Module 3: Financial Management

Participant Guide

First Nations
Development Institute

The Business of Indian Agriculture

MODULE 3: Financial Management

Lessons

This module covers the following lessons:

- Spending, Saving and Budgeting.
- Understanding Credit.
- Understanding Insurance.
- Financial and Strategic Planning.

Module 3:
Financial Management

LESSON 1: Spending, Saving and Budgeting

LESSON 1: Spending, Saving and Budgeting

Lesson Topics

This lesson covers the following topics:

- Introduction to Personal and Business Financial Management.
- Developing a Spending Plan.
- Developing a Savings Plan.
- Payments and Invoicing.
- Developing a Budget.

Learning Objectives

Upon completion of this lesson, participants will:

- Understand the differences of personal and business finances, and the considerations of co-mingling personal and business finances, particularly in family-operated businesses.
- Understand and gain practical experience in how to develop a spending plan.
- Understand and gain practical experience in how to develop a savings plan.
- Understand and gain practical experience in payments and invoicing.
- Understand and gain practical experience in how to develop an operating budget.

Definitions

Certificate of Deposit (CD): A financial savings product that pays higher interest rates than traditional savings accounts, and in return, keeps money in the account until it reaches the end of an agreed-upon time period.

Enterprise budget: A budget that covers all the income and costs associated with a part or business unit of the agribusiness.

Individual Development Account (IDA): A matched savings account designed to help families and individuals save for specified long-term goals. A matched savings account means that for every dollar an IDA participant saves, the program will match that amount with additional money paid toward an asset goal.

Liquidity: The ability or degree with which an asset can be converted into cash quickly.

Operating budget: A budget that covers all income and expenses over a period of time, usually for a year.

TOPIC 1: Introduction to Personal and Business Financial Management.

Learning Outcome: Students will understand the differences of personal and business finances, and the considerations of co-mingling personal and business finances, particularly in family-operated businesses.

- For many operators, farming or ranching is more than a job – it is a way of life. So, it can be strange to think about separating the business aspect of farming and ranching with the personal side.
    - Yet, that is exactly what should occur in the realm of financial management: the financial management of your business life should be separate from your personal life.
    - Although there is often a temptation to "borrow" from your business or personal accounts to make ends meet, co-mingling your personal and business finances is almost always a bad idea.
    - There are a number of important reasons personal and business finances should be separated. Here are just a few:
        - Financial obligations in your personal life may negatively affect your business's financial position and likewise, financial obligations in your business may negatively affect your personal finances.
        - Your personal or household assets should be sheltered from the risks associated with your agribusiness.
        - For tax purposes, your personal and business financial account and recordkeeping must be clearly separated. If you have off-farm income, this also needs to be separately managed.
        - Having an accurate picture of your business's performance is difficult if your personal finances are co-mingling with your business accounts.
        - Future financing opportunities (such as loans and ownership shares) may be jeopardized if personal finances are mixed within your business finances.
        - The goals for personal finances and business finances may be different. Personal finances may sustain a family, build security and perhaps save toward some goal. Business finances may seek to make profit, increase market share or develop new product lines.
    - Note that in some cases, personal and business finances legitimately interconnect, as when the owner or family member collects a salary from the business or draws upon owner's equity through profit taking.

- Also, lenders will want to see both personal and business financial holdings and will often include personal finances in their decision to lend to the business.

➢ Because many operators' personal lives are so intertwined with their work, sometimes it may be difficult to determine which financial holdings are personal, family or household, and what are business financial holdings.

  - Generally speaking, personal, family and household financial holdings include income, expenses, liabilities and assets NOT associated with the agribusiness. These financial holdings may include the following:
    - Off-farm family income from jobs not directly related to the agribusiness (for example, a spouse's job working in town or temporary work).
    - Interest and dividend income from personal savings and investment accounts.
    - Pension, disability, unemployment or other disbursements.
    - Payments for home mortgages, car loans, personal credit cards and other short- and long-term liabilities.
    - Payments for recurring expenses such as home utilities, health insurance and contributions to savings and pensions.
    - Payments for irregular expenses, such as home and auto repair, travel or health care.
    - Payments for food, clothing and personal supplies.
    - Assets such as home equity, vehicles, personal property, life insurance payouts, pensions plans, investments and savings.
  - Business-related financial holdings include income, revenues, liabilities and assets such as the following:
    - Business income and revenue from sales and services, and any rents.
    - Interest and dividend from any business savings and investment accounts.
    - Cash reserves, inventories and accounts receivable.
    - Payments for land mortgages and leases, business debt, accounts payable, and other short- and long-term liabilities.
    - Payments for recurring business expenses, such as utilities, insurance, salaries, service or maintenance contracts, and taxes.

- Payments for irregular expenses such as equipment purchases, and maintenance and repair.
- Assets such as owner's equity, land, buildings and structures, and equipment.

➢ Keeping your personal and business finances separate involves several practical steps, including the following:

- Maintain a completely separate set of accounting books and records for personal and business finances. This greatly simplifies tax accounting (and audits) and provides an accurate financial picture of your business.
- Maintain separate bank accounts. This sends a signal that your business is more than just a hobby and that it is a professional endeavor. Many vendors and suppliers will not accept personal checks.
- Maintain separate credit card accounts. Get a business credit card if you don't have one. This will also help your business establish its own credit rating.
- Consider forming a limited liability company (LLC) or an S Corp for the business entity. This protects your personal finances should the company incur financial damages.

➢ Although personal and business finances should be separate, building good habits that deal with one aspect of your financial life will benefit the other financial parts of your life.

- This module's lessons will discuss strategies that will apply to and benefit both your personal and business finances.

Case Study: Sue's Gardening Business Takes Off

Sue had always been an avid gardener and was well-known for growing the best tomatoes in the county. Over the years, her garden grew and grew in size, and as she planted more vegetables (squash, melons, cucumbers, peppers), she harvested more and more produce. She gave much of her produce away until one year a friend suggested that she sell some of her fruits and vegetables at the farmers market in town.

Much to Sue's delight, her experience at the farmers market was both fun and profitable. She enjoyed interacting with customers and other producers, and she started to make a lot of money. What started out as a hobby was turning into a profitable business. After a few seasons, she started to expand her product line to canned vegetables, pickles, and salsas that were sold in local stores off-season and at the farmers market in summer and fall.

At first, Sue just pocketed the money she made at the farmers market. But after a while, it became difficult to keep track of her business income and expenses. Her personal checkbook was filled with check entries for purchases related to her business and deposits from her sales. Likewise, her credit card was used for both personal and business needs, and she was never quite sure that she had enough money in her checking account to pay off the credit card balance each month.

Finally, Sue was thinking about asking the local bank for a loan to buy a small tractor so that she could increase the size of her garden operations. She knew her business was doing well, but she couldn't say how well.

Discussion questions:

What personal and business financial co-mingling issues does Sue have?

What potential financial problems are there for Sue's business?

What do you think Sue should do?

TOPIC 2: Developing a Spending Plan.

Learning Outcome: Students will understand and gain practical experience in how to develop a spending plan.

- One of the leading causes of personal or business bankruptcy is simply spending more than you make. This may seem like stating the obvious, but you will be surprised at how often businesses fail, and personal finances fall apart, because of overspending.

    1. Overspending is common, and is encouraged by easy access to credit cards and a society that promotes consumerism and consumption.

    2. Most of the problems with overspending can be fixed with better tracking of income and expenses.

        - Once income and expenses are known, a spending plan can be developed that makes sure that one spends less than one brings in.

- There are six basic steps to developing a spending plan (you should do this for your personal/household finances, and then separately for your business):

    1. First, income needs to be calculated. This includes salaries and wages and other sources of income over a certain period of time (usually monthly).

        - Find your paystubs, bank deposits, copies of receipts and any other documentation of income.

    2. Second, your daily spending habits need to be tracked. This may take a little work over a few weeks, but you may be surprised in what you learn.

        - Be sure to count your morning coffee, newspaper, lunch and other small purchases that occur daily.

    3. Third, identify expenses that occur regularly (monthly and yearly), such as utility bills, mortgage payments and car insurance.

        - Don't forget gas costs, travel and the holidays. If you give gifts at a certain time each year, count them.

    4. Fourth, assess your total debt (including credit cards) and determine how much you need to pay off each month.

        - Don't count what you are currently paying, but what you need to pay to lower and eventually eliminate your debt. This is especially important with credit card debt, where making the minimum payment means that it will take a very, very long time (and a lot of money) to pay off the entire debt.

5. Fifth, summarize your daily spending, recurring payments and debt payments to record your total monthly expenses.

6. Finally, subtract your total monthly expenses from your total monthly income.

    - If you have money left, congratulations. This is what can be saved and/or used to further reduce your debt.

        - Saving should not be an afterthought, or something to do if you just happen to have money left, Rather it is a critical component of your spending plan. So, make sure that you are saving something each month.

    - If you spending more than you make, as said earlier, you are not alone. Nevertheless, this is time to review and adjust your expenses downward so that you are not over-spending.

        - This is often easier said than done. Many times, families are barely making ends meet and it can be difficult to see how to cut your household budget any further.

        - Many times, reducing your spending comes down to a decision about what you value. Take a moment to list and rank the things that you value in life (family, health, education, community, culture). Your spending should be in alignment with your values and if you discover that you are spending a lot on something that you don't value highly in life, this may be an area to reduce spending.

        - Another approach is to think about what you "need" versus what you "want." Only you can decide if you "need" an item or if you "want" it. If you truly need something, then that is something you should support, but if you only "want" something, then consider if that is something you should spend your money on.

➢ There are many types of tracking systems and tools that can assist you in developing a spending plan.

    - One of the simplest systems is to use a journal or log to record expenditures during the day, or over a month or year. This can be written down or can be entered into a computer spreadsheet.

    - A debt tracker is also easy to create. It can be a journal that lists a debt, its starting balance, interest rate, payment amount and the new balance.

- There are many software programs that help you track spending. Many are free to download, or come with the base software that came with your computer.
- There are also financial education workshops that are often provided by your local college or university, or other community organization such as nonprofits and local banks.

➢ Let's go through an example of developing a spending plan, following the six steps described previously.

1. First, calculate your monthly income. Let's say that you earn $2,200 per month take home pay (after taxes) as a wage earner.

2. Next, let's calculate your daily spending. Let's say that you tracked your daily spending over the past month and that your routine daily spending is as follows:

   - A cup of morning coffee, at $2.
   - Lunch at the local diner, at $7.
   - Afternoon snack, at $2.
   - Evening newspaper, at $1.
   - These daily expenditures total $12 per working day. Multiply the daily amount by five work days, which equals $60 per week. Then multiply the weekly amount by four weeks for your monthly amount, which equals $240.

3. Now we identify the expenses that occur regularly (let's say monthly), such as utility bills, mortgage payments and car insurance. For our simple example, we'll use the following expenses:

   - Rent, at $400 per month.
   - Utilities (power, gas, water and garbage) totaling $300 per month.
   - Car payment, plus insurance, totals $300 per month.
   - Cable, phone and Internet, at $100 per month.
   - Entertainment, which includes movies, dining out and events, at $150 per month.
   - These monthly expenses total $1,250 per month.

4. Fourth, we calculate our debt payments, which include credit card and loan repayments. We'll use the following payments for our example:

- Credit card payment, at $50 per month.
- Student loan repayment, at $100 per month.
- Total monthly debt payments are $150 per month. (Note that we could have listed the car payment as a loan repayment, but chose to combine it with insurance and treat it as a monthly expense.)

5. Now we summarize our daily spending, recurring payments and debt payments to record our total monthly expenses, as shown below.

Monthly Income	
Salaries & Wages	$2,200

Daily Spending	
Coffee	$2
Lunch	$7
Snack	$2
Newspaper	$1
Total daily	**$12**
Total weekly (x5)	**$60**
Total monthly (x4)	**$240**

Monthly Expenses	
Rent	$400
Utilities	$300
Car	$300
Cable, phone, TV	$100
Entertainment	$150
Total	**$1,250**

Monthly Debt Payments	
Credit Card	$50
Student loan	$100
Total	**$150**

6. Finally, we subtract our total monthly expenses (daily spending, monthly expenses, and monthly debt payments) from our total monthly income, as shown below.

Final Monthly Balance	
Monthly Income	2,200
Daily Spending (by month)	-240
Monthly Expenses	-1,250
Monthly Debt Payments	-150
Total balance	**$560**

➢ From the example above, you can see a monthly balance surplus of $560. This means that the person above is making more than they are spending, which is good. However, before we congratulate them, remember what this example does not take into account.

- First and foremost, there is no monthly savings contribution in our example. As we will see in the coming lessons, savings is a critical component to your financial health.
- Second, there are no irregular (or one-time) expenses that often cannot be anticipated, such as household repairs (e.g., leaking roof, appliance breakdown, car maintenance or repair, emergency family needs). These can be planned for by creating a "rainy day" fund or emergency savings.
- Third, the numbers used here were hypothetical and do not reflect the variability and uncertainty of real life. For example, your utility bill may be much higher in the winter and, if so, your $560 surplus may be in fact much less. Likewise, your car insurance could go up due to an accident, or you could take a pay cut during the summers.
- All these factors need to be considered when analyzing your spending plan.

➢ Once you have developed your spending plan, consider the following questions:

- Am I financially secure on a month-to-month basis?
- What costs can I reduce or eliminate, and what income can I increase?
- Am I saving enough for the future?
- Am I saving for emergency needs?
- Am I paying down my debt at an appropriate rate?
- What trends am I seeing from month-to-month? Is my monthly balance steady throughout the year?

TOPIC 3: Developing a Savings Plan.

Learning Outcome: Students will understand and gain practical experience in how to develop a savings plan.

- As mentioned in the previous topic, saving should not be an afterthought, or something to do if you just happen to have money left. Rather, it is a critical component of good financial health, both for your household and for your business.
    - Having inadequate reserves (or savings) is another common factor in business failure and personal bankruptcy.
        - Savings provide a buffer in case of unexpected expenses (for example, accidental damage to equipment or buildings, medical bills), and unanticipated loss of income/revenue (job layoff, loss of a customer, sales or price decline).
    - Savings is also a way to plan for a major purchase without having to use credit or take out a loan. Savings can be used toward a down payment that reduces the amount borrowed, lowers the interest rate, and/or reduces the loan term.
    - Savings improves your credit standing, allowing you to obtain loans more easily, and at more favorable terms.
    - Long-term savings are a way to secure your financial future. Saving for retirement or a college education or a business start-up are important ways to provide security for your family.
    - Financial savings, and the sense of security it provides, is an important factor in a family's (and a business owner's) emotional and even physical health. The stress that financial insecurity brings can often cause conflict and sickness within families and businesses.
- As important as savings are to a business or household, there are many factors in today's society that discourage savings.
    - First, our nation's economy is based in large part on consumer spending, and so businesses devote much of their revenue-making strategies toward advertising and marketing to customers, and providing easy access to products and to credit.
    - For most Americans, real wages that are adjusted for inflation have been flat or falling over the past years, while prices for most items have risen. In order to make ends meet, many households have had to stop saving, tap their savings, and in many cases, borrow themselves into debt.

- In the late 2000s and 2010s after the Great Recession, the nation's fiscal policy has been to encourage spending as a way to stimulate economic growth. One tool to do this is to set interest rates at historically low levels, providing virtually no interest returns on savings. In general, low interest rates encourage spending (and borrowing) and discourage saving.

➢ The first step in developing a savings plan is to identify your savings goals.

- Savings goals are statements about things you wish you could afford. You can accomplish these goals if you manage your finances and set aside savings on a regular basis.
- Savings goals can be short-term and long-term. Short-term savings goals are things that you can save for in a few weeks or months. Long-term savings goals are things that you can save for in a few years or longer.
- Remember, just like your spending preferences, savings goals are often linked with your personal values. The things that you choose to save for should be related to the things that you value in life.
- Likewise, savings goals should first be about the things that you "need," as opposed to the things that you "want." If you have all your needs met, then you can think about your wants. But, for most of us, there are plenty of unmet needs to work toward.
- Let's go through an example of creating some savings goals. For example, let's say that an individual has several short-term goals such as:
  - Buy a new washing machine in three months, which will cost $450.
  - Purchase a birthday gift for a child next month, which will cost $75.
  - Buy a new pair of shoes next month, for $150.
- Let's also say that there are several long-term savings goals, as follows:
  - Buy a used car in a year, which will cost $2,500.
  - Go on a two-week vacation for the whole family in two years, which will cost $5,000.
  - Build an add-on room to the house in five years, which will cost about $15,000.
- Next, list the short- and long-term savings goals as shown below.

