TelFarm Newsletter

Volume 20, Issue 1 Summer 2020

TelFarm Participation Awards

Congratulations to the following farms for reaching these milestones last year and thank you for working with us!

50 Years—

- Wieber Dairy LLC—Fowler
- Wonderland Farms—Eaton Rapids
- LEW-MAX, LLC—Belding
- Fisk Farms—Sand Lake
- Setzler & Sons Farm—LaSalle

25 Years—

- Thorne Farms—Hanover
- Buckham Farms—Schoolcraft

What is the lender looking for?

Jon LaPorte, MSU Extension

One of the most important activities you may have during the year is meeting with your local lender. It is also probably the one that causes you the most anxiety. Whether the meeting is for general operating funds or to purchase capital assets (i.e. equipment, livestock, real estate), you want the lender to make an investment in the farm and approve your request. The key to a successful outcome begins with first understanding what the lender is looking for when you apply for a loan.

Believe it or not, lenders don't simply want to see the "right numbers" put in front of them. What they really want to see is that you are taking charge of the loan approval process. That may seem strange, since you're the one asking for money and they have to say "yes." However, lenders recognize that you are the manager of the farm and know more about the business than they do. They also realize that providing a loan impacts your business and they want to know how that impact will be beneficial to the success of your farm.

Simply showing the "right numbers" doesn't provide enough insight into the success of the business. That is why lenders often proceed with caution and look for assurances that approving your request is a good decision.

To provide assurance, begin with understanding the parts of the loan process and what the lender wants to see. Most loan applications require a balance sheet, your recent IRS tax returns, production history, and a cash flow projection.

<u>Balance Sheet</u>

A balance sheet lists the value for all that you own (assets) and the amount of all that you owe (liabilities). What is a lender looking for here?

It's not simply a matter of putting values to your assets and showing that you own more than you owe. The lender uses the balance sheet as a first look into your operation and first impression of you as a manager. How much detail do you provide? Are all the farm assets included? Are assets valued using reasonable, realistic values?

There are four main areas of concern with the last question: crop inventory, farm machinery, livestock, and real estate.

- Crop inventory should be based on market values as of the date of the balance sheet. This helps identify if you have enough collateral (debt free assets) to secure the loan. It also demonstrates your awareness of market conditions and their potential challenges. Market awareness is crucial if you sell commodities or potentially have to purchase them for feed.
- Farm machinery is always worth more to you than it would be to a potential buyer. What matters to a lender is what you would realistically expect to receive in an actual sale. To value your equipment, start by looking at farm auction listings and avoid sales advertisements. Auction listings give you an idea of what buyers are actually paying for equipment similar to what you own. Sales advertisements only provide what other people "think" their equipment is worth, but the final purchase value may be much lower.
- Livestock should be valued similarly to farm machinery using the same reasoning. This is especially true in cases of high market volatility where prices are known to fluctu-

What is the lender looking for, continued

ate. For much of the livestock industry, market volatility has been an on-going problem for the past several years. One place to look for livestock values is the USDA Agricultural Marketing Service that provides reports from various states across the country. While a report for Michigan is often not provided, these market reports still provide you with an idea of what livestock are actually being sold for in your region.

- Real estate is best valued based on appraisals, which compare sales of similar property within the previous year. However, appraisals can be costly and are generally done prior to a sale or purchase of real estate. Another option is to use the State Equalized Value (SEV) and multiply by two. This is the market value determined by the local assessor. While this value may be less than perceived market prices, it is a good starting point in the absence of actual sales data of similar properties.

IRS Tax Returns & Production History

Loan requests typically require a copy of your IRS tax returns and production history for the past three years. What is a lender looking for here?

Lenders want to gain an understanding of the financial and production capabilities of your farm. They use these documents to review your ability to turn production into revenue and pay expenses during that time period. This review includes calculating an average for the past three years and identifying any trends. Prior to applying for a loan request, you should identify the same average and trends that the lender will see and prepare yourself to talk about them.

If production or revenues are trending down or expenses trending up, what is causing the trend? Being able to talk about your history demonstrates your understanding of what conditions the farm is operating within and what actions you have taken to change them. It also provides an opportunity for you to discuss how you plan to continue working through them and how the loan will aid you in those efforts.

