A Letter to the Members
By: Jim Kurtz

Dear Association Members -
Four years ago I retired from UMN Extension, but for a number of reasons opted to stay with your Association as a Contract Fieldman (or more appropriate now – Field Person). The reasons included the fact that the manpower of the remaining staff was not real strong in 2011 (not that it should have been a big concern to me, but it was). Also, I was not really ready to wind my career down and quit working all together. Friends and family have advised me all along, that when it was time for me to retire, I will know it. At this time, I believe they are correct, as the time feels right. I never wanted to stay on so long that the mind or body just couldn’t keep up. I hope my assessment is correct and that has not yet happened.

None of us know how long we will be blessed with good health, a good mind, a lot of interests and curiosity, and a spouse that has these as well. At this point, life is wonderful! In fact, I am writing this in the camper, parked a few miles between Bryce Canyon and Zion National Parks in southern Utah. We are happy for this trip and would like to think that many more are waiting to happen.

The manpower of your association (both UMN Extension and Contract) is the strongest it has been in the past several years. You have a great crew of dedicated and talented people working with you and for you. Again, that probably should not be a strong driver in my decision of when to retire, but when you care about the cause you are working for, you do want it to thrive.

I have enjoyed the opportunity to work with each of you. Your Association is made up of a wonderful group of professional farmers. You are smart, well-educated, successful, eager to learn, and ethical in your ways. Thank you for the privilege! It is you the people that I will miss the most. I hope to bump into you now and then in the future.

I have a few loose ends yet to complete for the Association, but the workload is winding down, and feels very good. Take care, and best wishes for the future!
Transitioning Clients & Field Staff
By Don Nitchie

Jim Kurtz announced his retirement from association work. He has been working part-time since his 2011 retirement from a full-time University position as fieldman for the association. We thank Jim greatly for all of his work and the expertise he has brought to the association. Personally, he was a big help to me as I started, and I have appreciated having him continue as he has the past four years. He has been a great colleague to the association.

Business planners urge good managers to plan for transition of responsibilities on their team. We have a plan to transition Jim’s remaining clients to field staff and will be communicating directly with those clients in the next few days. It has worked well to bring on new staff and train them with experienced staff. It has also been beneficial for all that we as staff work as a team. Although you may only meet with your field person for a farm visit, tax planning and analysis or tax preparation, they have a team of professionals backing them up. When one of us runs into a unique challenge, we work together for research and advice. We do this for consistency and to take full advantage of the knowledge and experience of the team.

I think you can feel very good about the depth and breadth of our team’s knowledge and experience beyond just taxes and financial analysis. Each team member brings with them several aspects of experience in the agricultural financial world. There is direct farming experience, banking, commodity marketing, personnel management, account management in agribusiness, farm financial analysis, and tax preparation. In all of these capacities, most importantly, there is a wealth of experience among all team members in building and maintaining trusted working relationships with agricultural producers.

We will miss Jim, but he has helped us build a firm foundation to move forward.

Managing Your 2015 Profitability-Small Improvements Add Up!
By Don Nitchie

The table below can also be found on page 21 of your SWMFBMA Annual Report. It shows the assumptions used to determine the likely outcomes for the average association farm in the second table that follows. The first column looks at the impact of a 5% increase in gross income or revenue, through improved selling prices, yields, or both-combined with a 5% decrease in costs. This decrease in costs could be from negotiating lower purchase prices for inputs, more effective use of inputs applied, or a combination of both.

Secondly, the most probable outcomes for the average association crop farm and statewide average livestock farm with no management changes are illustrated in the columns to the right. In our discussions with the Center for Farm Financial Management staff and association staff and after review of numerous forecasts by Ag economists, we felt that crop farm gross incomes could likely be 5% lower in 2015 even though operating costs may be down 4%. We also felt that gross incomes for the average livestock farm could be down 19% in 2015 from the record highs in 2014.