Short-Term Goals		Long-Term Goals	
Item	Approximate Cost	Item	Approximate Cost
Washing machine	$450 in 3 months	Used car	$2,500 in 1 year
Birthday gift	$75 in 1 month	Vacation	$5,000 in 2 years
New shoes	$150 in 1 month	Add-on room	$15,000 in 5 years

- Now, calculate each of your savings goals into a dollar amount per month by dividing the approximate cost by the number of months, and then total all your savings goals as a monthly amount, as shown below. For long-term goals, divide years into months first, then divide approximate costs by months.

Short-Term Goals		
Item	Approximate Cost	Savings per Month
Washing machine	$450 in 3 months	$150/month
Birthday gift	$75 in 1 month	$75/month
New shoes	$150 in 1 month	$150/month
Long-Term Goals		
Item	Approximate Cost	Savings per Month
Used car	$2,500 in 1 year	$208/month
Vacation	$5,000 in 2 years	$208/month
Add-on room	$15,000 in 5 years	$250/month
		Total savings per month: $1,041

- As you can see from the table above, listing your savings goals can quickly and clearly show how realistic your goals may be, and what financial planning is needed to achieve those goals.
- A consideration of your savings goals should prompt questions about your "needs" versus "wants." For example, are some of the savings goals really necessary (e.g., new shoes), and/or could some of them be scaled back (e.g., a one-week vacation instead of two weeks)?
- Finally, developing savings goals should ideally be a family and/or business endeavor because there will be different goals and perspectives for different members of the family or business.

➢ The next step in developing a savings plan is to incorporate your savings goals into your spending plan (discussed in the previous lesson topic).

- Add your savings goals (as a per month amount) into your Spending Plan's Monthly Expense Tracker. Recalculate the Spendable Income (top table), and then the Total Spendable Income minus Total Expenses (bottom table).
- If you are unable to save the amount of your goals without going into deficit spending, then you will need to adjust your savings goals expenditures, or spendable income.
    - This is rarely an easy task, and it may take months or even years to achieve the ideal mix of income, expenses and savings for your household or business.
    - Before you get discouraged, think of your savings plans as a roadmap that helps you get to your final financial destination. Just like any journey, it starts with a first step, and it will take time to complete. But you will also find that it can go by quickly and that before you know it, you'll have achieved your savings goals.

➢ There are many products in the financial marketplace to help you save money.

- Perhaps the simplest product is a savings account at your local bank. There are several advantages to using a bank savings account.
    - First, your savings account can be linked to a checking account at the same bank, which makes transferring money between accounts easy.
        - In many cases, you can set up an automatic transfer of funds from your checking account to your savings account each month, thereby ensuring that you save a certain amount each month.
    - Bank savings accounts are very liquid. In other words, you can withdraw savings immediately and easily with few, if any, withdrawal penalties or fees.
    - There may be minimum amounts required for your savings account, so be aware of those limits. Many times, if an account is below a minimum amount, a monthly maintenance fee will be charged.
        - You should always make sure that you are not paying a monthly maintenance fee for the savings account.
        - If your bank does charge a fee and/or has an unreasonable minimum limit, shop around. There are many savings plans in the marketplace that do not charge maintenance fees and have very modest minimum account limits.

- Bank savings (and checking) accounts are very safe. They are insured by the Federal Deposit Insurance Corporation (FDIC), which insures your deposits up to $250,000 per account. Even if the bank fails and cannot pay you back the money you deposited, the FDIC will pay you.
- The major disadvantage of bank savings accounts is that they have offered little or virtually no interest yield in recent years. Thus, your savings are earning almost nothing and, if you consider the effect that inflation has on reducing the value of money, your savings may actually be losing net worth over time.
- Nevertheless, it is still important to have an easily accessible amount of cash that can be used in an emergency or for an urgent need.

- Another popular savings product is a money market account.
  - These are FDIC-insured bank savings accounts that offer a higher rate of interest return on deposits.
  - Money market accounts are also highly liquid, that is, you can withdraw funds at any time.
  - The limitation with money market accounts is that there is usually a higher minimum amount that must be maintained, and there is usually a limitation on how many withdrawals can be made within a given time.
- Another widely used savings product is a certificate of deposit, commonly referred to as a CD.
  - A CD pays more interest, but in return, you must agree to keep your money in the account until it "matures," or reaches the end of an agreed-upon time period.
  - There are many time periods you can choose from, ranging from as short as 30 days, to as long as five years. Typically, the interest rate will rise with an increasing time period.
  - You may be able withdraw your CD account before maturity, but there will probably be an early withdrawal penalty that will typically mean that you forfeit some or all the interest earned so far.
  - Thus, it is important that you carefully consider how long you will be able to keep your money in the CD account without withdrawing it.
  - CDs are also FDIC-insured up to $250,000 per account, so there is no risk.

- Finally, every bank offers different CD rates and rates change every week or so. So, it pays to shop around.
    - You may wish to support your local bank by purchasing their CD product, which is commendable. However, the CD market is national in scope, and many banks are competing for your dollars.
    - It is relatively easy to purchase CD products at any bank that is FDIC insured, no matter where they are located.
    - However, before sharing any sensitive information or depositing any money, be sure to check the legitimacy of any bank you are considering.

- Finally, an Individual Development Account (IDA) is a relatively recent financial product that is available under certain circumstances.
    - An IDA is a matched savings account (usually deposited in a local bank) designed to help families and individuals save for long-term goals that will help them build their financial futures.
    - Some IDA programs may encourage you to save money to buy a new home, start a business or go back to school. Other programs may let you use your savings to repair your existing home, or buy a car to get to work, or invest in some other type of savings goal. Your asset goal is determined by you and your IDA program staff.
    - "Matched savings account" means that for every dollar an IDA participant saves, the program will match that amount with additional money paid toward an asset goal.
        - For example, if the match rate is $1.00 for every $1.00 saved (also known as a "1-to-1" or 1:1 match rate), for every $1.00 you save, the IDA program will match it by providing $1.00 towards your designated asset purchase.
        - For example, if you save $25 per month for one year, that would equal $300 ($25 X 12 months) plus $300 in matched money for a total of $600 at the end of the year.
    - In order to earn the savings match, you usually have to make a deposit every month, take financial education classes, and learn to budget and save.

- Some IDAs require you to put your money in a savings account that is in both your name and the name of the program. That way, you will not be tempted to make a withdrawal because you cannot make a withdrawal without the permission of the program staff. This is called a "custodial" account.
- Other IDA programs require you to open a savings account and practice self-discipline by not taking money out of the account. This is called a "non-custodial" account.
- IDAs are only available in communities where IDA programs exist. IDA programs may be administered by tribal agencies, community development financial institutions (CDFIs), or non-profit organizations.
- Contact your local bank or tribal office to see if an IDA program is available in your community.

➢ The financial products mentioned above are not the only ones that can help you save money. These products were mentioned first because they have no risk.

  - There is another class of savings, commonly referred to as investments, which may yield considerably greater returns, but contain various levels of risk.
  - Investments are beyond the scope of this curriculum, but an excellent resource on investments is available from the First Nations Development Institute, and FINRA Investor Education Foundation, and is called *Building Native Communities: Investing For the Future.*

TOPIC 4: Payments and Invoicing.

Learning Outcome: Students will understand how to make payments, and how to issue invoices for products and services rendered.

- In a certain sense, making payments, issuing invoices and receiving payments represents the lifeblood of a business. Without the cash flow of money going out to pay suppliers and creditors, and money coming in from sales of products or services, a business would soon fail.
    - Typically, these business transactions are accounted for in the Accounts Payable and Accounts Receivable journal entries. There are many computer-based payment and billing systems available to help with these functions.
- As important as these payment and invoice functions are, this is an area where many business operators can fall short, causing cash flow problems that can become quite severe and even fatal to the business.
    - Most of the time, the problems that occur are the result of the timeliness of making payments (paying your bills on time), issuing invoices (billing your customers promptly), and receiving payments (ensuring customer payment has been made and then recording and depositing the payment).
- Making payments, and paying your bills on time, is very important to the financial health of a business for several reasons.
    - First, it helps build and maintain a positive credit history and score, which is vital to a business's ability to access credit.
    - Second, it keeps your suppliers and creditors happy and loyal to your business. Keeping your suppliers satisfied helps protect your supply chain, which is vital for your product cycle. A supplier is much more likely to offer you attractive terms and to make your business a priority if you have a history of paying on time. Likewise, a creditor is much more likely to offer you credit in the future if you have proven to be reliable in making your payments.
    - Making timely payments helps you avoid penalties and interest charges, which can be quite expensive, especially for credit cards.
    - Finally, making timely payments keeps your cash flow and balance accounting numbers accurate and current. You can be confident that you are looking at an accurate picture of your business's financial condition when your payments are up to date.
- In practice, making payments is simple and we have all had experience paying bills. You receive a bill, check the balance in an account, make and record the payment, and then archive the documentation.

- The challenge is often a matter of time and efficiency. When you only a have handful of bills, it's often not a problem to pay them as you go. However, an active business can often have dozens of bills or more coming in each month, which can easily overwhelm a business operator.
- Often times, a company will hire clerical staff to make payments, but if this is not practical, then the business operator must become efficient and accurate in handling payments. Here are several tips to consider.
    - Consider making payments (or "cutting checks") on a regular schedule, such as one day per week. Over the course of each week, set aside your bills in a safe place for processing on your payment day. That way, you will have your full attention to the task, and you will be more efficient by making multiple payments at the same sitting. Related to this, create an office space to pay your bills so that you have all of your materials in a reliable place.
    - Create an organized payment tracking system using an off-the-shelf computer application, or your own spreadsheets. Make sure you link these systems to your banking information so that you can keep your balances accurate.
    - Consider setting up auto-pay for regular expenses and payments that you know occur monthly.
    - Consider pre-paying or bulk paying for some expenses to help reduce the number of bills you receive. You can also look for ways to consolidate some payments.
    - Finally, make sure you keep proof of payment in case you are questioned by the biller and also to be able to write off your business expenses for tax purposes.

➢ Issuing invoices is also not a difficult task in concept. It involves billing a customer for some service rendered or product delivered. Like making payments, the challenge is with the timeliness and efficiency of issuing invoices.

- Typically, customer payments are due upon receipt of a service or product, but these terms can vary. For example, retainers, down payments, upfront parts or material payments may be required in advance before a product or service is delivered. Installment payments can be agreed upon, whereby the customer has a scheduled payment plan after the product or service is delivered.
- In any case, invoices are the official document that trigger customer payments and are usually required by customers to justify payments.

- Like making payments, there are many strong reasons for issuing timely invoices.
    - First, timely invoicing helps to ensure that you are paid on time and that your cash flows remain healthy.
    - Second, it keeps your customers happy and loyal to your business. This may not seem obvious because we often think of getting a bill as a bad thing. But, in fact, responsible customers expect to get a bill on time and want to reconcile their payments and obligations in a timely fashion. Failing to invoice a customer keeps an outstanding obligation on their books and can distort their financial balances.
    - It provides official documentation of attempts to bill a customer, should lack-of-payment issues arise.
- There are several practical tips to make invoicing more efficient and accurate.
    - First, be on time. As with payments, schedule a regular time each week or so when you issue your invoices. Set up a space in your office where all your materials are handy. Use a computerized tracking system, if appropriate.
    - Second, keep good records, sorted by customer. Just like a creditor, you will want to create your own payment history for each customer so that you will know what to expect from them in the future.
    - Third, create a clean, consistent and informative format for your invoice. Don't clutter your invoice with too much information or too many distracting logos or graphics. The invoice is an official business document and should look clean and professional. At a minimum, each invoice should contain the following information:
        - Description of the product delivered or service rendered
        - Order number
        - Item and quantity amounts, and total amounts due
        - Summary of the total payment (bottom line total due)
        - Due date
        - Payment options
        - Details of any discounts
        - Outstanding payment details (if there are past due charges)

- Delivery charges if any
- Late payment charges
- Details of any taxes charged
- Contact number for any queries

- Let's go through an example of creating an invoice. This company sells commercial construction equipment, including air compressors. Below you will see an invoice template (from Microsoft Office) for two air compressors. Note the basic information that is contained and how easily one could modify the template for a variety of purposes.

Date

Invoice No. 1234

To
John Smith Customer
111 Mail Street
Anytown, USA

Ship To
Same as recipient

Instructions
Payment due upon receipt

Quantity	Description	Unit Price	Total
2	NorthStar® heavy-duty 3 HP, 60-gallon electric commercial air compressor	599.99	1,199.98
	Subtotal	599.99	1,199.98
	Sales Tax	41.99	83.98
	Shipping & Handling		
	Total Due	**641.98**	**1,283.96**

Due upon receipt

Thank you for your business!

Company

Tel Telephone
Fax Fax

Street Address
City, ST ZIP

Website
Email

replace with LOGO

- Now, let's try creating an invoice below with the following information:
  - You are billing a customer for three (3) portable generators. The item description is "Generac GP17500E Electric Start Portable Generator Model No. 5735." The unit cost is $2,999.00.
  - There is 7% sales tax.
  - There are no shipping or handling fees.

Quantity	Description	Unit Price	Total
	Subtotal		
	Sales Tax		
	Shipping & Handling		
	Total Due		

- Finally, ensuring that customers have indeed paid their invoices is the final step. The challenge here is with tracking payments, issuing reminders and reissuing invoices (if needed), adding any penalty and interest charges, and proceeding with payment collection if required.
    - Once you have received payment, make sure to record the payment at the same time as it is deposited into your business accounts. Make sure to keep the checks safe and actually deposit them – this sounds obvious, but there are numerous examples of checks getting misplaced and lost. Asking a customer to cancel a lost check and then reissue a new check is costly to them and sends a bad signal.
    - On a regular basis, check on all outstanding invoices and set up a policy on when you will issue reminders, how you will handle late payments, and what you will do when payment becomes uncollectable.
    - Of course, we all want to avoid a situation where bill collection is necessary. There are several ways that you can encourage your customers to pay on time.
        - First, make your payments "payable upon receipt" rather than offering 30-, 45- or even 60-day payment deadlines.
        - Second, set up and send automatic reminders through e-mail or text messages so that your customers don't forget. You can follow up with mailings also.
        - Third, offer a variety of ways to pay. Consider offering payment options through online payment systems (such as PayPal) or with credit cards. However, remember that these options will charge merchant processing fees that will cut into your profits. Requiring advance payments and down payments can also help.
        - Consider offering "early payment" incentives such as discounts for payment at the time of sale.

- Make sure you have all your payment terms in writing, on the invoice and in the sales agreement or receipt.
- Finally, try to maintain a respectful and professional relationship with your customer as you work with them on payments. It is a rare case when customers are intentionally trying to avoid payment – more typically they have forgotten or misplaced your invoice, and have other things on their mind.

TOPIC 5: Developing a Budget.

Learning Outcome: Students will understand how to develop a budget, and will gain practical experience in developing an operating budget.

- A "budget" can mean different things depending on how it is used and whether it is used for household or business purposes.
    - In its simplest form, using a budget is a way to limit your spending, and its most common form is the household monthly budget.
        - In this context, it is similar to the spending and saving plans discussed in the previous lesson topics. You have "x" amount of money to spend each month, and your budget helps you keep within that amount.
    - Let's go through a simple example of a household budget, using the spending and savings plans we developed in the previous topics. If we transfer our spending and savings plan information into a budget spreadsheet, it might look something like this (note we included daily spending into regular costs):

Household Budget (monthly)		
Income:	Target	Actual
Salaries and wages	2,200	
Total Income	**2,200**	
Regular Costs:		
Daily spending	240	
Rent	400	
Utilities	300	
Car payment and insurance	300	
Cable, Internet, phone, TV	100	
Entertainment	150	
Total Regular Costs	**1,490**	
Irregular Costs:		
Total Irregular Costs		
Debt payments:		
Credit card	50	
Student loan	100	
Total Debt Payments	**150**	
Savings goals contributions:		
Emergency "rainy day" fund	25	
Washing machine	150	
Used Car	208	
Total Savings contributions	**383**	
Net Balance: Total of Income – Costs, Debt payments and Savings	**177**	

- Note that this budget has "target" and "actual" columns. This highlights the main purpose of a household budget, which is to hold you on track and accountable to your budget. You set a spending amount as a "target", and then at the end of the month you record your "actual" spending. Hopefully, your actual spending is equal or less than your target, which means you are spending within your budget.

