Exam #2 Review

AAE 320
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Exam #2: Monday November 9, 2020

• Available as Word Document 9:00 AM to 11:59 PM on Canvas page as assignment, on Main class page for download and emailed to you

• **Submit answers as Word Document on Canvas by 11:59 PM**
  • Add clear scans/photos for potential partial credit for quantitative answers
  • Suppose you type “ROROA = 5.7%”, but if correct answer is 6.5%, will look at work to see if you earn partial credit: if right method, but made a simple mistake, will get some partial credit
Exam #2

• 1. Quantitative Questions (math problems to work out)
  • Problem sets: balance sheets, income statements, depreciation, taxes
  • Basically an extended problem set

• 2. Context questions on Quantitative Questions
  • Give short written answers on terms, interpret results

• 3. Non-Quantitative Questions
  • Write short paragraph or few sentences, space provided will guide you
  • Expect questions asking for answers that are longer than on older exams: you have more time & access to more information
  • Questions from materials and issues discussed in class
  • Readings, videos, small groups, assignment sheets, ...
What’s Covered?

• Major topics since last exam
• 1) Farm Finance: Balance Sheets, Income Statements
• 2) Taxes, Business Arrangements and Farm Transfer
• Posted old Exams #2 over similar topics, plus answers
  • Sometimes material ordered differently
Balance Sheets

• Basic structure and how to read one
• Know what current, non-current assets and liabilities are (basic definitions)
  • Be able to give simple examples of each
• Asset Valuation
  • Market vs Cost basis: be able to explain advantages & weaknesses, why you might want to use each
Depreciation

• What it is and why do it
• How to depreciate an asset by the three methods we covered
  • Straight line, Declining balance, Tax table
    • Problems with declining balance and salvage value
  • Tax depreciation a mix of DB and SL
  • Tax depreciation and section 179 depreciation
• Think Breaks, Problem Sets, Old Exams
Balance Sheets

• Liquidity and Solvency:
  • Basic definitions, How are they assessed/measured?
• Know how to calculate and interpret ratios: Current Ratio, Debt to Asset, Equity to Asset and Debt to Equity Ratios
• Basic idea of what’s “typical” in Midwest crop/livestock farming, why some are low and some are high
• Interpret aggregate trends in the industry data
  • What they mean for farming sector’s financial health
Income Statement

• Basic structure and how to read one
• Examples of cash and non-cash revenues and costs
  • Accounts receivable, inventory changes, depreciation recapture vs. depreciation and accounts payable
• Why farms may want to do accrual adjustments of income statement
  • Move costs/revenues to season when grown
  • How much income did I make in 2019?
  • How much income did I make from my 2019 corn crop?
Income Statement

• Know how to calculate and interpret
  • Net Farm Income (Accrual Adjusted NFI)
  • (Rate of) Return on Assets
  • (Rate of) Return on Equity
  • Operating Profit Ratio/Profit Margin

• Think Breaks/class notes, Problem Sets, old Exams for examples

• Basic idea of what’s “typical” in Midwest crop/livestock farming

• Interpret aggregate trends in the industry data
  • What they mean for farming sector’s financial health
Taxes

• Focus on the issues that stay the same, not the details that vary
• Our focus: Income, self-employment, capital gain, gift taxes
• Basics of how these work and pertain to farmers
  • Revenue, Schedule F costs, depreciation and depreciation recapture, capital gains
  • Tax advantages of section 179 depreciation and cash versus accrual accounting
Taxes and Farm Transfer

• How to calculate gain:  = Sale Price – Basis
• What triggers recognizing gain?
  • Sell/buy or give/receive assets???
  • Contribute to or remove from Partnership, LLC, Corporation???
• Why does Basis change?
  • Death, depreciation, sale, gift???
• Gift taxes: what triggers and who pays?
Business Arrangements and Asset Transfers

• Types of Business Arrangements
  • Sole proprietor, partnership, corporation (C or S), limited liability company (LLC)

• Main differences among them
  • Establishment: how do you form one?
  • Management: who makes decisions?
  • Taxation: how does it deal with income taxes and does it trigger recognition of gain?
  • Liability: are owners’ personal assets at risk?
Final Topics

• Inelasticity in Agriculture
  • Great for true/false or short answer
• Let’s Talk: Dairy Farming in WI
• Data on typical financial ratios for farms
• Income tax forms
Exam Preparation

• Know where to find things we covered in class
• What’s covered where: pre-recorded lectures, recorded live lectures, problem sets, other materials
• Treat it like a work project: get it done and move on
• Contact me with questions or problems/crises that arise
• Cell: 608-320-1162 text or call
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