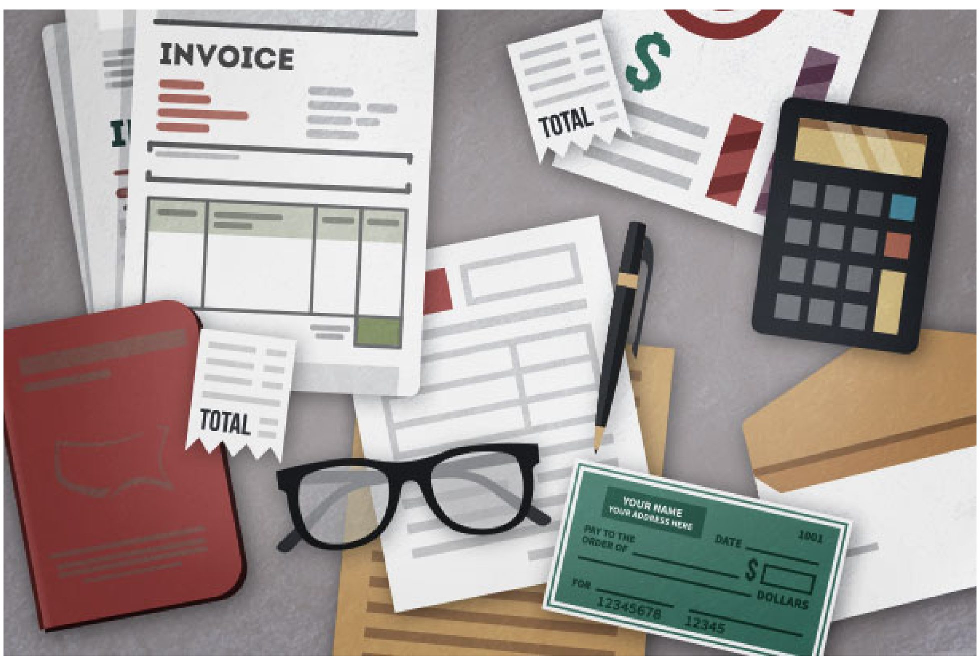
Starting 2021 on the right foot financially

J.E. Tranel, John Hewlett and Jay Parsons for Progressive Cattle   Published on 10 February 2021



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This can be a busy time of year for many farmers and ranchers. Calving season may be in full swing, feeding and other chores are carried out in cold weather, and tax returns are completed and filed. In addition, there are a plethora of meetings, conferences and other educational opportunities.

Finalizing last year's financial records in order to file tax reports and analyze the business is not a fun task to consider. Some farmers and ranchers are required to file their tax returns by March 1, while others have until a later date. Filing deadlines depend, in part, on business form (sole proprietorship, partnership, etc.) and any estimated taxes paid throughout the year.

The procedures and rules pertaining to tax filings did not change much in 2020 for less complicated businesses. New guidance from the Internal Revenue Service and rulings by the U.S. Tax Court may impact all businesses, especially those with a more complex structure or operation.

2020 changes in tax code

The Coronavirus Aid, Relief and Economic Security (CARES) Act, other legislation and executive orders all resulted in changes to the internal revenue code, both temporarily and permanently, as well as created new opportunities for business owners.

The Paycheck Protection Program (PPP) expanded the Small Business Administration's (SBA) loan program for small employers and eligible self-employed individuals impacted by COVID-19. Loans were designed to be forgiven if program requirements were met. Forgiven loan proceeds are excluded from gross income and expenses paid with PPP loan proceeds remain deductible. The rules pertaining to PPP loan forgiveness, qualified uses and tax ramifications are evolving – sometimes on a daily basis. It is critical that business managers stay abreast of the issues and seek appropriate counsel. Two good resources, among many, are **Rural Tax Education** and **Iowa State University**.

Review financial performance

This is also a good time to review last year's financial information and make changes for the coming year. A business owner should question if the business made money. Where might revenues have been increased or expenses cut? What enterprises or departments generated profits or losses? Are there strategies for reducing tax liabilities?

The foundation of business management is financial records that are complete, accurate, detailed and legible. Complete and accurate financial records are needed to file tax returns, develop financial statements, obtain loans and guide management decisions over the coming year. They should be reviewed each year and adjustments made as appropriate. A few tweaks may be all that is needed, or a new chart of accounts may be required to meet desired objectives.

Completion of four financial statements – cash flow statement, income statement, balance sheet and statement of owner equity – will help managers determine profitability, measure changes in net worth, and monitor revenues and expenses. Financial statements may have no relation to income tax reports and tax liabilities. However, complete financial statements can help managers better understand options for adjusting the amount and timing of tax liability.

Cash flow statement

The cash flow budget developed last year should be adjusted to reflect actual cash inflows and outflows. From this, managers will be able to quickly and easily see how much money was brought in and how much money was spent each period and if there were any unexpected or missing sales or purchases. The previous year's statement of cash flow can be a valuable resource for developing a profitable road map for the coming year.

Income statement

An income statement, also called a profit and loss statement or P&L, is used to calculate profitability of a business over the past year. One developed using the cash method of accounting will measure income and expense items when cash changes hands. An income statement developed using accrual accounting matches revenues from the period's production to actual expenses associated with generating that revenue, including non-cash transactions, to provide an accurate estimate of profitability.

Balance sheet

A balance sheet should be completed at the beginning or end of each year. Balance sheets completed at the same time each year provide a measure of business performance over time. Some business owners and managers develop a "book value" balance sheet, a "market value" balance sheet or both. It is important to note that information on the balance sheets does not indicate why those values changed – only that they did change.

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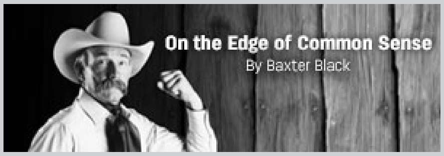

All business owners must file tax reports each year. Complete, accurate, detailed and legible financial records are required to do so. Those same records should then be used to conduct a year-end financial analysis. Did the business truly make money? How might the business improve? Is net worth increasing or decreasing over time? Consult professional counsel (lender, attorney, tax preparer, wealth advisor, insurance agent and others) prior to implementing a particular management strategy.

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