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<tbody>
<tr>
<td>Gross Income</td>
<td>+5%</td>
<td>-5%</td>
<td>-19%</td>
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<tr>
<td>Operating Expenses</td>
<td>-5%</td>
<td>-4%</td>
<td>-2%</td>
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<tr>
<td>Interest Rates</td>
<td>-</td>
<td>+1%</td>
<td>+1%</td>
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<tr>
<td>Current Assets</td>
<td>+5%</td>
<td>-8%</td>
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<td>Noncurrent Assets</td>
<td>-</td>
<td>-5%</td>
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"Managing Your 2015 Profitability Small Improvements Add Up"
The next table shows the likely results on numerous financial measures for the average farm in 2015, if the previous assumptions come true.

The second column shows the results if the average association farm improves gross revenues by 5% and lowers operating costs by 5% over 2014 for 2015. It is striking that just these small changes result in Net Farm Income almost doubling to $207,093, Return on Assets more than doubles from 2% in 2014 to 5% in 2015, and Net Worth grows by 9%. Repayment Capacity also improves from 1.4 in 2014 to 2.6 in 2015. This is a significant improvement across several key financial measures. Small changes have a BIG impact on your bottom line.

Is it possible to achieve a 5% improvement in gross revenue? Probably - by doing a little better than average on selling prices, yields, or a little of both. Is it possible to lower costs by 5%? Probably - it is true that successful managers do a lot of little things just a little better rather than doing one thing really well. Being more effective with expenditures on inputs is the key. Getting the most revenue possible for each dollar spent on herbicides, pesticides, seed, fertilizer and feed etc. Sharpen your production management skills. Know where your costs are relative to competitors. It pays off when profits are scarce!

### Put your analysis and benchmark reports to work.

By: Garen Paulson, SWMFBMA Analyst

A benefit of membership in the Southwest Minnesota Farm Business Management Association is the comprehensive year-end analysis and your individualized benchmarking report. Used together, these reports can help you identify your farm’s strengths and weaknesses. Your farm is benchmarked with your peers in SWMFBMA using the standardized methods, so you can be assured that the comparisons are valid.

I encourage you to study your analysis and the last several years of benchmarking reports to identify trends on your farm.

Your year-end closeout analyzes your farm in terms of profitability, liquidity, and solvency. Looking first at profitability, how does your farm compare in terms of net farm income and rate of return on assets? Over time are these factors towards the top percentiles? Profitability is volume times efficiency. Look at the volume factors of gross farm income and asset turnover rate and the efficiency factor of operating profit margin. What is your strength, weakness? If one is weak and the other strong, what can you do to improve the weakness while maintaining the strength? In crops, if your volume is low, look at yields and value per unit. Over time are you toward the top or bottom? If your volume is good but efficiency is lacking, look at your costs. What can you do to improve costs without hurting volume?

The most common liquidity factor is working capital. While working capital is important, I prefer to look at term debt coverage ratio. This ratio ties your profitability to your loan commitments. A ratio of less than one indicates not enough profitability to cover your commitments. If your ratio is less than one, working capital and equity will suffer. Most banks, when looking at cashflows, like to see a ratio of at least 1.1, indicating a 10% cushion. How is your farm doing over time?
The most common solvency ratio is debt to asset ratio. This factor indicates how much of your business you own and how much your lenders and deferred taxes own. The median farm in SWFBMA is 34%. How are you doing? Is it a strength or a weakness? Look at change in retained earnings. Are you earning enough to cover family living and taxes with enough left over to cover term debt payments and improve working capital? Look at family living; family living is a significant cost to farms in SWFBMA – 13% of gross farm income was spent on family living for the average farm in 2014. How is your farm doing?

Knowing your farm’s strengths and weaknesses will be important as margins continue to narrow. Your analysis and benchmarking reports can help you in this process.