- Also note, as we discussed before, that there are no irregular costs included, which could negatively affect your budget. To help plan for irregular costs, we included a savings payment of $25 each month into a "rainy day" fund.
- You will also notice that a budget only acts as a cash flow sheet, and does not account for assets (such as money in checking and savings accounts) or liabilities (debt and loan amounts that are owed). These financial items should also be tracked on a monthly basis, along with your household budget.

- In a business, a budget can be used as a tool for planning and decision-making.
- There are four basic types of budgets used in business.
  - An Operating Budget covers all income and expenses over a period of time, usually for a year, but it could be monthly.
    - Operating budgets can be applied to both household finances and to business finances.
  - An Enterprise Budget covers all the income and costs associated with a part of the agribusiness. For example, a farm operation may have an enterprise budget for its hay production, and another enterprise budget for a cow/calf operation.
    - Enterprise budgets allow operators to accurately monitor the performance of various units of the business, and to make informed plans and decisions.
  - Partial Budgets cover the income and costs associated with a specific decision.
    - For example, a business owner may be considering the purchase of a new truck and the partial budget would include the income (old truck sale/trade-in, maintenance/repair savings) and costs (new truck payments) of the decision.
  - A Cash Flow Budget monitors the cash that comes into the business and that is used to pay bills.
    - It is an extremely useful tool to ensure that you have enough cash flow to pay your immediate obligation, and/or to plan for when short-term credit may be needed.
- An operating budget for a farm, ranch or agribusiness is an essential management tool. It can tell you if your business is profitable, it can warn you of potential shortfalls, it can help you make important decisions, and it can help you plan for various situations.

- Operating budgets contain three major sections: revenue (usually from sales/services), expenses (fixed and variable costs) and income (other sources of money).
- To develop an operating budget, which is a forecast, you need to first gather records of your past financial performance.
- All the information needed for your operating budget comes from your businesses journals, ledgers and financial statements (see Module 2: Accounting).
- Typically you will need to make some educated predictions of future sales and pricing, as well as the costs of your inputs.
    - Trial budgets are your first attempts at an operating budget and they will include your best estimates of the future.
        - If your trial budget shows a net loss, then adjustments will need to be made to lower costs or raise revenues and income.
        - Because no one can predict the future with certainty, it is recommended to develop a trial budget for the best-case scenario, a budget for a worst-case scenario, and a budget for what is most likely to happen.
    - As the year unfolds, you may find yourself reviewing and updating your various trial budgets, hopefully working with the best-case budget.
- Usually, it is best to start with enterprise budgets for each part of your agribusiness, and then to combine them together for an overall operating budget.

➢ Let's go through an example of creating an operating budget for a small household business. The business caters meals to community organizations and events. The business has forecasted its sales to be 5% higher in the coming year, and its variable costs as 10% higher in the coming year.

- At the end of last year, the revenue to the business from sales was $34,500.
- At the end of last year, other income included $230 in interest earned from savings and investments.
- At the end of last year, fixed costs included:
    - $3,600 in car loan payments
    - $3,900 for utilities
    - $15,000 in hired labor

- $4,500 taxes and insurance

- At the end of last year, variable costs included:
  - $1,100 in repairs and maintenance
  - $3,900 for supply inventories
  - $1,100 in miscellaneous purchases
- Cash at the beginning of last year was $3,250.
- Based on the information above, we would develop an operating budget as shown in the table below.
- Note that although variable costs are rising by 10%, sales represent a much greater number and so a 5% increase in sales more than offsets the rise in costs.
- Also note that cash at the end of the year is rising and that, while the business is only barely profitable, if the trend continues it will be in good financial condition.

Operating Budget

For the Year

Revenue:	Last Year	Coming Year
Sales	34,500	36,225
Total Revenue	34,500	36,225
Income:		
Interest	230	230
Total Income	230	230
Fixed Costs:		
Car loan payment	3,600	3,600
Utilities	3,900	3,900
Hired labor	15,000	15,000
Taxes and Insurance	4,500	4,500
Total Fixed Costs	27,000	27,000

Variable Costs:		
Repairs and maintenance	1,100	1,210
Supply inventory	3,900	4,290
Miscellaneous	1,100	1,210
Total Variable Costs	6,100	6,710
Net Total of Revenue + Income - Costs	1,630	2,745
Cash at beginning of year	3,250	4,880
Cash at end of year	4,880	7,625

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The Business of Indian Agriculture

MODULE 3: Financial Managment

LESSON 1: Spending, Saving, and Budgeting

Spending Plan Worksheet

On the next pages, there are blank templates of a monthly income tracker, a daily expense tracker, monthly expenses tracker, an annual expense tracker, and a debt tracker.

As a group, pretend that you are all members of the same family. Fill out the trackers for your family finances (not your business) using the following information. If information is not provided, you may make up your own answers. Try to base your answers on what you typically spend.

- Your family income is $2,000 per month (after taxes) in salary. There is no other source of income.
- Your monthly rent payment is $400.
- You have a monthly car payment of $220, with a current balance of $4,400.
- You have total credit card debt balance of $1,615.93, with an annual interest rate of 15%. Your monthly minimum payment due is $24.00.

Income Tracker

Identify the money that comes into your household – your income. Afterwards, calculate your total monthly income.

Monthly Income	
Salary	$
Per Capita Earnings	$
Food Stamps	$
Seasonal Earnings	$
Social Security	$
Military	$
Child Support	$
Dividends/Investment Income	$
Other	$
Other	$
TOTAL	$

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Daily Expense Tracker

Track how much you spend on a daily basis. Use this worksheet to keep track of everything you spend each day.

Day	What did you buy?	How much did it cost?
Sunday		$
		$
		$
	Daily Total	
Monday		$
		$
		$
	Daily Total	
Tuesday		$
		$
		$
	Daily Total	
Wednesday		$
		$
		$
	Daily Total	
Thursday		$
		$
		$
	Daily Total	
Friday		$
		$
		$
	Daily Total	
Saturday		$
		$
		$
	Daily Total	

Evaluate your week's spending. Circle items that you could have gone without. Calculate how much money you could have saved by adding all the circled items. What could you have saved? $_____

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Monthly Expense Tracker

Use information from the Daily Expense Tracker to estimate monthly expenses. How much do you spend each month on the following items?

Income		Savings	
Subtotal of Monthly Income *(from Monthly Income Worksheet, page 18)*	$	Monthly Contributions for Savings	$
		Monthly Contributions for Investments	$
		Subtotal Monthly Savings Contributions	$
Spendable Income *(Subtotal of Monthly Income **minus** Subtotal of Monthly Savings Contributions)*	$		

Annual Expenses	Monthly Payments	Miscellaneous Expenses	Monthly Payments
Subtotal of Amount to be Saved Each Month for Annual Expenses *(from Annual Expenses Worksheet, page 20)*	$	Church Tithes & Offerings	$
Debts		Other Charitable Contributions	$
Subtotal of Monthly Debt Repayment *(from Debt Tracker Worksheet, page 21)*	$	Childcare	$
Housing Expenses		School Tuition/Supplies	$
Rent or Mortgage	$	Ceremonies/Powwows	$
Utilities (Elec., Phone/Cell, Cable/Sat., Water/Sewer)	$	Medical Bills and CoPays	$
Insurance (do not enter here if already included in Annual Expenses)	$	Prescription Medicines	$
Repairs (do not enter here if already included in Annual Expenses)	$	Pet Supplies & Vet Exams	$
Taxes (do not enter here if already included in Annual Expenses)	$	Entertainment, Going Out, Video Rentals	$
Subtotal of Housing Expenses	$	Club Dues (Homeowner's Assoc., Fitness, etc.)	$
Car Expenses		Newspaper, Magazine Subscriptions	$
Loan Payment(s)	$	Clothing	$
Gas	$	Haircuts	$
Insurance (do not enter here if already included in Annual Expenses)	$	Gifts	$
Maintenance & Repairs (do not enter here if already included in Annual Expenses)	$	Cash (impulse purchases: coffee, soda, snacks)	$
Subtotal of Car Expenses	$	Finance - Check cashing, bank fees	$
Food Expenses		Tribal Credit Loan Program	$
Groceries		Finance - Check cashing, bank fees	$
Eating out		Other _____	$
Subtotal of Food Expenses		Other _____	$
Monthly Expense Totals		Other _____	$
Subtotal of Monthly Annual Expenses	$	Other _____	$
Subtotal of Monthly Debt Repayment	$	**Subtotal of Miscellaneous Expenses**	$
Subtotal of Housing Expenses	$		
Subtotal of Car Expenses	$	**Monthly Surplus or Shortage**	
Subtotal of Food Expenses	$	**Total Spendable Income *minus* Total Expenses**	$
Subtotal of Miscellaneous Expenses	$	negative number = spending too much, adjust spending positive number = spending in control, good job!	
Total Expenses	$		

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Annual Expense Tracker

In addition to your monthly spending, think about those bills that are due periodically throughout the year. If you don't know how much you spend on these less frequent expenses, then look through your account statements and old receipts, or just call the companies you owe. The following worksheet will help you calculate the amount you need to put aside each month to prepare for these bills.

What costs do you have multiple times a year?

Expense	Cost	Divided by # of months	To be saved each month
Example Expense	*$300/year*	*$300/12 months = $25 per month*	*$25*
1. Car Insurance			
2. Renters Insurance			
3. Ceremony Expenses			
4. Sport Activities			
5. School Supplies			
6. Holidays & Gifts			
7. Vacation & Travel			
8. Taxes			
9. Other:			
10. Other:			
11. Other:			
12. Other:			
Total Annual Expenses		**Total to be Saved Each Month for Annual Expenses**	

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Debt Tracker

Your spending plan needs to include a strategy for paying off debts. Some types of debt (for example, car loans) require a set of monthly payments that needs to be a part of your spending plan. Other types of debt allow you to pay a minimum monthly payment (for example, credit cards). Try to repay more than the minimum payment due each month.

List your debts in the chart below.

Creditor/Debts	Balance	Interest Rate	Other Finance Charges	Minimum Payment	Amount You Can Pay Each Month	New Balance
Example: credit card	*$1,500.00*	*% 26*	*$30.00*	*$39.00*	*$50.00*	*$1,488.00*
1.	$	%	$	$	$	$
2.	$	%	$	$	$	$
3.	$	%	$	$	$	$
4.	$	%	$	$	$	$
5.	$	%	$	$	$	$
6.	$	%	$	$	$	$
7.	$	%	$	$	$	$
8.	$	%	$	$	$	$
9.	$	%	$	$	$	$
10.	$	%	$	$	$	$
11.	$	%	$	$	$	$
Estimated Total Debt Repayment You Can Make Each Month					$	

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The Business of Indian Agriculture

MODULE 3: Accounting

LESSON 1: Spending, Saving and Budgeting

Savings Goals Worksheet

Below, list some things you would like to be able to afford.

Short-term goals: Identify some things you can save enough money for in a few weeks or months.

Long-term goals: Identify some things you can save enough money for in a few years or more.

Short-Term Goals	
Item	Approximate Cost
Ex: Kids' bicyles	*$500 in 6 months*

Long-Term Goals	
Item	Approximate Cost
Ex: Used car	*$1500 in 1 year*

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Calculate each of your savings goals into a dollar amount per month, and then total all your savings goals as a monthly amount. How much per month do you need to save? $_____.

Next, incorporate your monthly savings amount into your spending plan's monthly expense tracker (from the previous lesson topic). How do your savings goals affect your spending plan?

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MODULE 3: Financial Management

LESSON 1: Spending, Saving and Budgeting

Operating Budget Worksheet

On the next page, there is a blank template of a simplified operating budget. Using only the information below, complete the budget for the last year and coming year and be prepared to discuss your results. Forecast your equipment and supply sales to be 5% higher in the coming year, and your variable costs as 10% higher in the coming year.

- The company's name is AAA Farm Equipment and Supplies.
- At the end of last year, the revenue from operations included:
  - $214,500 received from equipment sales
  - $49,500 in supply sales
- At the end of last year, other income from operations included:
  - $2,500 in payments for land you leased
  - $450 in interest earned from savings and investments
- At the end of last year, the fixed costs included:
  - $1,800 in payments for truck loan
  - $2,900 for utilities
  - $5,000 in land mortgage payments
  - $32,000 hired labor
  - $6,500 taxes and insurance
- At the end of last year, the variable costs included:
  - $3,100 in repairs and maintenance
  - $192,900 for equipment and supply inventories
  - $4,100 in miscellaneous purchases
  - Cash at the beginning of last year was ($2,650) – that's a negative amount.

Operating Budget

For the Year

Revenue:	Last Year	Coming Year
Total Revenue		
Income:		
Total Income		
Fixed Costs:		
Total Fixed Costs		
Variable Costs:		
Total Variable Costs		
Net Total of Revenue + Income - Costs		
Cash at beginning of year		
Cash at end of year		

Module 3:
Financial Management

LESSON 2: Understanding Credit

The Business of Indian Agriculture

MODULE 3: Financial Management

LESSON 2: Understanding Credit

Lesson Topics

This lesson covers the following topics:

- Introduction to Credit.
- Short-Term Operating Credit or Loans.
- Intermediate Operating Credit or Loans.
- Long-Term Mortgages and Contracts.

Learning Objectives

Upon completion of this lesson, participants will:

- Understand credit as a business management tool and the decisions and plans needed to make wise use of credit.
- Understand the use of short-term credit for operating expenses compared to using cash reserves.
- Understand intermediate operating loans and various repayment options.
- Understand the advantages and disadvantages of long-term mortgages and contracts, and be able to calculate annual payments and total borrowing costs.

Definitions

Amortizations: the reduction of the value of an asset (for example, a loan) through regular payments over a period of time.

Contract sale: a purchase agreement directly between a seller and a buyer with specified terms and conditions. Ownership in the property transfers upon the complete payment of the full purchase price.

Lien: the right to possess something that is owned by someone else until a debt is repaid.

Mortgage sale: a purchase agreement using a third-party financial institution that lends to the buyer and provides full payment to the seller. The seller transfers ownership to the buyer immediately, while the financial institution holds a lien on the property.

TOPIC 1: Introduction to Credit.

Learning Outcome: Students will understand credit as a business management tool and the decisions and plans needed to make wise use of credit.

- The wise use of credit is an important business management tool that has many advantages for agricultural producers and entrepreneurs.
    - Credit provides capital (cash) at important phases in the development of the agribusiness, such as during start-up, expansion or improvements.
    - Credit provides funds for operating expenses during off-season or low revenue periods, and reduces the need for large reserves to keep an adequate cash flow.
    - Credit allows for the ownership of large capital assets (such as land and buildings) that are often too costly to purchase outright.
    - Credit increases your purchasing power because it spreads out repayments over a longer period of time.
    - Credit provides a source of cash for emergencies and unexpected expenses.
    - The responsible use of credit can build the agribusiness's credit rating, which in turn will make future lines of credit more accessible with more favorable terms.
    - Some businesses that take loans from banks may receive tax benefits, as the profits used to repay the loan principal or interest may be exempted from tax.
- Credit also has several disadvantages that need to be considered carefully.
    - Loan repayments can lower cash flows and create thin operating margins.
    - An unexpected loss of revenue may result in the inability to repay loans, default, or damaged credit ratings.
    - High or variable interest rates may make the repayment of the loan's principal difficult and costly.
    - Collateral (assets used to secure your loan) may be at risk if the business defaults on the loan.
    - A business's debt load may reduce the flexibility to make financial decisions that take advantage of profitable business opportunities.
    - High debt loads may lower your credit ratings and your credit worthiness from a lender's perspective.

