	<u>50,000</u>
		\$250,000

Total Returns:	Mgmt	Ownership	Total
Sr. Farm Mgr	\$60,000	\$125,000	\$ 185,000
Asst Farm Mgr	50,000	75,000	125,000
Jr. Farm Mgr	<u>40,000</u>	<u>50,000</u>	<u>90,000</u>
Totals	\$150,000	\$250,000	\$400,000

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Policy on Path to Ownership Capital Contributions, Withdrawals

- Minimum balances to maintain?
- Should everyone be “equal?”
- Is revenue earned based on ownership ratios or other criteria?
- Compensation for excess balances?
- Who can invest in the farm?
- “*Can I ever get my money out?*”

Audience experience with these problems?
...only 1 in 5 say they have a policy!
...MANY have problem & DON'T KNOW IT!

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Example: Minimum Capital Target*

Minimum Capital Target = \$5,000,000

Owners	Share	Book Capital	Target	Excess (Deficit)
Partner A	50%	\$3,000,000	\$2,500,000	+500,000
Partner B	30%	1,500,000	1,500,000	-0-
Partner C	20%	800,000	1,000,000	(200,000)
Totals	100%	\$5,300,000	\$5,000,000	+300,000

*Based on goals set for debt/asset ratios & working capital

...Are you getting your \$'s worth from your professional advisors?

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Farm Balance Sheet

A S S E T S	D E B T S
	N E T Partner A- 50%
	W O R T H Partner B- 30%
	Partner C- 20%

Beginning NW + Earnings – Withdrawals = Ending NW

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Good Management Practice

Make Valuation Equity Transparent!

Owners	Book Capital	Unreal Gain*	Total Equity
Partner A	\$1,750,000	\$1,300,000	\$3,050,000
Partner B	1,500,000	1,113,000	2,613,000
Partner C	900,000	675,000	1,575,000
Totals	\$4,150,000	\$3,088,000	\$7,238,000

*Unrealized Gain (Valuation Equity) = 43% of Total Equity Value

...How much of your NW is YOURS vs. TAX owed to government?

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Retained Earnings and Capital Withdrawals – (Partnerships and Sub S Corporations)
SAMPLE POLICY

The amount of capital provided by each capital provider is a key component in determining how net revenue of the business will be shared among owners or risk takers. The partners, joint members, or stockholders providing capital shall establish at least annually a common agreement on the base level of capital each capital provider is expected to keep invested in the joint operation. This base level will be established giving consideration to:

- Minimum financial constraints or objectives (i.e. targets for working capital level, debt to equity ratio, and borrowing reserves)
- Needs of the business to fund future growth
- Ratio of ownership each capital provider wishes to maintain for future revenue sharing.

An analysis of capital account balances will be done following final draws for tax purposes on April 15 annually. Capital providers can withdraw excess capital for personal living and tax payments, outside investments, or other needs. Excess funds can also be loaned to the joint operation at a market rate of interest.

If a capital provider cannot maintain a target capital share level after an extended shortage situation, the partners will re-evaluate the at-risk capital resources provided and adjust the revenue sharing arrangement to reflect the change in capital contribution level.

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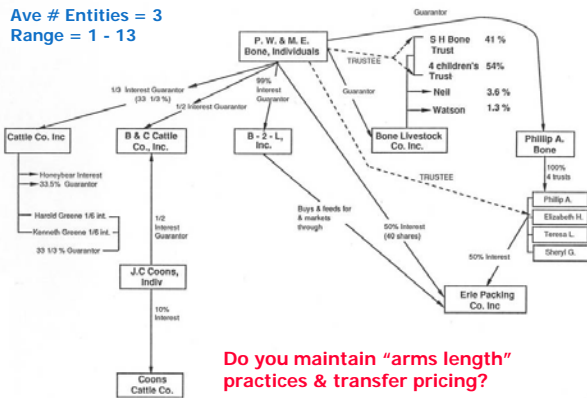
Inter-entity/Insider Transactions

Keeping Policies “Arms-length”

- Common Situations:
 - Personal side-ventures
(Use of feed, farm inputs, supplies, pasture)
 - Loans to the business
 - Leases of land/equip to/from the business
- Are transactions done on “arms-length” or competitive market basis?
- Arrangements renewed regularly?

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Ave # Entities = 3
 Range = 1 - 13



Do you maintain “arms length” practices & transfer pricing?

Source: 1989 Financing Multiple Entities – Wittman Cartoon

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Using Intra-Family Financing

\$50,000 to invest

Gen I John

6% Rate

Gen II Sue

Bank MM Rate = 3%

Lender Rate 9%

Could owners loan funds to the business?

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Building Financial Management Knowledge Owners and Management Team

- Lifetime learning process
- Individuals responsible for own education ... CFO only coach & trainer
- Engage full management team in data collection, analysis, technology use
- Share records professionally

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Are Your Farm Records ...



- Open to all?
- Circulated monthly?
- Reviewed annually?
 - cash vs. accrual
 - cost and market value balance sheets
 - profit & cost center (enterprise) analysis
 - key ratio calculations – trend analysis

Confucius say: "People do what is inspected... not what is expected!"

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Peer Groups Comparisons

Benchmark Groups

- FBFM Associations
- "20 Groups" – Spader
- Local "information exchange" groups



"Comparability" Pitfalls

- Non-standardized data
- Dissimilar operations, agronomics, climate, enterprises
- Un-reconciled year-year data

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Financial Literacy Resources


- Farm Futures Magazine/FFSC – Financial Boot Camp
→ <https://www.farmfuturesummit.com/en/ag-finance-boot-camp/boot-camp>
- King Ranch Institute – Managerial Acctg Lectureship
→ <http://krim.tamuk.edu/accounting/>
- NW Farm Credit System – Learning Center
→ www.northwestfcs.com/eLearning
- Centrec Consulting
→ www.centrec.com/self-study
- Farm Financial Standards Council – Financial Guidelines
→ www.FFSC.org
- Wittman Consulting-Financial models, templates, trend sheets
→ www.wittmanconsulting.com
- FINPACK – ratio definitions, templates
→ www.cffm.umn.edu/finpack/
- Wisconsin-PDPW: Financial Literacy Program
→ www.pdpw.org/programs/PDPWFinancialLiteracyForDairy20192020/details
- Kansas (Approved for FSA Borrowers Financial Training Credit)
→ <https://www.fsa.gov/whats-new/2019/08/2019-fsa-borrowers-financial-training-credit>

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Time to Head to the Barn!

Key Points – Finance I

- Your challenge: Data → Information → Knowledge → **Better** Decisions
- Add key financial “gauges” to your dashboard
- Use proven models to optimize results
- Empower whole business team to understand and benefit from good financial mgmt



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Do we seek better management skills
“just for the fun of it?”

Wheel of Life- 7 Habits

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