AGRICULTURAL
FINANCIAL AND TAX PLANNING
Making the Ranch Operation Profitable

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In the past couple of issues of the Florida Cattleman Journal our articles were focused the Internal Revenue Service's ("IRS") use of the Hobby Loss rules to increase tax exposures of ranch operations. As discussed in the articles the best defense is to have a profitable business and have the knowledge and documentation to support the profit motive of the operation that has not shown a profit in two out of the last five years.

Current forecast for the cattle industry

The recent good news is in Burt Rutherford's June's article in the Beef Magazine. His conclusion is that optimism of ranchers has significantly increased so far in 2017. However, per The Beef posting of July 5, fed cash cattle market has dropped $26 in May and June to levels not seen since January 2017. Optimism is great but increased profit is the goal.

Quick review of our recent articles to emphasis how to increase profits

Having a written budget provides a focus for one's operation and support for an IRS audit. It also identifies key points that measure the activity of the operations and its progress. Items such as feed cost and product selling prices can change quickly and can have a significant impact on the business. By establishing a good budget the manager can identify changes in the cattle industry as they impact the operations. This will give the manager time to develop changes in the operation to counter the negative impacts and to maximize the positive impacts. As discussed in our previous articles, per Stan Bevers and David Anderson of Texas A & M University, the budget should identify key performance indicators "KPIs" for the business to be successful in the long run. Some examples of KPIs that have been covered in prior articles are;

1. Pregnancy rate
2. Pounds weaned as a percent of the dame's weight
3. Revenue per calving dame
4. Cost per CWT. of weaned calf
5. Total cost of developing heifers
6. Total cost of developing purchased heifers
7. Direct input cost of breeding herd as percentage of total cost of ranch operations
8. Labor as percentage of total revenue
9. Equipment cost as percentage of total revenue
10. Operating expense excluding interest and depreciation as percentage of revenue
11. Net income ratio

12. Debt per breeding female
13. Equity to Asset Ratio
14. Asset turnover ratio
15. Rate of return on land (including other sources of income other then cattle)
16. Other activities that increases income per ranch operations such as blue berries, timber, etc

In order to survive and even grow in a downturn of the cattle market it is imperative that cost be controlled daily.

1. Have KPIs been identified and monitored for the operation?
2. If so, are they being calculated properly? For example when calculating the revenue per breeding female how are the culls, death losses and the calves kept for the breeding herd handled?
3. If KPIs are known are they being compared to prior years operating KPIs and/or compared against third party numbers like those calculated by the Texas A&M University?
4. Have you calculated the value of investing in genetics of your herd verses investing in land and equipment

As we discussed in our April article, review the data that you currently have to identify variable cost that might have the least impact on the overall performance of the herd. Are you spending more on your maintenance of bulls than on the improved genetics of your bulls? Did you over or under develop your heifers? New data indicates that first breeding at 55% of mature cow weight is adequate as opposed to the traditional considered 65% required weight. Is the size of your cows giving you a maximum return per acre? Studies are showing that a smaller cow provides a better return per acre because of a higher pregnancy rate and lower maintenance cost (feed) per pound of beef produced. Consider using technology in your operations such as “Artificial Insemination along with Synchronization” (AI) to improve the herd performance. In a case study at the UF North Florida Research and Education Center, AI produced an increase of 6% in weaning rate and a 38 pound increase in weaning weight. With the lower prices of heifers it may be a good time to improve the herd by culling the underperforming and adding genetically improved new heifers.

Consider grazing vs. making hay and buying additional hay as needed. Do you know your true cost of producing hay? If you do produce hay, should a third party harvester be hired instead of using your equipment and labor? A small operation that owns its equipment could have cost that exceeds $200 per ton. Remember that 90% of what goes in a cow is expelled at the rear. When hay is purchased the 90% organic matter is a net add of minerals to your pasture. Your other input cost such as feed supplements and minerals is another area were cost savings of up to 25% might be realized via prudent choices and negotiations when purchasing. The convenience of tub supplements over the liquid form carries a significant cost that could be eliminated. Research your sources and benefits of your feed and supplements to carve out cost. Many more areas for cost improvements may be identified like: vehicle usage, overhead items, pasture maintenance and equipment cost. A systematic review of all of you cost should be made with an awareness of the operation’s capital reserves when compared to any projected cash burn rate.

Team up with your financial advisor.

Having the right financial team can provide critical financial and operational information timely to the manager/owner so proper decisions can be made based on facts and not just on gut feelings. In today's world of razor thin margins there is no room for errors in your numbers. Your financial advisor can help review and/or prepare a budget for your operation that identify and calculate KPIs which will provide new tools to better manger the operations. These numbers should be reviewed at least quarterly.

Summary

The main purpose of this article is to discuss the importance of having a financial plan and establishing methods to measure how you ranch performance compares to those plans and third party KPIs. In this period of market flux good financial information is critical for the manager to make the correct timely decision. If the financial and herd management data system in your business does not provide this type of information timely, consideration should be given to update that system(s). If system improvement is needed, find a financial advisor that understands your ranch operation so they can help with the improvement of your system.

In addition, a written plan provides a focus for everyone in your operation. It helps the operations look at the total profitability and performance on a per acre basis instead of revenue per cow. Include other sources of income that might be generated from alternative uses of land discussed above. A financial plan also aids in tax planning so questionable expenditures are avoided like buying additional equipment to reduce taxes when it has a negative impact on your KPIs and cash flow. In the current market, financial analysis by management is critical and your financial advisor should be able to help with that process.

For more information on this topic and other tax planning for ranching, please contact me at (863) 640-2008 or Tom@beasleybryantcpa.com and/or Ryan Beasley at (863) 646-1373 or Ryan@beasleybryantcpa.com . Please visit our website at www.beasleybryantcpa.com for information on other relevant topics.

We at Beasley, Bryant & Company, CPA's, P. A. are experienced in agricultural business problems, tax issues or concerns, and are here to help you.

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