**What Can You Do About Your Liquidity and Solvency?**

By: Jim Kurtz

Your balance sheet gives you a snapshot of your financial position at a given point in time. Association members fill out their balance sheets as of January 1st of each year (or if your business year begins at a different date, it is the beginning of the year) for a number of excellent reasons. This allows for consistency of dates from year-to-year, and it makes it possible to do an accrual-adjusted income statement to measure profitability.

The balance sheet shows your financial condition as of that date. This financial condition is measured by liquidity measurements (current ratio, working capital, and working capital to gross revenues) and solvency measurements (debt to asset ratio, equity to asset ratio, and debt to equity ratio). Liquidity measurements deal with the relationship of your current assets and current liabilities and measure your ability to meet your financial obligations on a timely basis. Solvency measurements deal with the total assets, total debt and net worth and measure your ability to repay your debts if you were to liquidate your assets.

It may seem like you have no control over your balance sheet and how it changes year-to-year, but I would claim that no one has a greater control over your balance sheet than you do. Most of your financial actions affect your liquidity and solvency. We are going to look at six examples of everyday activities. You determine what affect each has on your: a.) Current Ratio b.) Debt to Asset Ratio and c.) Net Worth. The answers will be found in a different location in this Newsletter.

1. **Sell Current Assets (perhaps grain) and pay Current Debt**
   a. Effect on Current Ratio (Increase, Decrease or No Change)
   b. Debt to Asset Ratio (Increase, Decrease or No Change)
   c. Net Worth (Increase, Decrease or No Change)

2. **Sell Current Assets (perhaps grain) to accelerate Long-Term Debt**
   a. Effect on Current Ratio (Increase, Decrease or No Change)
   b. Debt to Asset Ratio (Increase, Decrease or No Change)
   c. Net Worth (Increase, Decrease or No Change)

3. **Sell Current Assets (perhaps grain), and keep as cash**
   a. Effect on Current Ratio (Increase, Decrease or No Change)
   b. Debt to Asset Ratio (Increase, Decrease or No Change)
   c. Net Worth (Increase, Decrease or No Change)

4. **Buy Current Assets (perhaps feeder livestock), with a Short-Term Loan**
   a. Effect on Current Ratio (Increase, Decrease or No Change)
   b. Debt to Asset Ratio (Increase, Decrease or No Change)
   c. Net Worth (Increase, Decrease or No Change)
5. **Buy Intermediate-Term Assets (perhaps equipment) with a Short-Term Loan**
   a. Effect on Current Ratio (Increase, Decrease or No Change)
   b. Debt to Asset Ratio (Increase, Decrease or No Change)
   c. Net Worth (Increase, Decrease or No Change)

6. **Refinance Short-Term Loan into Long-Term Loan**
   a. Effect on Current Ratio (Increase, Decrease or No Change)
   b. Debt to Asset Ratio (Increase, Decrease or No Change)
   c. Net Worth (Increase, Decrease or No Change)

*Sources: SWMFBMA 2013 Annual Report; 27 years of ag. banking and 14 years working with SWMFBMA members.*

**Answers to – What Can You Do About Your Liquidity and Solvency?**

By: Jim Kurtz

If the article on “What Can You Do About Your Liquidity and Solvency?” sounds a little like a “test”, I guess that is the teacher in me coming out. But honestly, we are tested every day. Our actions have consequences. Thankfully members of SWMFBMA have excellent farm records and analysis and have gained in their understanding of what all the analysis terms, ratios and measurements mean. This understanding is crucial to your future and will help determine whether you fail, survive or thrive. Congratulations to you for having the financial tools that you have.