- The first step in making the decision to use credit is to clearly identify its purpose and a plan on how it will be used.
    - There are two basic kinds of credit: consumption credit and production credit.
        - Consumption credit is used to purchase consumable products such as food and clothing that are not related to the agribusiness.
            - Consumption credit should not be intermingled with your business finances. In fact, debt from consumption credit can limit the ability of an agribusiness to access production credit.
            - Typically, consumption credit is secured through the use of credit cards, but other types of credit can be used such as payday loans or home equity loans.
        - Production credit is used to increase or improve farm production or income through the purchase of land, equipment, inputs or other uses.
        - Your use of production credit should be directly related to your business plan.
            - For example, if your business plan calls for diversifying your farm operation by adding a specialty vegetable crop for off-season revenue, then your use of credit should directly support that goal.
            - Your business plan will dictate the type of credit needed. There are three major types of credit:
                - Mortgages and long-term contracts used for major purchases, such as land and buildings.
                - Intermediate-term operating credit, with terms usually more than one year but less than 10 years. This type of credit typically finances equipment purchases or building improvements.
                - Short-term operating credit, with terms less than a year, typically is used to maintain adequate cash flows and meet short-term obligations or unexpected expenses.
                    - Often times, a line of credit can be secured in advance for short-term needs, even though it is not used immediately.

- The purpose of production credit should be clear, so that you and your lender understand exactly how the credit will help the agribusiness achieve its goals.
    - For example, let's say that the purpose of a loan is to purchase a greenhouse with heating and irrigation systems to support winter tomato production.
    - Start-up costs to install and operate an 84 x 91 ft. polycarbonate greenhouse with propane heating and drip irrigation systems will require about $80,000.
    - Next, the plan for using the credit should include specific tasks, a timeline and how the loan will be repaid.
    - For example, the purchase and installation of the greenhouse will occur in the spring so that the initial establishment of the tomato crop can occur during the fall with production during the first winter season. By the second winter season, full production will be established.
    - After the operation is fully established by its second season, the estimated yield will be about 50,000 pounds of fresh greenhouse tomatoes per season. At about $1.10 per pound retail, the estimated gross revenue for the season is around $55,000, with about a 17% profit margin.
    - Until profits are realized, loan repayments will be made from profits from other parts of the farm operation.
    - Be sure to factor in the full costs of borrowing, which includes the interest, but may also include servicing fees and insurance. These exact costs will not be known until you select a lender, but you can estimate these costs for planning purposes.
    - Consider that longer-term credit will have higher total borrowing costs than shorter-term credit. The more you borrow, the higher the costs. The higher the interest rate, the higher the cost.

➢ Your financial statements should be used to help make your decision, and to support it with your lenders.

- Reviewing Lesson 2-4: Analyzing Financial Statements provides you with a good foundation on how financial statements can be used in making a credit decision.

- Pay particular attention to the debt and liquidity ratios. High debt-to-equity and debt-to-assets ratios may mean that assuming additional debt is unwise at the time. Low liquidity ratios may call into question the agribusiness's ability to repay the debt.
- Lesson 2-5: Preparing for Credit and Assistance Applications also provides important information on how to prepare for your credit application.
- Review the financial statements, use ratio analysis to support your decision, and then prepare your materials to present to your lender.

➢ Once the decision has been made to use credit, the next step is to prepare yourself for your credit worthiness to be evaluated. There are several criteria that lenders use to evaluate the credit history and financial health of a potential borrower. One of the most common is the "Five Cs of Credit."

- The Five Cs of Credit refers to the major criteria or areas of focus that lenders use to evaluate the credit worthiness of an applicant.
  - The first C stands for Character, and this is often determined by reviewing one's credit history, which highlights your track record in making payments on time, paying off debts, and if your debt load is too high. Credit histories are maintained by three major credit bureaus: Experian, TransUnion and Equifax, and they provide your credit report to lenders.
    - You should check your credit history regularly with <u>each</u> of the three credit bureaus to make sure your information is accurate and current. AnnualCreditReport.com offers one-stop free credit reports that access all three credit bureaus.
  - The second C is for Capacity and refers to the ability of the borrower to repay the debt. Often times, financial ratios are used (such as debt-to-income) to determine this factor. Lenders may also look at the length of time at the current job and job stability.
  - The third C stands for Capital and refers to the ability to provide down payments or the borrower's own assets. When a borrower is willing to include their own assets, this signals that they are serious and confident.
  - The fourth C is for Collateral and is the assets that the borrower is willing to place at risk (and thus share risk) with the lender. This lowers the risk for the lender and assures them that they can repossess or recover their losses if there is a loan default.

- Finally, the fifth C is Conditions and refers to the terms of the loan (amount, interest rates, length, repayment plan), as well as the purpose of the loan and any market trends.

- Some of the Five Cs can be improved upon relatively quickly, but much of the criteria will take long-term planning to manage. For instance, if your credit history has information that lowers your credit worthiness, then it will take time and effort to repair that history.

- If you determine that your credit history needs to be repaired, there are several areas where you can (and should) focus your attention.

    - First, you must understand that your credit history is used to create a single overall credit score called a FICO score, which is the primary way that your credit worthiness is measured. You want a high FICO score – they generally range between 300 and 850. The higher your score, the less risk to the lender.

        - The score is calculated by accounting for your payment history (worth 35% of the FICO score), your debt and amounts owed (30%), how long of a credit history you have (15%), new credit or inquiries (10%), and the mix of accounts and types of credit (10%).

    - To improve your payment history, make sure you are always on time with your payments and that you fully repay all of your debts. Delinquent payments, even if only a few days late, and collections can have a major negative impact on your FICO scores.

        - If you are behind in your payments, work quickly to get current and stay current.

        - If you are having difficulty making your payments, talk to your lender to see if there are ways to adjust your repayment plan.

        - Set up automatic reminders and auto-pay so that you don't forget to make your payments.

        - Finally, if you see errors in your payment history, work with your creditors and the credit bureaus to correct your information.

    - To improve your debt and amounts owed factor, keep your balances low on credit cards and other "revolving credit". High amounts of debt can negatively affect your credit score.

- The most effective way to improve your credit scores in this area is by paying down your revolving (credit cards) debt. In fact, owing the same amount but having fewer open accounts may lower your scores.
- Pay off your debt rather than just moving it around.
- Don't close unused credit cards as a short-term strategy to raise your scores. Also, don't open a number of new credit cards that you don't need just to increase your available credit. This approach could backfire and actually lower your credit scores.

- If you have a short credit history, don't open a lot of new accounts too quickly. New accounts lower your average account age, which will have a more negative effect on your scores if you don't have a lot of other credit information. Also, rapid account buildup can look risky if you are a new credit user.
- To improve your new credit or inquiries, shop for a given loan within a focused period of time. FICO scores can tell the difference between searching for a single loan versus searching for many new credit lines, in part by the length of time over which the inquiries occur.
    - Be careful not to generate a lot of credit inquiries needlessly. For example, don't generate a credit inquiry "just to see" unless you are seriously considering applying for that credit.
    - Note that it's fine to request and check your own credit report. This won't affect a score, as long as you order your credit report directly from the credit reporting agency or through an organization authorized to provide credit reports to consumers.
- Finally, to improve the mix of accounts and types of credit, apply for and open new credit accounts only as needed. Don't open accounts just to have a better credit mix – it probably won't raise your credit score.
    - Manage credit cards responsibly. In general, having credit cards and installment loans (and paying timely payments) will rebuild your credit scores. Someone with no credit cards, for example, tends to be higher risk than someone who has managed credit cards responsibly.
    - Closing an account doesn't make it go away. A closed account will still show up on your credit report, and may be considered by a score.

- Once you have a plan to use credit and to strengthen your credit worthiness, the next step is to identify a lender.
    - Many financial institutions will provide credit for your needs, but it is generally a good idea to work with a lender who is familiar with agribusiness clients.
    - Lenders who are unfamiliar with agribusinesses may not even consider lending for operating expenses, which is typically not supported in many business sectors.
    - Lenders who work with the agricultural sector will be familiar with the unique characteristics of farm and ranching operations, including the industry-accepted financial measures that indicate credit worthiness.
    - They will also understand the seasonal nature of agribusinesses and cash flows, as well as the capital-intensive nature of farming and ranching operations.
    - Agricultural banks, local banks, and Farm Credit Services institutions are good places to start your search for a lender. USDA's Farm Service Agency (FSA) may provide loans when traditional lenders decline to provide a business credit.
- Once you've identified a lender, it will help you understand your lender's position if you understand his/her risk.
    - In general, short-term operating loans represent greater risk than longer-term loans. That is because there is often no recoverable asset involved in a short-term operation loan.
        - For example, a loan to purchase seed or fertilizer leaves no asset to recover if the loan cannot be repaid. The lender may place a lien on the crop, but if the crop fails then there is nothing to recover.
    - Long- and intermediate-term loans involve less risk because they often involve assets (land, buildings, equipment,) which can be repossessed to cover a lender's loss.
        - Intermediate-term loans that involve equipment and vehicles are more risky because of depreciation and the potential wear and tear of the assets.
    - Understanding your lender's risk will help you appreciate the information that he/she requires from you, and the areas where both you and the lender need to work together toward a common outcome.
- Carefully study the loan product being offered by looking at the total costs of borrowing the terms and conditions, and by comparing it with competitive products on the market.

- Your lender should provide you with the total cost of borrowing, including service fees, insurance, and the interest rate and how it will be applied.
- Typically for short-term loans with a single payment at the end of the term, interest will be simply calculated by the amount borrowed and is due at the end of the term.
- For long-term loans (such as land mortgages), interest is usually calculated from the unpaid balance. The payment amount remains the same, but less interest and more principal is paid with each successive payment.
- There are other ways that interest can be calculated and repayments scheduled. The best choice for you will depend on your specific needs and your ability to repay the loan over time.
- Most lenders will use amortization tables to quickly determine a repayment schedule. There are also many loan calculators on the web that can assist you in evaluating various interest rates and repayment schedules.

➢ Once a lender and the loan product have been chosen, the lender will assist you in preparing your application.

- It will be helpful to review Lesson 2-5: Preparing for Credit and Assistance Applications, and have all the necessary supporting documentation ready for your lender.
- Be honest about your agribusiness's financial situation. Don't try to hide any unfavorable information.
- Keep in close communication with your loan officer. If something changes in your business, be sure to tell your lender. Touch base with your loan officer regularly to check on the status of your application.
- Prepare yourself for the possibility that your loan application may be denied. If you are denied, don't take it personally. Denial may not reflect your financial standing as much as it reflects the lender's finances.
- Ask your lender why your application was denied and what you could do to improve your chances next time. This is an important learning moment.
- Have a back-up plan ready if you are denied. There are many lending institutions on the market, and if your financial situation is solid, you will be able to find another lender.
    - USDA's Farm Service Agency is now an option if you have been denied by a traditional lender.

➢ A related topic to understanding credit is loan consolidation, where several outstanding loans are repackaged into a single loan.

- Loan consolidation is usually undertaken when the agribusiness wants to lower its monthly payments, extend the length of the repayment term, or take advantage of lower interest rates.
- Loan consolidation will typically raise the total borrowing costs, but in the case of lower interest rates, it may lower total borrowing costs. Don't forget that there may be refinancing and servicing fees to consider in the costs.
- As with any credit decision, loan consolidation should be directly related to the business's plans and goals.
- In many ways, loan consolidation has the same advantages and disadvantages as the basic use of credit decision.
- Be careful that the short-term benefits of loan consolidation (such as improved cash flow with lower repayments) are not outweighed by longer-term problems (higher costs of borrowing that reduce profits).

➢ One final topic related to credit is the decision to extend credit to an agribusiness's customers.

- The exact nature of the agribusiness will largely dictate whether credit should be a part of the services extended to customers.
- In some types of agricultural businesses, a short-term line of credit is a natural part of the business transaction.
- For example, farm inputs required to produce a crop are often paid when the crop is sold.
- In other cases, credit may be requested under unusual circumstances. For these cases, it is helpful to develop a standing business policy before the situation arises so that the decision is based on careful thought and planning.
- Exceptions to the policy can be made depending on the circumstances, but a standing credit policy provides the basis for the decision.
- In many ways, the decision for an agribusiness to extend credit to its customers is similar to traditional lenders: assessing the risk and reward.
    - The rewards may include continued customer business and loyalty, and increased sales and revenues.
    - The risks include paying for inventories or services with your own money until the customer pays, the additional accounting necessary to track the credit, and ultimately, the potential risk of non-payment.
    - Because most agribusinesses that choose to extend credit will offer unsecured short-term credit, there are few assets to recover if non-payment were to occur.

TOPIC 2: Short-Term Operating Credit or Loans.

Learning Outcome: Students will understand the use of short-term credit for operating expenses compared to using cash reserves.

- As mentioned in the previous topic, short-term operating credit are typically loans with terms less than a year, and are often used to maintain adequate cash flows and meet short-term obligations or unexpected expenses.
    - Short-term operating loans typically follow the agricultural production cycle, which is usually yearly, but can be longer or shorter.
        - They are often used to purchase farm inputs such as seed, fertilizer, fuel and chemicals, and are repaid when payment for the crop is received.
        - Short-term loans may also allow the business to take advantage of cash discounts, prepay for inputs while prices are low and gain some tax advantages.
        - A lender may secure the short-term loan with a crop lien or other business asset.
        - The risk involved in using annual operating loans includes the potential for crop failure or price drops that would lead to a loan default. Crop insurance should be considered to manage this risk.
    - A line of credit that can be secured in advance (and not used immediately) is also considered short-term operating credit.
        - A line of credit can be revolving (like a credit card), which means that money can be loaned and repaid over and over, within the limits of the credit agreement.
        - A non-revolving line of credit allows the agribusiness to draw upon the credit and repay it only once.
        - The advantage of a line of credit is that it doesn't cost anything until it is used, and interest is charged only on the amount borrowed for a specific amount of time.
- The terms and conditions for short-term credit will depend on the specific lender and the loan product.
    - One type of payment arrangement may be interest-only payments made monthly, quarterly or semi-annually with the full principal payment due at the end of the term.

- Another type is regular payments (of both principal and interest) of a fixed amount throughout the term of loan.
- Interest rates may be fixed for the full term of the loan, or have a variable rate that resets at given intervals (for example, every three months).
- Simple interest is often used for single payment loans. Interest is calculated on the loan amount for the given period of time and is due at the end of the term.
    - For example, a person who borrows $10,000 at a 6% simple interest rate would pay $600 in interest at the end of the term (plus the principal amount).
    - The effective interest rate in this example is also 6%, because $600 interest costs divided by the $10,000 loan amount is equal to 6%.
- Discount interest is subtracted from the loan amount up front. It results in a higher effective interest rate than simple interest. It is usually used only for very short-term loans (for example, 30, 60 or 180 days).
    - For example, a person who borrows $10,000 at a 6% discount interest rate would have $600 deducted from the loan amount, leaving $9,400 to borrow.
    - The effective interest rate in this example is 6.4%, because $600 interest cost is divided by the $9,400 loan amount.
- Compound interest is calculated on the principal and the accumulated interest at certain intervals. Usually this type of interest is not used for short-term agricultural operating credit.
- Don't forget to account for any fees and service charges for the credit, in addition to the interest.
- As with any loan repayments, a major consideration is how the repayment schedule will affect the business's cash flow and liquidity.

➢ There are several alternatives to using short-term credit for operating expenses.

- Cash reserves, if adequate, can be used for short-term obligations, emergencies and unexpected costs, and to maintain adequate cash flows.
    - The benefits to using cash reserves for short-term operating expenses may include lower borrowing costs and interest payments for other credit, lower debt ratios, lower risk of default, easier and more favorable access to credit, and greater financial flexibility for other profitable opportunities.

        - The downside to using cash reserves may include the reduction of cash available for other uses such as emergencies or maintaining adequate cash flows. It may also lower asset ratios and reduce the business assets needed to stay credit worthy, making some credit more difficult to access.
        - If they are used, cash reserves should be restored as soon as possible.
        - Remember that there is an opportunity cost to using cash reserves or savings to fund your short-term business needs. That means the cash being used can't be used for some other opportunity.
    - Borrowing from owner's equity (lending from yourself, from personal assets or profits to the business) may be an option, as long as the transaction and terms of repayment are clearly defined.
        - One concern with this option is that it could lead to a pattern of co-mingling of personal and business finances.
    - Borrowing from family members or friends is also an option, but one that should be carefully considered.
        - You should treat any loan from family or friends with the same standards as you would for a business transaction. Terms and repayment plans should be clearly defined and agreed upon.