Cash Flow Projection

Loan requests typically include providing a cash flow projection. What is a lender looking for here?

A cash flow projection is an opportunity to demonstrate your ability to make money and address risks or concerns to your business. Lenders want to see a projection that is consistent with your farm's historical production, revenue, and expenses, and also takes into account current market conditions.

To ensure consistency to your history, be sure to start any projection using your farm records. They were used to fill out your IRS tax returns, so they should be used when creating your projection. Then consider any changes you are going to make for the coming year. Are you anticipating lower costs to inputs than in the past? Are production volumes (yields or livestock sold) expected to be higher? Are you using prices consistent with what is available on the market?

These questions can all have an answer of "yes" and the reasons "why" can be acceptable to a lender. The key is being able to explain why those differences exist and how they fit into the overall plan for your business. A common example is introducing a new fertilizer program that increases yields at similar or reduced costs. Another example is having a new livestock feeding program that lowers cost and increases rate of gain efficiencies.

As you prepare to meet with your lender, remember that they want nothing more than to see you be successful. They understand the importance of the request but also that there are risks involved in farming. They consider your well-being and whether additional funding will truly be a help to your operation. Knowing how to assure them that the loan will benefit your farm is what will put you in charge of the process. Most importantly, it will increase the likelihood of a "yes" to your request.

COVID 19 Related Programs Available to Farmers

MSU Extension has compiled a list of COVID 19 Programs with some details about how to qualify, who qualifies, etc. The adjacent table gives you a brief overview of these programs. The full listing and additional resources can be found at https://www.canr.msu.edu/farm_management/Agribusiness-Resources-for-Novel-Coronavirus/

Program Name	Who Qualifies	What it does
Emergency Economic Injury Disaster Loan Program—EIDL	Farmers added in Mar 2020- Less than 500 Employees.	Loan/Forgiveness - $10,000 for an temporary economic injury with fast processing. Forgivable if used for payroll expenses.
Economic Injury Disaster Loan Program - EIDL	Small businesses that have suffered losses in Federal Disaster areas. The CARES Act expanded the program to make it easier for borrowers adversely affected by COVID-19 to get a loan especially farmers.	Loans up to $150,000 for an economic injury. Maturity up to 30 years and interest rates up to 3.75%. Intended for payroll and other operating expenses.
Federal Disaster Loans	Must have farm located in disaster county. County receives declaration of disaster from Secretary of Ag or US President. Only 7 counties in Michigan have received a declaration.	Loan - Restore/replace essential property, pay all or part of production costs associated with the disaster year, pay essential family living expenses, reorganize the farming operation, refinance
Paycheck Protection Program-PPP	Business (including Farms) with less than 500 Employees includes: Pays for 2 and 1/2 months of Payroll including self-employed individuals and qualifying other expenses. qualifying compensation, vacation, medical, health ins, retirement, payroll taxes. Updated on 6-5-2020	Forgiveness -- 60% must be payroll related for forgiveness qualification. 40% other forgivable expenses are mortgage interest, rent, and utilities. 24 weeks or until 12-31-20 allowed for the qualified expenses spend down.
Families First Coronavirus Response Act	Most farms. Farms under 50 employees are required to pay for 2 weeks of leave taken under the act, but may be exempt from the additional 10 weeks of leave (school closing related)	FFCRA covers up to 12 weeks of leave taken between 4/1/2020 – 12/31/2020.
Michigan Disaster Assistance program	A qualified loss of 25% or more in major enterprises or a qualified loss of 50% or more in production of any 1 crop Producers in USDA Declared Disaster counties	Loan at 1%, 5 years, up to $3 million
SBA Express Bridge Loan	Existing SBA Customers	Help to overcome the temporary loss of revenue and can be a term loans or used to bridge the gap
SBA Debt Relief	Existing SBA Customers	SBA will pay 6 months of principal, interest, and any associated fees that borrowers owe for all current 7(a), 504, and Microloans
Employee Retention Benefits	Employers are eligible for the credit for any quarter in which they have either had to fully or partially suspend operations because orders due to COVID-19, or if they have had more than a 50% decline in gross receipts as compared to the same quarter a year ago. For employers that averaged 100 or less full-time employees in 2019	Retain affected employees to receive refundable tax credit
Coronavirus Food Assistance Program (CFAP)	A producer (either a person or a legal entity) must have an average adjusted gross income of less than $900,000 for tax years 2016, 2017, and 2018. The $900,000 limit does not apply to producers for which 75% or more of adjusted gross income comes from farming, ranching, or forestry. Commodities that did not experience a price drop of 5% or more are ineligible for CFAP payments, though the USDA may reconsider excluded commodities in light of credible evidence of a 5% price decline.	Up to $250,000 per person or legal entity; corporations, limited liability companies (LLCs), and limited partnerships are eligible for up to $750,000 if they have at least have three shareholders that meet labor/management contribution requirements