The answers to the “Increase”, “Decrease” or “No Change” on the Current Ratio, Debt to Asset Ratio and Net Worth are:

1. a. Increase b. Decrease c. No Change
2. a. Decrease b. Decrease c. No Change

3. a. No Change b. No Change c. No Change
4. a. Decrease b. Increase c. No Change
5. a. Decrease b. Increase c. No Change
6. a. Increase b. Decrease c. No Change

Review how you did. You will notice the relationship of your current assets and current liabilities can affect your Current Ratio in different ways. Whenever you increase debt by purchasing assets, your Debt to Asset Ratio increases. Moving debt around on your balance sheet affects liquidity, but not solvency. Notice that the Net Worth was not affected by any of these activities. Your Net Worth increases or decreases based on your net income and how much was spent (family living and taxes). When earnings exceed spending and taxes, the “cost basis net worth” increases. Changes in market value of assets also affects the “market value net worth”. “Pennies from heaven” such as inheritances, lottery winnings, etc. show up from outside of your operation and could also affect your net worth.

Remember, you are in control of your financial life. Know what is comfortable or dangerous for each measurement. Know where your strengths and weaknesses are. Your understanding of how it all works is tremendously valuable to your success.

**Top 10 Tips to Know if You Get a Letter from the IRS**

By: Don Nitchie

The IRS mails millions of notices and letters to taxpayers each year. There are a variety of reasons why they might send you a notice. Here are the top 10 tips to know in case you get one. Feel free to involve your SWMFBMA field person in reviewing the letter – many people do.

1. Don’t panic. You often can take care of a notice simply by responding to it.

2. An IRS notice typically will be about your federal tax return or tax account. It will be about a specific issue, such as changes to your
account. It may ask you for more information. It could also explain that you owe tax and that you need to pay the amount that is due.

3. Each notice has specific instructions, so read it carefully. It will tell you what you need to do.

4. You may get a notice that states the IRS has made a change or correction to your tax return. If you do, review the information and compare it with your original return.

5. If you agree with the notice, you usually don’t need to reply unless it gives you other instructions or you need to make a payment.

6. If you do not agree with the notice, it’s important for you to respond. Many members involve their SWMFBMA field person in deciding how to respond. You should write a letter to explain why you disagree. Include any information and documents you want the IRS to consider. Mail your reply with the bottom tear-off portion of the notice. Send it to the address shown in the upper left-hand corner of the notice. Allow at least 30 days for a response.

7. You won’t need to call the IRS or visit an IRS office for most notices. If you do have questions, call the phone number in the upper right-hand corner of the notice. Have a copy of your tax return and the notice with you when you call. This will help the IRS answer your questions.

8. Always keep copies of any notices you receive with your other tax records.

9. Be alert for tax scams. The IRS sends letters and notices by mail. The IRS does not contact people by email or social media to ask for personal or financial information.

10. For more on this topic visit IRS.gov. Click on the link ‘Responding to a Notice’ at the bottom left of the home page. Also, see Publication 594, The IRS Collection Process. You can get it on IRS.gov/forms at any time.

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**Minnesota Revised Uniform Limited Liability Company Act**

By: Connie VanderPoel

You may or may not have heard about the changes coming to the LLC laws. On April 8th, 2014, Minnesota Governor Mark Dayton signed into law the Minnesota Revised Uniform Limited Liability Company Act. The new law becomes effective August 1, 2015, for all LLC’s formed on or after that date. LLC’s in existence on July 31, 2015, will remain governed by the present Minnesota LLC Act, Chapter 322B, but may elect after that date to be governed by the New Act. Any Chapter 322B LLC’s that have not elected to be governed by the New Act will automatically become subject to the New Act on January 1, 2018. This will affect how all LLC’s will be organized in the future and makes Minnesota LLC’s shift from a corporation-based model to the partnership-based model used by most other states.

The extent to which documentation for Minnesota LLCs developed under the Existing Statute will need to be revised or re-drafted to operate under the Revised Statute will depend on the facts and circumstances on an entity-by-entity basis. The governing documentation for some LLCs will require little or no modification, while the need for modification will be greater in other situations. You will want to consult with your legal counsel regarding if you need to revise your LLC Operating Agreement after August 1, 2015. A helpful summary of the New Act can be found at [gpmlaw.com](http://www.gpmlaw.com).

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*Source: IRS Tax Tip 2015-65*
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