- One type of short-term credit that bears special consideration is a paycheck advance (also known as payday loans), which provides short-term loans secured against the customer's next wages or a delayed deposit of a customer's check.
    - Paycheck advance lenders charge a fee for a loan over a short period of time and while they may appear to be cheap, in fact, the annual percentage rate of these loans range from hundreds to over a thousand percent.
    - These loans are very expensive, but because they are easily accessible and renewable, they encourage a cycle of indebtedness that often worsens the financial standing of the customer.
    - These types of loans are sometimes called "predatory" because they target customers who may be uninformed about the true borrowing costs and are in desperate financial circumstances.
        - They also target customers during tax refund season, potentially sapping assets from individuals and communities.
        - Sometimes these tax refund loans are packaged with unaffordable big ticket purchases such as cars and furniture. This practice encourages people to buy things beyond their means.
    - These types of loans are highly discouraged and should only be considered carefully under the most compelling reasons.

Case Study: Comparing Short-Term Operating Credit for Joe and Frank

Joe and Frank are both corn famers on neighboring land in Clinton County. Joe and Frank have both estimated that they will need $10,000 for the purchase of seed, fertilizer and fuel for the coming season's crop.

Joe chooses not to use his cash reserves for these purchases and so contacts a lender who will loan him $10,000 at 5% simple interest for six months, with no service charges or fees. His interest and principal will be due at the end of the term.

Frank has $5,000 cash reserves that he will use. It is in a money market account that earns 1% simple interest per year. So, Frank contacts a lender who will loan him $5,000 at 5% simple interest for six months, with no service charges or fees. Interest and principal are due at the end of the term.

Discussion questions:

What is the total cost of borrowing and interest for Joe and for Frank?

What are the benefits and costs to using cash reserves for short-term operating expenses?

Who made the better credit decision, Joe or Frank?

TOPIC 3: Intermediate Operating Credit or Loans.

Learning Outcome: Students will understand intermediate operating loans and various repayment options.

- As mentioned in the first topic of this lesson, intermediate-term operating credit has terms usually more than one year but less than 10 years, and typically finances equipment purchases, breeding livestock, building improvements or other operating capital needs.
    - Intermediate-term loans will have more options for terms and repayment than short-term operating loans, and so will require more analysis and decisions.
    - Loans of intermediate terms will also require forecasting into the future on expected revenues, expenses and cash flows, as well as the condition, maintenance and repair of equipment, buildings and other business assets.
    - Because intermediate-term loans typically involve large dollar amounts, lenders may be hesitant to lend the entire amount needed for the full potential of the business opportunity to be realized.
        - A common pitfall is when a business owner accepts less credit than what is truly needed, and then risks the failure of the entire business opportunity.
        - Lenders may also try to shorten the term of the loan which, if accepted, will mean higher payments and potential problems with cash flows.
    - Borrowers should also be aware of any "demand clauses" in the loan's terms, which allow the lender to demand full repayment of the loan at any time for any reason.
    - As with all credit decisions, intermediate-term credit must directly support the business plan.
- There are several common types of intermediate-term repayment plans that may meet the needs of the agribusiness. Many times, the choice has more to do with

the ability of the business to maintain adequate cash flows and liquidity than with the total costs of borrowing.

- Fixed, equal payments are when interest and principal amortizations (meaning paying down over a period of time) occur at set times (monthly, quarterly, yearly), and where interest charges represent the bulk of early payments. The principal portion of the payment increases and the interest portion decreases over time, so that the bulk of the payment is for the principal near the end of the loan term.
    - The USDA Farm Service Agency and many farm credit service institutions use this type of repayment plan. This is the repayment method for many home mortgages.
    - The advantage of this type of repayment is that it is easier to plan and budget for fixed equal payments over the life of the loan. There may also be tax advantages associated with higher interest payments early in the loan term.
    - The disadvantage of this type of repayment is that there are higher total borrowing costs (more interest charges) than other methods, and the principal amount declines very slowly in the early term of the loan.
- Fixed principal payments are when the principal amortization is set to fixed, equal amounts over the life of the loan term, and interest is calculated on the declining principal amounts.
    - The advantage of this type of repayment is that there are lower total borrowing costs (less interest charges) than the fixed equal method because the principal amount declines faster and so less interest charges are generated.
    - The disadvantage of this type of repayment is that there are higher payments in the early part of the loan term, which may lead to cash flow problems.
- A third type of repayment plan is the balloon payment, which is a relatively short-term loan (for example, three years) but which calculates interest and principal payments based on a longer term (such as 10 years).
    - The understanding with a balloon payment is at the end of the shorter term, the full principal will become due, and the borrower will pay the principal in full, renew or refinance the loan.
    - The advantage of this type of loan is that it results in lower payments during the relatively short period of the loan term. Lower payments result in less stress on cash flows and liquidity.

- The obvious disadvantage is making the large bulk payment due at the end of the short term if the loan cannot be renewed or refinanced.
- Usually the lender will work with the borrower to renew or refinance the loan, but this is not certain, especially in cases where the borrower's credit worthiness has been downgraded.

➢ Leasing may be an attractive alternative to taking out a loan to purchase equipment.

- Leasing has several advantages over taking out a loan.
  - It allows you to use equipment if you cannot secure credit to purchase it.
  - Lease payments may be lower than loan repayments, which may help the cash flow situation.
  - Leasing does not negatively impact the debt ratios of the business, so flexibility to take advantage of profitable opportunities is not reduced.
  - Leasing shifts the depreciating ownership value of equipment to the lesser, and lease payments are typically a tax-deductible expense.
  - In many cases, an option to purchase the equipment at the end of the lease is available. However, this is almost always more expensive than purchasing the equipment from the start.
- Ownership has several advantages over leasing.
  - You have full right to the equipment and can sell it if your business needs change, and so retire the debt.
  - You can customize or modify your equipment to meet any unique needs of your operations.
  - You can account for depreciation as a business expense, and you may be able to claim the interest portion of your loan repayment as a tax deduction.
- The major considerations in deciding whether to lease or purchase equipment is cash flow (as discussed with other types of credit) and tax implications, which may be considerable.
  - The tax considerations for purchasing equipment include the depreciation on the equipment and the interest payments for the loan.

- The tax considerations for leasing are the tax deductions for the lease payments.
- Tax benefits vary by state and types of businesses. Your tax professional is the best source of advice on the tax advantages of ownership and leasing.

Case Study: Comparing Intermediate-Term Operating Credit for Joe and Frank

Joe and Frank are both corn famers on neighboring land in Clinton County. Joe and Frank have both estimated that they will need $100,000 for the purchase of a new field tractor.

Joe meets with his local agricultural lender and agrees to a five-year loan at 10% interest, with *fixed, equal payments,* one payment per year.

Frank also meets with an agricultural lender and agrees to a five-year loan at 10% interest, with *fixed principal payments,* one payment per year.

Review the table below which summarizes the payments and costs associated with Joe and Frank's loan agreements, and then discuss the questions following the table.

	(Joe) Fixed Equal Payment Method					(Frank) Fixed Principal Method				
Year	Beginning Balance	Principal Payment	Interest Payment	Total Payment	Ending Balance	Beginning Balance	Principal Payment	Interest Payment	Total Payment	Ending Balance
1	100,000	16,380	10,000	26,380	83,620	100,000	20,000	10,000	30,000	80,000
2	83,620	18,018	8,362	26,380	65,602	80,000	20,000	8,000	28,000	60,000
3	65,602	19,820	6,560	26,380	45,782	60,000	20,000	6,000	26,000	40,000
4	45,782	21,802	4,578	26,380	23,980	40,000	20,000	4,000	24,000	20,000
5	23,980	23,980	2,398	26,378	0	20,000	20,000	2,000	22,000	0
Total		100,000	31,898	131,898			100,000	30,000	130,000	

Table adapted from Ellinger, Paul N. and Peter J. Barry. nd. A Farmer's Guide to Agricultural Credit. The Center for Farm and Rural Business Finance, University of Illinois at Urbana-Champaign.

Discussion questions:

What is the total cost of borrowing and interest for Joe and Frank?

What are the benefits and challenges to cash flow with the two payment methods?

Assume that corn prices were high and yields were good in Years 1 and 2. Who made the better credit decision, Joe or Frank?

Assume that corn prices were low and yields were poor in Years 1 and 2. Who made the better credit decision, Joe or Frank?

TOPIC 4: Long-Term Mortgages and Contracts.

Learning Outcome: Students will understand the advantages and disadvantages of long-term mortgages and contracts, and be able to calculate annual payments and total borrowing costs.

- Long-term mortgages and contracts are typically used to purchase land and/or construct buildings, with terms longer than 10 years.
    - Mortgages are loans that are secured by real estate through a mortgage lender or bank, while contracts are lending agreements directly between a buyer and a seller. There are advantages and disadvantages to each type of agreement.
- Mortgages are where a lender provides most of the funds to purchase property. The seller is paid in full at the time of purchase, and the buyer agrees to make payments to the mortgage lender until the debt is retired. The mortgage lender maintains a lien on the property to secure the loan.
    - Mortgages are the most popular method to securing land, and they have several advantages.
        - First, the major advantage is that the buyer owns the land at the time of purchase. He or she is then free to sell any part of the land. They can also make additional investments to the property.
            - The buyer can also build up equity as payments are made, and can refinance the loan if it makes sense to do so.
        - Second, the seller is paid in full at the time of purchase and relinquishes ownership rights and responsibilities.
            - Thus, there is no longer any need for the buyer and seller to maintain any business relationship between themselves.
        - Third, mortgage loans are an effective way to build a solid credit rating (assuming that payments are prompt). When working with a full-service lender, a mortgage may make access to short- and intermediate-term credit easier with more favorable terms.
        - Fourth, mortgages are widely available from a variety of lenders at competitive terms.
    - The major disadvantages of mortgages (as compared with contracts) are that they typically require a larger down payment, and involve higher interest rates and closing costs and servicing fees.

- Some mortgages may be available at lower interest rates if they are provided by lenders who use Farmer Mac (Federal Agricultural Credit Corporation) and other government-sponsored enterprises that buy mortgages on the secondary market.
    - Farmer Mac ensures that more money is available in the agricultural mortgage market at reasonable rates and lower risk.
    - Loans that are eligible for Farmer Mac support include first-lien mortgages that are secured by agricultural land or rural housing. Your local lender can provide more information on specific qualification criteria.

- Contracts (sometimes called "contract for deed") are typically made directly between a buyer and a seller, where the buyer agrees to make payments to the seller until the full amount of the debt (both principal and interest) is paid, whereupon the ownership title is transferred.
    - A contract is especially attractive for a beginning or limited resource farmer who is looking to establish or expand their operation. A contract has several advantages for the buyer.
        - First, depending on the seller's needs, contacts can involve smaller down payments and/or better interest rates than a traditional lender.
        - A seller may be more flexible regarding the credit worthiness of the buyer and with repayment options.
        - Contracts typically avoid closing costs and service fees charged by many traditional lenders, which can add up to significant amounts.
    - There are also several advantages to the seller.
        - A seller may be able to sell the land more quickly through a contract instead of a traditional mortgage process because it increases the number of potential buyers.
        - A contract generates immediate and regular cash income to the seller through the payment plan.
        - A seller may be able to defer any capital gains taxes associated with the sale of land until the purchase is completed and title transferred.
    - There are also a number of disadvantages to contracts, especially to the seller who assumes greater risk.
        - A seller is typically less sophisticated than financial institutions in assessing the credit history of buyers, and so may not fully understand the ability of the buyer to repay the debt.

- Should the buyer default on the contract, taking possession of the land can be costly in terms of time and money.
    - If the buyer refuses to leave the property, evictions can require lengthy and costly court proceedings.
    - If the seller still owes a mortgage on the land, then he or she will need to continue to make payments, even without payments from the buyer.

- There are disadvantages to the buyer as well.
    - The major disadvantage of contracts for buyers is that they have no ownership rights until the contract is fulfilled.
        - This means that the buyer cannot make any investments in the land, sell any part of it, or use its equity without the permission of the seller.
        - Further, if the seller's situation suddenly changes negatively (due to death, court judgments or bankruptcy, etc.), the buyer may be at risk of losing the land and any payments that have been made.
        - Some contracts have strict default clauses that allow the seller to take full possession of the land if a payment is missed. This may include forfeiting all payments made to that point.

- The bottom line is that contracts can provide more flexibility and efficiency, and lower costs than mortgages, but carry higher risk for both seller and buyer.
    - Sellers need to carefully assess the buyer's ability to fulfill the contract, and buyers need to carefully assess the seller's character and the status of the property.

➢ Payment options and terms for long-term mortgages and contracts are similar to those discussed with intermediate-term credit, except that terms will usually be longer than 10 years.

- Additionally, long-term credit can have interest rates that remain fixed through the life of the loan, or are adjusted at given points.
    - Fixed interest rates provide a guaranteed rate and predictability, but are set higher than variable rate loans. Should interest rates fall, the loan may be refinanced, but additional service fees and costs need to be considered in the total costs of refinancing.

- Variable rate loans typically have lower interest rates, but carry the risk of higher rates and costs if the adjustments occur as interest rates rise.
    - Some variable rate loans will specify a "cap" or maximum amount that rates can be raised during an adjustment.
    - You may be able to convert to a fixed rate loan product if rates rise to unacceptable levels.
        - However, the risk is that you may not be able to qualify for another loan product if your credit standing has been downgraded or if the financial marketplace is stressed. In that case, you may be stuck with your current adjustable rate loan.

- Generally speaking, lenders are more willing to offer more loan products with flexible rates and terms when they know that their credit is secured with land or real estate.
- It pays to shop around, and think carefully about how the agribusiness will manage its long-term debt obligations. As before, the use of long-term credit should be linked directly to the business plan.

Amoritization Table. Annual Principal and Interest Paid on every $1 borrowed, by Length of Loan and Interest Rate.

	Annual Interest Rate													
Yrs.	3%	4%	5%	6%	7%	8%	9%	10%	11%	12%	13%	14%	15%	Yrs.
3	.35353	.36035	.36721	.37411	.38105	.38803	.39505	.40211	.40921	.41635	.42352	.43073	.43798	3
4	.26903	.27549	.28201	.28859	.29523	.30192	.30867	.31547	.32233	.32923	.33619	.34320	.35027	4
5	.21835	.22463	.23097	.23740	.24389	.25046	.25709	.26380	.27057	.27741	.28431	.29128	.29832	5
6	.18460	.19076	.19702	.20336	.20980	.21632	.22292	.22961	.23638	.24323	.25015	.25716	.26424	6
7	.16051	.16661	.17282	.17914	.18555	.19207	.19869	.20541	.21222	.21912	.22611	.23319	.24036	7
8	.14246	.14853	.15472	.16104	.16747	.17401	.18067	.18744	.19432	.20130	.20839	.21557	.22285	8
9	.12843	.13449	.14069	.14702	.15349	.16008	.16680	.17364	.18060	.18768	.19487	.20217	.20957	9
10	.11723	.12329	.12950	.13587	.14238	.14903	.15582	.16275	.16980	.17698	.18429	.19171	.19925	10
11	.10808	.11415	.12039	.12679	.13336	.14008	.14695	.15396	.16112	.16842	.17584	.18339	.19107	11
12	.10046	.10655	.11283	.11928	.12590	.13270	.13965	.14676	.15403	.16144	.16899	.17667	.18448	12
13	.09403	.10014	.10646	.11296	.11965	.12652	.13357	.14078	.14815	.15568	.16335	.17116	.17911	13
14	.08853	.09467	.10102	.10758	.11434	.12130	.12843	.13575	.14323	.15087	.15867	.16661	.17469	14
15	.08377	.08994	.09634	.10296	.10979	.11683	.12406	.13147	.13907	.14682	.15474	.16281	.17102	15
20	.06722	.07358	.08024	.08718	.09439	.10185	.10955	.11746	.12558	.13388	.14235	.15099	.15976	20
25	.05743	.06401	.07095	.07823	.08581	.09368	.10181	.11017	.11874	.12750	.13643	.14550	.15470	25
30	.05102	.05783	.06505	.07265	.08059	.08883	.09734	.10608	.11502	.12414	.13341	.14280	.15230	30
35	.04564	.05358	.06107	.06897	.07723	.08580	.09464	.10369	.11293	.12232	.13183	.14144	.15113	35
40	.04326	.05052	.05828	.06646	.07501	.08386	.09296	.10226	.11172	.12130	.13099	.14075	.15056	40

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The Business of Indian Agriculture

MODULE 3: Financial Management

LESSON 2: Understanding Credit

Word Game Worksheet

Fill in the blank spaces with words having the exact number of letters, and then find the words in the word puzzle on the next page.