New PPP Loan Update—The Wild Ride Continues

Important Changes

The deadline for applying for aid has been extended. On June 30th, the Senate legislated to extend the deadline for businesses to apply for coronavirus aid under the Paycheck Protection Program (PPP) until August 8th, which was to expire on June 30th.

Apply through any cooperating bank or lender. For agriculture, Greenstone is one of the cooperating lenders.

In general, the borrowers can receive a PPP loan on 2 ½ months of payroll costs based on their aggregate payroll costs using data from the previous 12 months or from the 2019 calendar year.

The forgiveness "covered period" was also increased from an 8-week period to a 24-week period, but not to extend past December 31, 2020. The SBA also reduced the level that eligible payroll expenses needed to cover from at least 75% down to 60% of the eligible forgiveness amount. This eligible forgiveness amount will often be the full PPP loan amount now.

Self-employed profits on Schedule F or C are also consider labor costs with Paycheck Protection Program, and forgivable if documented that they are paid out in draws from the loan.

Qualifying Forgivable Expenses

Eligible payroll costs for the PPP Loan Forgiveness documentation:

- Compensation to employees (net of federal income taxes withheld and FICA/Social Security)
- Payments for vacation, family, medical, sick leave
- Payments required for group health care benefits and premiums
- Payment for retirement benefits
- Payment for state and local taxes on wages
- Net earnings from self-employment (includes Schedule F)

PAYCHECK PROTECTION PROGRAM SBA

You may need to use the detailed payroll report in PcMars to give you all the details needed for documenting the expenses for PPP loan application or for the forgiveness documentation. Just be careful to specify the exact date range needed.

Some non-payroll costs can qualify for forgiveness, if less than the 40% of the forgivable amount. Qualifying non-payroll costs include:

- rent obligations
- mortgage interest
- utilities

An easy way to "tag" any qualifying forgivable cost/expense in PcMars would be to add a unique code, such as "PPPF", in the description field while entering. This code could be saved in the pick list for quick retrieval. Then use the unique code to generate a detailed report of qualifying expenses.

Tax treatment

The general rule is that if 2020 deducted expenses are eligible PPP expenses and are forgiven then the forgiveness is taxable income, hence there is a wash and no change in net income. Some media broadcasts and articles have stated that any forgiven expense is not deductible. Then if the qualified PPP expense is not deducted the forgiveness of the loan principal is not taxable income. The net effect is exactly the same and no change in net income.

The self-employed "labor payments" (draws) are not deductible expenses. Hence, any forgiven PPP loan to "replace" the lower SE income (draws) is then taxable income, the same as if the farm profits were magically increased. Be sure to call us if you have questions.

PcMars 3.0 Upgrade

We just want to remind everyone that the PcMars 3.0 upgrade is on going. We have had many users upgrade to the new version, in most cases, without any issues. We sent out a few communications back in March and April with instructions. If you never received them, can't locate them, or just need additional help, feel free to call us anytime to walk through the process with you.

PcMars Farm Accounting Software

Don't forget, the fee for your 2020 books in Pc Mars is covered by your 2020 TelFarm enrollment fee.

TelFarm Center
Morrill Hall of Agriculture
446 W Circle Dr Rm 414
East Lansing, MI 48824
517.355.4700 (Phone)
517.432.9805 (Fax)
telfarm@msu.edu
http://canr.msu.edu/telfarm

MICHIGAN STATE UNIVERSITY | Extension