Mortgages and long-term contracts are used for major purchases, such as _ _ _ _ and buildings.

Intermediate-term operating credit, with terms usually more than one year but less than 10 years, typically finances _ _ _ _ _ _ _ _ _ purchases or building improvements.

Short-term operating credit, with terms less than a _ _ _ _, typically is used to maintain adequate _ _ _ _ _ _ _ _ _ , short-term obligations, or unexpected expenses.

The full costs of borrowing include the interest, but may also include _ _ _ _ _ _ _ _ fees and _ _ _ _ _ _ _ _ _.

When analyzing financial _ _ _ _ _ _ _ _ _ _, pay particular attention to the debt and liquidity _ _ _ _ _.

USDA's _ _ _ _ Service Agency (FSA) may provide loans when traditional lenders decline to provide a business credit.

Loan consolidation, where several loans are repackaged into a single loan, may raise the total borrowing _ _ _ _ _.

The decision for an agribusiness to extend credit to its customers is similar to traditional lenders: assessing the _ _ _ _ and reward.

The plan for using the credit should include specific tasks, a _ _ _ _ _ _ _ _, and how the loan will be _ _ _ _ _ _.

Your use of credit should be directly related to your _ _ _ _ _ _ _ _ plan.

L S T A T E M E N T S

A S K O M R E P A I D

N X E Q U I P M E N T

D S F V S S W A X Z I

S E Y W O K C K L A N

S R C A S H F L O W S

E V S K O U A W I P U

N I Q B I E R V Y U R

I C O S T S M X E W A

S I U E A P O S A Q N

U N Z R R C X U R E C

B G T I M E L I N E E

Module 3:
Financial Management

LESSON 3: Understanding Insurance

The Business of Indian Agriculture

MODULE 3: Financial Management

LESSON 3: Understanding Insurance

Lesson Topics

This lesson covers the following topics:

- Introduction to Insurance.
- Making Decisions about Insurance.
- Life Insurance and Estate Planning.

Learning Objectives

Upon completion of this lesson, participants will:

- Understand insurance as a business tool used to manage risk.
- Understand the considerations in deciding to use insurance and what type of insurance to use.
- Understand the use of life insurance in estate planning.

Definitions

Market value: The value that is usually reflected by the initial purchase price of an asset and then is adjusted over time by factors such as depreciation, inflation or market forces.

Replacement value: The value that is the cost that it would take to replace the lost asset today.

Term life insurance: The simplest and least expensive type. It is an agreement that the insurance company will pay a certain amount to your beneficiary upon death, and in return a premium will be paid for a set time, or term.

Universal life insurance: A policy that combines the characteristics of whole life insurance, with an associated investment sub-account that is managed separately.

Whole life insurance: A policy that collects larger premiums in younger years to offset higher premiums in older years. A cash reserve is built with excess of premiums paid in early years and is used to support costs later.

TOPIC 1: Introduction to Insurance.

Learning Outcome: Students will understand insurance as a business tool used to manage risk.

- Insurance is an important business tool used to manage risk.
    - Insurance policies can provide protection against losses related to the business, household and individual.
    - Insurance works best when the chances of loss or damage are low, but the costs of such hazards are very high.
    - Insurance works by pooling the premiums paid by a large group of policy holders so that payments can be paid to a small group of claimants.
        - The chance of a loss, or risk, is calculated carefully for each type of loss that can occur. Premiums, in large part, are based on the calculated risk and the size of the pool of policy holders.
    - At a minimum, every household should have insurance that protects them from the death/disability of the main wage earner, loss/damage of the home, health costs, and loss/liability of vehicles.
- There are several major categories of insurance that are especially relevant to an agribusiness.
    - Property insurance protects the agribusiness owner from loss/damage to buildings, equipment, crops or animals from a destructive event such as fire, hail storm or flood.
        - Most property insurance policies are a combination of fire insurance and liability insurance (liability insurance will be discussed separately in a moment).
        - A typical fire insurance policy will protect property from fire and lightening, and the removal of items from a burning structure.
            - Additional (or extended) protections beyond the basic fire policy require a rider or an endorsement.
            - Extended coverage can include damage from hail, wind, flood and snow. It can also include acts of vandalism and theft, and damage from electrical or water system failures.
            - Personal items (clothing, jewelry) may be covered, up to a set dollar amount.

- Separate structures from the farm home such as barns, sheds detached garages can be covered, but they need to be itemized.
- In general, a property insurance policy can be written to meet your unique needs. Coverage, exclusions, amounts of protection and deductible payments can all be tailored to meet your needs.
- The challenge for the agribusiness owner is to identify all the business's risk management needs and the level of protection needed.
    - You are in the best position to determine the risks of your business. Think about all the "What if?" scenarios that are possible for your business. For example, what might happen if there was an accident while transporting livestock?
    - A review of Lesson 1-4: Risk Management would be helpful in identifying the different types of risk involved in your business.

- Liability insurance protects the agribusiness owner against a lawsuit or claim for injuries to person or property due to some alleged negligence on the part of the agribusiness.
    - Damages or injury can range from physical injury to somebody on the agribusiness's property, to psychological and/or economic harm from a wrongful termination of employment.
- Liability policies can have many exclusions, so it is important that the business owner reviews the policy carefully. For example, family members might be excluded from coverage, or the coverage may not extend to non-farm operations.
- Crop insurance can protect the producer from losses due to crop failure or sharp market price changes.
    - Generally, crop insurance (called Multi-Peril) protects the farmer against crop failure due to natural events including drought, excessive moisture, freeze and disease.
    - There are many different types of crop insurance that cover different aspects of loss.

- One type of coverage protects against loss of crop yield, where a payout is made at the point where a certain loss of yield is realized. The specific levels of payment and yield loss need to be agreed upon in advance.
- Another type of coverage protects against revenue loss because of falling market prices, low yields or both.

- As with other types of insurance, there can be important exclusions and deductible payments involved, so it pays to review these policies carefully.

- Health insurance is another important protection to consider.
  - While one might not consider health insurance a central concern of the agribusiness, in fact, it is one of the most important.
  - The human resources of any company are critical to its success, and the health of the company's ownership and employees is directly related to the company's bottom line.
  - Providing health insurance for owners and employees protects the company from illnesses and injuries that can jeopardize work productivity, and also from the financial bankruptcy that medical bills can create.
  - Closely related, disability insurance provides a steady income when an individual is unable to work for extended periods due to some illness or injury.
- Finally, life insurance is an important part of estate planning and succession planning.
  - For example, if the agribusiness will go to surviving family members upon the death of the principal owner, then a life insurance policy could ensure that estate taxes do not cripple the business.
    - It could likewise ensure that other financial obligations do not harm the wellbeing and success of the family or the agribusiness operation.
  - Long-term health care insurance is a closely related concern. It pays benefits if someone is in a nursing home or requires assisted living.
    - This type of insurance can protect the family and agribusiness from the extremely high costs associated with long-term health care.

TOPIC 2: Making Decisions About Insurance.

Learning Outcome: Students will understand the considerations in deciding to use insurance and what type of insurance to use.

- When deciding to use insurance, there are a number of important considerations. The first step is to conduct a careful risk management analysis of the agribusiness. A review of Lesson 1-4: Risk Management would be helpful.
    - As mentioned in Lesson 1-4: Risk Management, there are four major steps to risk management:
        1. Risk Identification: knowing and appreciating the risks.
        2. Assigning Probabilities and Outcomes: determining the chance of the risk happening and the potential results of the risk if it happens.
        3. Identify Risk Goals: deciding upon what you want or need to accomplish regarding the risk.
        4. Identify the Risk Management strategies, tools and products: learning about the risk management solutions and choosing the right ones.
    - Once the business's risks have been identified and their probabilities and outcomes determined, then the decision is how to manage the risk. There are four major choices on how to manage risk:
        1. Shift the risk to someone else. You can shift risk through the use of insurance policies, as well as contracts, forward pricing and transferring the ownership of product.
        2. Reduce the risk. Reducing the likelihood of loss can include improving safety practices, for example.
        3. Avoid the risk. You can avoid the risk by simply not engaging in the activity that has that risk. For example, you may choose not to sell retail cuts of meat because of liability risks related to food safety.
        4. Do nothing. In other words, you decide that you will accept the risk and potentially absorb the full loss.
            - This choice may involve self-insuring, which means that the business maintains a reserve that can be used to cover the loss.
            - Doing nothing does not mean simply ignoring or denying the risk. It means making a deliberate decision to accept the risk and full loss. If your business cannot do that, then you need a different risk management plan.

- In some cases, the decision is already made for you and insurance coverage will be required.
    - For example, many financial institutions require business assets that have liens or mortgages on them to be insured, such as buildings and farm machinery.
    - Some states may require insurance. For example, workers compensation insurance may be required if you have a certain number of employees.

➢ Once a general risk management assessment is made for the business, the next step is to identify those assets that are at risk and need to be insured against loss.

- These assets should first be critical to the operations of the business, and second, of high enough value that their loss and replacement would be financially damaging to the company.
- The table below illustrates the types of risks and events that should be insured.

Cost of Occurrence	**Probability of Occurrence**	
	Low	***High***
Low	Keep Risk 1	Keep Risk 2
High	Transfer Risk 3	Insurance too costly or not available 4

Reproduced from Howell, Beverly Riggs. nd. Farm and Ranch Survival Kit, Issue 5. USDA Ag Risk Library.

- In Box 1, the probability of the event occurring is low, and the costs of such an event are also low. In these cases, there is no need for insurance.
- In Box 2, the probability of the event occurring is high, but the costs of the event are low. There is no need for insurance.
- In Box 3, the probability of the event is low, but the costs of the event are high. These cases should be insured.
- In Box 4, the probability of the event is high, and the costs of the event are high. Insurance companies will not cover these cases or if they do, the premiums will be very costly. In these cases, try to reduce or avoid the risk, or be prepared to accept the risk and absorb the loss.
- Farm inventory checklists, financial statements, farm maps, and other business and household documents can help you identify those assets that should be insured against certain events.

➢ After you have decided what to insure, the next decision is for how much? In other words, what dollar amount should an asset be insured for?

- Assets can be insured at their market value. That value is usually reflected by the initial purchase price and then is adjusted over time by factors such as depreciation, inflation or market forces.
  - Depreciation and normal use will lower the market value of assets over time.
  - Inflation may cause the value of assets to rise beyond depreciation, for a net gain of market value.
  - Other market factors, such as land values, may cause the values of assets to rise or fall over time.
- Assets can also be insured at replacement value. That value is the cost that it would take to replace the lost asset today.
  - For example, a farm house might have a market value of $40,000 (if it were sold today), but it might cost nearly $100,000 to build a new house if the old one were to burn to the ground.
    - In that case, if the home were insured at market value and was lost, you might only be able to afford to live in a trailer.
- The bottom line is that when considering how much to insure an asset, think about how much it would cost to replace that item, how essential it is to your business, and how quickly it would need to be replaced to keep your business running.

- The trick is to insure your assets for enough so that you avoid financial catastrophe, but not so much that you are overpaying premiums.

➢ Once you have decided what to insure, and for how much, the next step is to identify an insurance agent and the types of policies that he or she can offer.

- The first step is to review all your existing insurance policies to make sure what is covered and at what premiums. You can often save money by bundling different types of insurance policies with the same insurance agent. You also want to make sure that you will not be insuring anything twice.
- Make sure to review the financial standing on the insurance company that the agent represents. An insurance agent might be a nice, honest person, but it is the insurance company that will provide you with protection.
  - Ask your local banker or a trusted financial advisor about potential insurance agents and the companies they represent.
  - Check with your state's Insurance Commissioner. They can tell you what insurance companies have the fewest or most complaints as compared to the number of policies they have.
- Make sure that the insurance agent provides you with a complete insurance coverage plan that fits your needs. They should not try to sell you insurance you don't need or for more than you need.
- Try to choose the highest deductible amounts that you can afford, as these will significantly lower your premiums.
- Always ask for any discounts, which may be available for good history or behaviors.
- Try to pay premiums annually, as they usually are cheaper than monthly payments.
- And, as always, carefully read and review the policies, paying particular attention to any exclusions or special conditions.

Case Study: Mary Makes the Decision on Insurance.

Mary and her husband John run a cow-calf operation on about 1,500 acres of land. They own the land with a mortgage and still owe about $120,000. They also own the farm house and detached structures that have a market value of about $50,000. Tractors and other farm machinery and equipment are probably worth about $100,000 on the market. Their livestock is worth about $40,000 on the market today. They employ one full-time ranch hand and some part-time help.

John runs the daily operations of the ranch, and Mary handles the bookkeeping and makes the major financial decisions. Mary also teaches at the local high school and her wages and benefits (health, disability and life insurance, pension plan) make her the primary wage earner for the family. Without Mary's teaching job, the family and business could not continue to operate. Without John, the household could survive financially, but the ranch operation might not.

Mary and John are both in their fifties and want to retire in about 15 years. Their dream is to buy a beach house in Florida and spend their retirement days fishing and gardening. Mary and John have saved about $50,000 for their retirement, plus can count on a modest payout from Social Security and Mary's school pension. Their two children are grown and have their own families and careers. They live in the city and are not interested in ranching.

Currently, Mary has health insurance for the whole family through her teaching job, and disability and life insurance ($100,000) on herself. Their property insurance (fire and liability) covers the house and detached structures for $50,000, with a personal items rider that covers an additional $2,000. The property insurance does not cover injuries for employees working on the farm property. They have basic auto insurance (public liability/property damage) on their two vehicles for $35,000 each. Both vehicles are paid for and have little market value.

One day, Mary read a newspaper story about a ranch family who lost everything when their house caught fire. It was a freak accident due to an electrical problem. That got her thinking about their retirement plans and the risks of life. John has no insurance except for medical through Mary's job. The ranch's land, livestock, equipment and machinery are not insured. What would happen if something terrible happened?

Discussion questions:

What should be Mary's first steps in developing a risk management plan?

What decisions does Mary need to make regarding insurance?

What types and levels of insurance would you recommend for Mary?

What information is missing and needed before a final decision on insurance can be made?

TOPIC 3: Life Insurance and Estate Planning.

Learning Outcome: Students will understand the use of life insurance in estate planning.

- As mentioned in the first topic of this lesson, life insurance for farmers and ranchers is an important consideration in estate and succession planning.
    - Life insurance protects the family against perhaps the worst case scenario: the loss of a wage-earning family head.
    - In all families, life insurance provides protection against the death of a wage earner whose loss of income could have financially crippling effects on the household.
        - Life insurance can replace lost wages and ensure that the family meets its living expenses.
        - Life insurance can also pay off existing debts (such as the home mortgage) or anticipated debts (such a college loans for the children).
    - For farming and ranching families, life insurance offers additional estate transfer and succession benefits.
        - Life insurance can pay estate taxes that can be so high as to force the family to sell the operation simply to pay the tax.
        - Life insurance can also pay off outstanding business debts that the new owners cannot, or do not want to assume.
        - Finally, life insurance can pay for costs associated with transferring the business to new ownership.
- Life insurance policies, like other types of insurance, are based on a large pool of policy holders contributing premiums, and a small group of claimants at any given time.
    - In general, life insurance premiums are based on life expectancy rates based on age, gender, health condition, lifestyle and other factors.
    - Of course, premiums are also based on the amount of payout should a claim be made.
        - The amount of coverage needs to be carefully considered based on the current income of the wage earner, his or her remaining work years, as well as years and the amount of debt and other financial obligations that would need to be covered.

- Your insurance agent can be helpful in advising you on the amount of life insurance you need, but the final decision should be based on your family's needs.

➢ There are several types of life insurance policies, each with advantages and disadvantages.

- Term life insurance is the simplest and least expensive type. It is an agreement that the insurance company will pay a certain amount to your beneficiary upon death, and in return a premium will be paid for a set time period or term.
  - Once the time period or term has concluded, the agreement ends. There is no residual value in the policy, and no further premiums are owed.
  - If additional life insurance is needed after the end of the term, a new policy must be written.
  - Premium payments can be level over the term, or can be graduated so that premiums are cheaper during the younger years of the term and become more expensive in the older years of the term.
  - The advantage of this type of life insurance is that it is relatively inexpensive, provides an immediate payout to your beneficiary, and provides good protection for the period of time.
  - The disadvantage of term life insurance is that there is no residual value in the policy after the term ends, and it is not permanent. Once the term ends, there is no protection.
- Whole life insurance collects larger premiums in younger years to offset higher premiums in older years.
  - In this way, it uses level (but higher) premium payments to provide permanent coverage.
  - Higher early premiums build up a cash reserve from the excess needed at that time. The cash reserve that generates interest and grows over time.
  - In some policies, the cash reserve is inseparable from the death benefit and so the beneficiary only receives the death benefit. Other policies may allow the beneficiary to receive a benefit from the cash reserve.
  - The advantage of this type of life insurance is that its premiums remain constant over the life of policy, payout is an immediate lump sum, and it is permanent (as long as premiums are paid).

- The disadvantage of whole life insurance is its higher premium costs.

- Universal life insurance combines the characteristics of whole life insurance, with an associated investment sub-account that is managed separately.
  - Premium payments are flexible (as long as the base life insurance amount is met) and any excess cash reserves is put into investment sub-accounts.
  - The investment sub-accounts can include various types of investments that provide a range of growth rates and risk (relatively safe). These are sometimes called variable life insurance policies.
  - The advantage of this type of life insurance is that its premiums are flexible, the payout can also be flexible, and it is permanent (as long as premiums are paid).
  - The disadvantage of universal life insurance is its higher premium costs, and that you may find a higher rate of return in other investments.

- There are many other types and variations of life insurance policies on the market. It is important that you work with a trusted financial advisor and insurance agent to find the policy that best meets your needs.
  - Be aware that unscrupulous agents have been packaging some reverse mortgage products (where you draw upon the equity of your home), with insurance annuities that pay out at regular intervals.
    - Although combining a reverse mortgage with an annuity may sound attractive, it is almost always more expensive and more risky than using just a reverse mortgage.
    - These products may sound very good, but they are complex and require careful thought about how these products will meet your long-term needs.
    - You should ask yourself how these products will meet your needs now and 10 years and 20 years from now.
    - Some cross-selling of reverse mortgages and insurance annuities may break state insurance laws.

References

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The Business of Indian Agriculture

MODULE 3: Financial Management

LESSON 3: Understanding Insurance

Introduction to Insurance Quiz

Circle the number, letter, or "True" or "False" corresponding to the best answer.

1. True or False: Disability insurance provides a steady income when an individual is unable to work for extended periods due to some illness or injury.

2. Choose the Best Answer: Insurance works by:

    1) Pooling the premiums paid by a large group of policy holders
    2) Making payments to a small group of claimants
    3) Calculating the chance of loss or risk carefully
    4) All of the above answers are true about insurance
    5) None of the above answers are true about insurance

3. True or False: Crop insurance is an important part of estate planning and succession planning.

4. True or False: Crop insurance can protect the farmer against crop failure due to natural events including drought, excessive moisture, freeze and disease.

5. Choose the Best Answer: Property insurance protects the agribusiness owner from loss/damage to:

    1) Buildings, equipment, crops or animals
    2) Long-term health care
    3) Crop failure or low yields
    4) Loss of life
    5) All of the above are true of property insurance

6. True or False: Liability insurance protects the agribusiness owner against a lawsuit or claim for injuries to person or property due to events considered as "acts of God" where no one is to blame.

7. Choose the Best Answer: Extended protections beyond a basic fire policy may include:

a) Damage from hail, wind, flood and snow

b) Acts of vandalism and theft

c) Personal items such as clothing and jewelry

d) Separate structures from the farm home such as barns, sheds and detached garages

e) All of the above answers are correct

8. True or False: Providing health insurance for owners and employees protects the company from illnesses and injuries that can jeopardize work productivity but also from the financial bankruptcy that medical bills can create.

9. True or False: A life insurance policy could ensure that estate taxes do not cripple the business upon death of the business owner.

10. True or False: Long-term health care insurance pays benefits if someone has a workplace injury and cannot work for an extended period.

Module 3:
Financial Management

LESSON 4: Financial and Strategic Planning

The Business of Indian Agriculture

MODULE 3: Financial Management

LESSON 4: Financial and Strategic Planning

Lesson Topics

This lesson covers the following topics:

- Family Financial Planning.
- Long-term and Strategic Planning.
- Whole Farm Planning.

Learning Objectives

Upon completion of this lesson, participants will:

- Understand family financial planning as a critical component of successful financial management.
- Understand how long-range and strategic planning can help an agribusiness prepare for the future more effectively.
- Understand the use of whole farm planning as a holistic planning tool.

Definitions

Goals: Goals support the mission statement with detailed directions that can be planned and executed. Goals are realistic, achievable, measurable and directly related to the company's vision and mission statements.

Mission Statement: A mission statement is similar to a vision statement, but more detailed and more focused on the present. It supports the vision statement by adding more information on how that vision will actually be achieved.

Net Income: Total expenses subtracted from total income will equal net income. This value is often reflected in an income statement.

Net Worth: Total liabilities subtracted from total equity/assets will equal net worth. This value is often reflected in a balance sheet.

Vision Statement: The vision statement reflects the core values and deeply held beliefs of the company's owners and employees. Its role is to communicate an overall purpose, direction and/or meaning of the company.

Whole Farm Planning: A holistic method of farm, ranch and agribusiness planning with a focus on the family-run business. It combines and integrates family planning, business planning, and natural resource and land use planning.

TOPIC 1: Family Financial Planning.

Learning Outcome: Students will understand family financial planning as a critical component of successful financial management.

- Just as a business plan represents the detailed goals and strategies of an agribusiness, so does a family financial plan for the family's goals and strategies.
    - A family financial plan should contain all the family's goals, aspirations, resources and roles of all the family members. It is a collective team effort.
    - Getting everyone in the family onboard with a financial plan may be a challenge when there are competing interests. A successful planning effort will require good communication, negotiation and compromise.
        - Some older members of the family may have goals related to retirement or a second career. Other family members may be interested in home ownership or establishing their first career. Younger members might want to save for college or a new car.
        - None of these goals prevents pursuing the other goals of the family. However, resources are limited, and so the financial plan will need to prioritize goals and share resources.
    - Another important aspect of family financial planning is creating an emergency plan if financial or other disaster hits the family.
        - This should include an analysis of risk, and using risk management strategies for the household.
- The first step in family financial planning is to understand your current financial situation.
    - The family should collect all the necessary financial information, such as income and expenses, liabilities and debt, and equity and assets.
        - In many ways, this is a similar process to developing financial statements for the agribusiness (discussed in Module 2: Accounting), except that it takes into account all the family's members.
            - Family members may or may not all live in the same house. However, if they are participants in the financial life of the family, then they should be included in the planning.
            - The first discussions should take place between the principals (usually the husband and wife). Then discussions should involve children, grandparents and other family members.

- Much of the work of gathering your financial information is discussed in Lesson 3-1: Spending, Saving and Budgeting.
- Income should include any non-farm wages, rent payments, and interest earnings. If you pay yourself a salary from your agribusiness, then include that as well.
    - Remember not to mix the agribusiness finances with your family financial planning. This planning is focused on the family.
- Expenses include regular monthly bills such as mortgage or rent, car payments and utilities. They also include living expenses such as food, clothing and personal spending.
- Liabilities and debt include any outstanding loans, mortgages and credit cards. List the total amount owed, not the monthly payment amounts (list the payments under expenses).
- Equity and assets include everything you have that has value. Include the equity value in your home, land and cars, as well as savings, investments, insurance policies and pensions.
- Subtracting your total expenses from total income will give you your net income. This is like a family income statement. If your net income is negative, then you are spending more than you make, which requires attention.
- Subtracting your total liabilities from total equity/assets will give you your net worth. This is like a family balance sheet. If your net worth is negative, one of your first financial goals should be to move into positive net worth territory.

➢ The next step in family financial planning is to identify and prioritize your family's goals.

- As mentioned the goals can vary among family members, so start with the principals' goals first, then work to include other family members.
- If you've discovered that you have negative net income and/or negative net worth, then fixing those situations should be one of your top financial goals. You will not be able to achieve any of your other goals until you correct negative spending or negative net worth.
- Financial goals will vary for different families, but some financial goals are important for all or most families. These goals may include the following:
    - Saving for a comfortable retirement

- Protecting the family in case of death or disability of a wage earner
- Protecting the family from health care costs
- Estate planning and succession planning
- Owning a home
- Starting a new business or a second career
- Having children
- Saving for college
- Paying off debt

- It will help to write down all the goals that are important to you.
  - You can categorize them as long-term (more than 10 years), medium-term (about 2 to 10 years), or short-term (1 year or less) goals.
  - Then, within each category, rank them in importance.
  - The table below provides an example. In this case, long-term goals include: 1) protecting the family from death and disability, 2) having a comfortable retirement and 3) downsizing the home after the children leave. Medium-term and short-term goals are likewise listed and ranked.

Long-term goals	Medium-term goals	Short-term goals
1. protect family from death/disability	1. buy new car to replace old one	1. pay off credit card debt
2. have a comfortable retirement	2. save for college for children	2. buy a new washer and dryer
3. downsize home after children leave – sell house and buy smaller one	3. help children with down payment on their first house	3. put more money each month into savings account
4. have a smooth transfer of estate and business to children	4. save for month-long vacation in Europe	4. paint the exterior of house
5. start a new web-based business	5. remodel the kitchen, with all new appliances	5. save for one-week vacation at Disney World

  - Then, rank the top 2 or 3 in each category across categories to give you your overall priorities, as in the example below.

Long-term goals	Medium-term goals	Short-term goals
1. protect family from death/disability	5. buy new car to replace old one	2. pay off credit card debt
7. have a comfortable retirement	6. save for college for children	3. buy a new washer and dryer
downsize home after children leave - sell house and buy smaller one	help children with down payment on their first house	4. put more money each month into savings account
have a smooth transfer of estate and business to children	save for month-long vacation in Europe	paint the exterior of house
start a new web-based business	remodel kitchen, with all new appliances	save for one-week vacation at Disney World

- For this family, the overall ranking of the family's financial goals, from most important to less important, are:

    1. Protecting the family from death and disability of the wage earner
    2. Paying off credit card debt
    3. Buying a new washer and dryer
    4. Putting more money into the savings account each month
    5. Buying a new car to replace the old one
    6. Saving money for college for the children
    7. Planning for a comfortable retirement

- The other goals do not go away. They simply go to the back burner while the planning starts with the priority items.
- Each priority goal should have a rationale or justification on why it is listed and how it is ranked. There should also be logic to the timing of these goals, so that accomplishing one goal prepares you for succeeding on the next goal. For example:

    1. **Protecting the family from death and disability of the wage earner:** This is the worst thing that could happen to the family and, if it did, then it would be a financial disaster and all the other goals would be lost.
    2. **Paying off credit card debt:** The family owes about $5,000 in credit card debt at 26% interest. The interest payments are extremely costly and are limiting the family's ability to save and plan for the future. The family needs to first stop the financial bleeding.

3. **Buying a new washer and dryer:** Both appliances are over 10 years old and in constant need of repair. Repair costs are eating into the budget and are wasted money. New energy-efficient appliances will save money over time.

4. **Putting more money into the savings account each month:** The family is barely saving any money, which is necessary for reaching the other financial goals.

5. **Buying a new car to replace the old one:** The old car is paid for, but repair costs are rising and it gets terrible gas mileage. In a few years, it will be time for a new, more gas-efficient car, which will save money in the long-term.

6. **Saving money for college for the children:** The oldest child will be enrolling in college in 9 years. The average cost of tuition at the public university within the state is $18,600 per year. The second child will enter college in 12 years.

7. **Planning for a comfortable retirement:** Assuming that the house is paid for, about $1,000 a month is needed to live comfortably.

- The final step is to develop detailed plans for achieving each goal. These plans should include realistic steps with a timeline and a responsible person. For example:

    1. **Protecting the family from death and disability of the wage earner:** Within one month, the husband and wife will review the current financial situation and research different types of insurance plans. By two months, they will contact an insurance agent and discuss options. By three months, they will purchase a life/disability insurance policy.

    2. **Paying off credit card debt:** Within one month, the wife will review the current family income and expenses, determine how much can be paid monthly to reduce credit debt as quickly as possible, and then begin making payments.

    3. **Buying a new washer and dryer:** Within one month, the husband will research the costs and features of new appliances, review the current family income and expenses, and determine how much can be saved each month for the new appliances. By two months, saving for appliances will start, and purchases will be made once the savings goals are reached.

4. **Putting more money into the savings account each month:** Within one month, the wife will review the current family income and expenses, and determine how much can be saved each month. By two months, saving will start. The start of this goal may be delayed until the previous two goals are achieved first.

5. **Buying a new car to replace the old one:** Within one year, the husband will research the costs and features of a new car. A savings goal will be made, and saving will start. The start of this goal may be delayed until the previous goals are achieved.

6. **Saving money for college for the children:** Within one year, the husband will research the costs of college tuition. A savings goal will be made, and saving will start. The start of this goal may be delayed until the previous goals are achieved.

7. **Planning for a comfortable retirement:** Within one year, the husband and wife will review the current retirement accounts and contributions and determine if they are adequate to meet their goal. If the current retirement plans are found to be inadequate, adjustments to retirement investments and contributions will be made within a year.

TOPIC 2: Long-range and Strategic Planning.

Learning Outcome: Students will understand how long-range and strategic planning can help an agribusiness prepare for the future more effectively.

- Just as it is helpful to develop a family financial plan with a set of goals and strategies, it is also helpful for an agribusiness to develop long-range and strategic plans that will help secure financial health.
    - Long-range and strategic planning approaches planning in a slightly different way than the business plan discussed in Lesson 1-3: Preparing a Business Plan, which would be helpful to review.
        - A business plan is usually made for lenders and other interested parties (as well as the owner), and contains detailed information about all important aspects of the business.
    - Long-range and strategic planning are internal processes that help the owners think about how the agribusiness will continue to succeed and meet the goals of the owners, employees and customers.
    - It involves vision and goal setting, and analyses of the company's strengths, vulnerabilities, opportunities and challenges both now and in the future.
    - It provides an opportunity for the owners to pause from the day-to-day operations of the business and think at a high level about the big picture factors that may affect the business in the future.
    - While financial management is not the only focus of long-range and strategic planning, it is a critical part of any major business analysis or planning.
- The first step in long-range and strategic planning is to develop a vision statement. This statement tells people about the overall values, hopes and aspirations of the company.
    - The vision statement reflects the core values and deeply held beliefs of the company's owners and employees.
    - Its role is to communicate an overall purpose, direction and/or meaning of the company.
    - The vision statement is important because it provides you, your employees, and your customers with a clear sense of the company's identity, which will help everyone support the company's goals.
    - Examples of vision statements may be something like the following:
        - ABC Ranch will produce the highest quality beef products.

- In ten years, ABC Farms will be the leader in winter wheat production in Montana.
- ABC Agribusiness Company will be recognized as the highest quality farm service provider in the Southwest.
- ABC Farm Equipment & Supplies support the livelihood of rural communities through agricultural services and supplies.

- Perhaps even more important than the vision statement is the process that the company goes through to develop the statement.
  - The process starts with every stakeholder in the business (owners, employees, family members and perhaps even longstanding customers). Stakeholders are anyone with a deep interest in the company.
  - The process should be undertaken during a quiet time for the business where time can be taken for deep thought, reflection and discussion.
  - Each stakeholder should write down and discuss their expectations of the company for the future, taking care to being specific and not too vague.
    - If they want, they can also use statements concerning the core values of the business and/or the beliefs of its stakeholders.
  - Remember that developing a vision statement is an internal process, and the vision statement will act as an internal sign post that helps steer the company into the future.
  - Each stakeholder should contribute to the process, and then discussions should focus on developing a statement that includes everyone's input.
  - The final statement should be brief (about 100 words), clear and something that everyone can agree upon.

➢ A mission statement is similar to a vision statement, but more detailed and more focused on the now, the present. It will support the vision statement by adding more information on how that vision will actually be achieved.

- Examples of good mission statements may be as follows:
  - The mission of ABC Ranch is to be recognized as the top producer of high-quality choice and prime grades of beef to the retail marketplace.

- The mission of ABC Farms is to always be one of the farms with the highest yields of winter wheat in north-central Montana.
- The mission of ABC Agribusiness Company is to maintain the highest score in annual customer satisfaction surveys of farm service providers in the Southwest region.
- The mission of ABC Farm Equipment & Supplies is to maintain a highly profitable business so that it can invest in the development of the rural communities it serves.

  - As with the visioning process, the process of developing a mission statement should be a team effort, including all stakeholders of the business, with the goal of finding a statement that reflects everyone's input.
  - The final mission statement should be brief (about 100 words), clear and something that everyone can agree upon.

➢ Like any planning effort, the goals will drive the plans. Developing a set of clear goals is the first step in your long-range and strategic planning.

  - Goals provide even more detail than the mission statement, and they work together to accomplish your mission. They provide the directions that your plans will seek to follow.
  - Examples of good goals may be as follows:
    - Within five years, ABC Ranch will be the top producer of choice and prime grade retail beef in the Upper Midwest region, as measured by gross sales per year.
    - Within one year, ABC Farms will be within the top 10% of farms harvesting the most bushels per acre of winter wheat in north-central Montana.
    - Within two years, the ABC Agribusiness Company will achieve an annual 99% highly satisfied customer score of its services within New Mexico, Arizona and Nevada.
    - Within five years ABC Farm Equipment & Supplies will achieve and maintain a 15% profit margin and invest 5% of profits in rural community programs.
  - Good goals are realistic, achievable, measurable and directly related to the company's vision and mission statements.
  - Detailed plans can then be developed that include specific roles and responsibilities, timelines, costs, other necessary resources and measurements that tell you when your goal has been reached.

- Unlike the process for developing vision and mission statements, it may be easier to set goals by involving just the company's management team.
    - Once the goals are written, they should be shared with all the stakeholders for their buy-in and any suggested revisions.

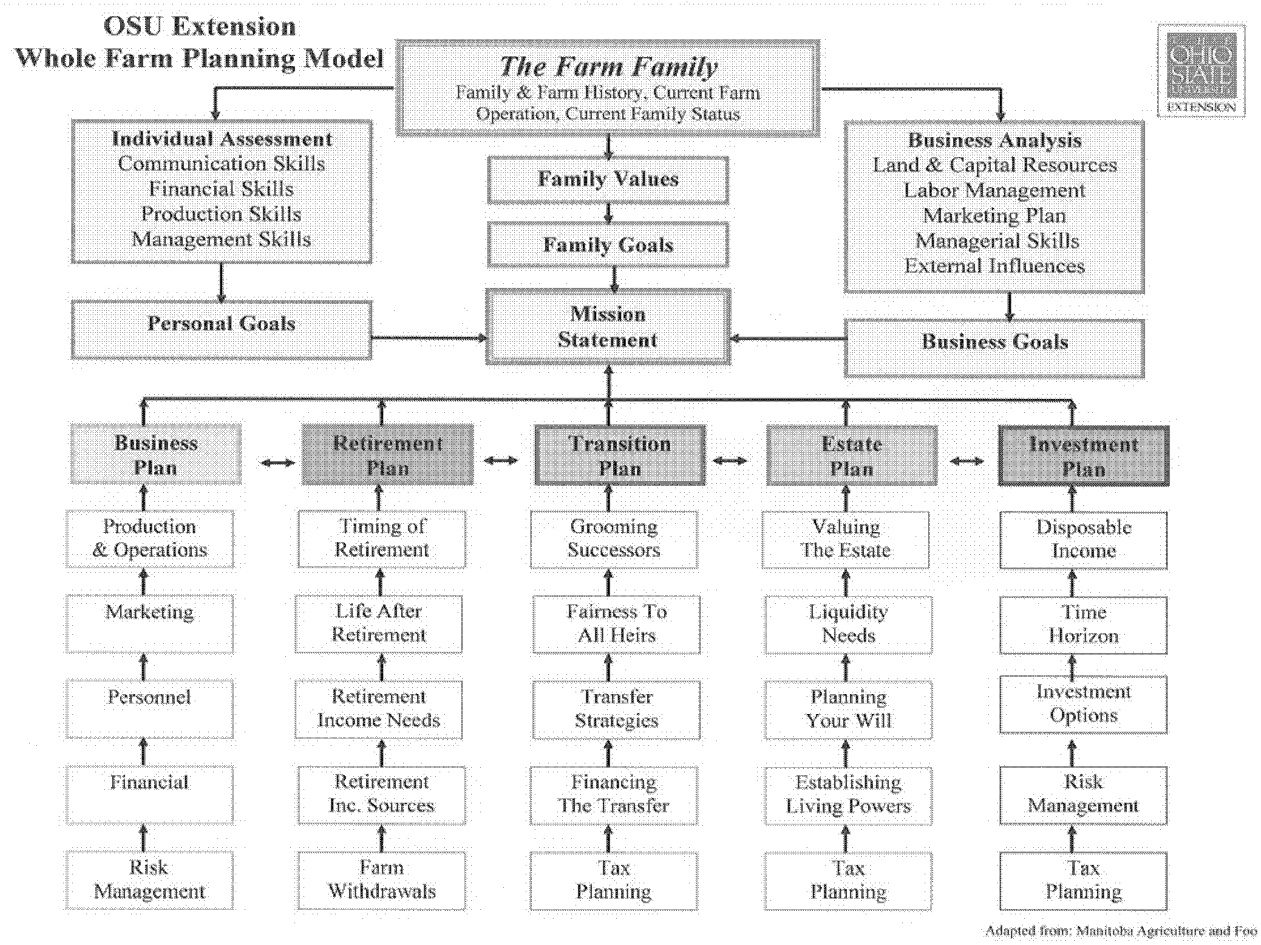
- The final step in the visioning and goal setting process relates back to financial considerations.
    - For each step in the process, ask yourself how the vision, mission, goal and plan affect the financial planning of the agribusiness. In other words, ask specific questions such as:
        - What financial resources will be needed, and by when?
        - What will be the impact on the company's balance sheet, income statement and other financial measures?
        - What needs to change now financially to accomplish the long-range and strategic goals?
        - Are the business's financial plans compatible with the family's financial plan?

TOPIC 3: Whole Farm Planning.

Learning Outcome: Students will understand the use of whole farm planning as a holistic planning tool.

- A holistic method of farm, ranch and agribusiness planning is called whole farm planning. Its focus is on the family-run business and it combines and integrates family planning, business planning, and natural resource and land use planning.
    - Some whole farm models emphasize the economic sustainability of the family business, while others may emphasize the environmental sustainability or the social/cultural sustainability.
    - Regardless of the particular model, whole farm planning is a model that seeks to include all the family's and business's interests in a way that does not exclude or conflict with any family member's interests.
    - It brings together many topics that have been discussed in this lesson and others throughout the curriculum.
    - While there are several whole farm planning models available, there are four general steps to the whole farm planning process:
        1. Set goals for the farm business, the family, your role in the community and the environment. Make sure to include goals both now and in the future.
        2. Conduct an honest appraisal of your resources, including human resources (skills, labor, leadership), infrastructure (buildings, equipment, irrigation), environmental resources (soils, water) and economic resources (assets, access to credit, household finances).
        3. Develop the plan and use it for your decision-making.
        4. Monitor your progress with the plan, using measurable indicators.
- One model of whole farm planning (developed by Ohio State University Extension) uses three main areas of analysis: the individual, the family and the business, with the family in the center. This model focuses on financial and economic sustainability.
    - The model suggests that the skills and capabilities, needs, values and goals of each area (individual, family and business) be considered and integrated into a mission statement. See Figure 1 for an illustration of the model.

Figure 1 – Whole Farm Planning Model



Reproduced from Marrison, David L. 2007. Whole Farm Planning Model. "Building for the Successful Transition of Your Agricultural Business" Fact Sheet Series. Ohio State University Extension.

- This model involves the development of five separate but related plans: business, retirement, transition, estate and investment.
- The business plan includes the long-range and strategic planning discussed in the previous topic, as well as elements of the standard business plan discussed in Lesson 1-3: Preparing a Business Plan.
    - The plan includes consideration of production and operations, marketing, human resources (personnel), finances and risk management.
- The retirement plan includes elements of estate planning (discussed in Lessons 3-3: Understanding Insurance, and 5-4: Understanding Indian Land Regulations and Processes), and family financial planning discussed in the first topic in this lesson.

- This plan includes considerations of the timing of retirement, the lifestyle after retirement, income needs, income sources and withdrawing from the business's operations and ownership.

- The transition plan is also known as succession planning. It makes sure that the business ownership and operations will be transferred efficiently.
  - It includes such things as mentoring successors, being fair to all the heirs, strategies for transferring the business and assets, financing the transfer, and tax planning.
- The estate plan lays out the steps and procedures to handle the business and personal estate upon the owner's death.
  - The plan includes assessing the value of the estate, liquidity needs to handle the death and estate administration, planning of the will, establishing any living powers, and tax planning.
- The investment plan is related both to family financial planning and business planning. It provides direction on the type of investments and levels of risk that the family and business are willing to accept.
  - The plan includes considerations such as how much income goes to investments (disposable), the time horizon (time until payout), investment options, risk management and tax planning.

➢ A whole farm planning model that focuses more on natural resources and land sustainability was developed by the Great Lakes Basin Farm Planning network.

- While this model is focused on a farm business, it can easily be adapted to any agribusiness. Its essential elements include the following:
  - The family's goals: the plan should include the personal goals of the entire family related to business, lifestyle, quality of life and the environment.
  - The economic viability of the family farm business: the plan's focus should be on profitability, not just productivity.
  - Water quality: the plan should protect all sources of water.
  - Soil conservation: the plan should control erosion.
  - Nutrient management: the plan should reduce pollution and maximize soil fertility.
  - Water management: the plan should consider water quantity issues related to irrigation and conservation.
  - Pest management: the plan should minimize pest problems while

protecting the environment.

- Soil quality: the plan should build soil quality over time.
- Crop rotations: the plan should maximize the benefits of crop rotations.
- Tillage: the plan should consider tillage practices that improve soil conservation and quality.

  - In this example, environmental sustainability clearly takes on major importance in the planning process.

- The whole farm planning process that you use may be a combination and adaptation of several models. The point is that the planning process be holistic and honest, and take into account everyone's needs.

References

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The Business of Indian Agriculture

MODULE 3: Financial Managment

LESSON 5: Farm, Ranch and Agribusiness Planning

Family Financial Planning Worksheet

On the next pages, there are blank templates of family financial goal setting tables. As an individual, fill out these tables and then discuss them in small groups.

As you set your financial goals, you may assume the following:

- Your family's net income is $1,000 per month. That means that, on average, you are making about $1,000 more than you are spending each month.
- Your family's net worth is $12,000. That means that all your assets and equity are worth $12,000 more than all your debts and liabilities.
- You and your spouse are both 50 years old and want to retire by 65. You have retirement accounts with a combined value of $100,000. If you want to live on about $1,000 a month when you retire, you will need a retirement savings of about $300,000 to $600,000 depending on how much investment risk you are willing to accept.
- You have $4,000 in credit card debt and are being charged 25% interest.
- You have one adult child who is living on his own, and one 17-year old who will be going to college (in-state, public) next year.
- It's November and your 18-year old furnace is starting to rattle and make strange noises.

Long-term goals	Medium-term goals	Short-term goals

First, write down as many financial goals as you can in the three columns (long-term, medium-term and short-term). Then rank them within each column.

Next, re-rank the top 2 or 3 goals from each column across all the columns and record them in the table below under column 1.

Goals (ranked)	Explanation/Justification	Plan to achieve goal

Next, fill in column 2 with an explanation or justification on why that goal is important and its ranking, and if it depends on other goals being achieved. Finally, fill in column 3 with a detailed plan of how that goal will be achieved.

Discussion questions:

What were your highest priority goals and why?

What was the mix of short-term, medium-term and long-term goals?

What goals relied on other goals to be accomplished first? Why was the order important?

How were your goals similar or different than your peers? If they were different, why (given that you all had the same assumptions)?

The Business of Indian Agriculture

MODULE 3: Financial Managment

LESSON 4: Farm, Ranch and Agribusiness Planning

Visioning and Goal Setting Worksheet

On the next pages, there are blank templates of a visioning table and a goal setting table.

As an individual, fill out the tables with your agribusiness in mind or an agribusiness that you are familiar with, or you can make up an agribusiness to use.

Once you've completed your tables, discuss the questions with your peers.

Questions to Consider	Now (Mission Statement)	Future (Vision Statement)
What business are we in? What products and services do we provide?		
What are my primary production techniques? Are they standard or unique?		
What do I see as the appropriate size and scope (enterprise mix) of the business?		
What are my marketing practices? Are they traditional or unique?		
How is the business to be managed, owned and organized?		
What are its social and environmental concerns and responsibilities?		
What is its human resource structure and philosophy?		
What is its expected financial performance, and how are profits distributed?		
What family values are expected from the business?		

Visioning Table. First, write down as many thoughts as you can about vision and mission statements. It does not have to be perfect. They are just notes to yourself.

Adapted from Jones, Rodney and Sarah L. Fogleman. 2005. *Farm and Ranch Strategic Planning (Visioning and Goal Setting). Farm Management Guide MF-2695.* Manhattan, KS: Kansas State University Agricultural Experiment Station and Cooperative Extension Service.

Next, using your notes from the Visioning table, try to develop several vision and mission statements that capture your business's long-range and strategic direction.

Vision Statements...

- tell people the overall values, hopes and aspirations of the company
- reflect the core values and deeply held beliefs of the company's owners and employees
- communicate an overall purpose, direction and/or meaning of the company
- provide you, your employees and your customers with a clear sense of the company's identity, which helps everyone support the company's goals
- should be brief (about 100 words), clear and something that everyone can agree upon

Vision Statement:

Vision Statement:

Vision Statement:

Mission Statements...

- are more detailed and more focused on the present
- support the vision statement by adding more information on how that vision will actually be achieved
- are a team effort, including all stakeholders of the business, with the goal of finding a statement that reflects everyone's input
- should be brief (about 100 words), clear and something that everyone can agree upon

Mission Statement:

Mission Statement:

Mission Statement:

Goal Setting Table. Next, fill in the table on the next page with one of the mission statements you developed and then identify some goals that support the mission. Then, add notes about the financial considerations related to the goals.

Goals are…

- realistic, achievable, measurable and directly related to the company's vision and mission statements
- the directions with which the plans will seek to follow
- shared with all the stakeholders for their buy-in and any suggested revisions

Financial Considerations…

- ask how the vision, mission, goal and plan affect the financial planning of the agribusiness
- include questions such as:
    - What financial resources will be needed, and by when?
    - What will be the impact on the company's balance sheet, income statement and other financial measures?
    - What needs to change now financially to accomplish the long-range and strategic goals?
    - Are the business's financial plans compatible with the family's financial plan?

Mission Statement	Goals	Financial Considerations
	1.	
	2.	
	3.	

Discussion questions:

What was easy and what was difficult in developing vision and mission statements? Why?

What types of vision and mission statements might you expect from other stakeholders in the business? How would you work to incorporate their views into final statements?

How did your mission statement eventually affect your financial considerations?

Could your goals be reasonably met by financial planning, or were they unachievable? If they were unachievable, what needs to change: the goals or the financial plans?