

EXIT STRATEGY – SHOULD YOU HAVE ONE?

By Nancy Ervin, Ag Business Consultant

Exit strategies have never been a hot topic in agriculture. Most people who farm for a living do so because their fathers did, as did their grandfathers before that. It is assumed that the family business will just continue on to each passing generation.

But in today's changing environment, it makes sense for business owners to consider their options. Staying in business isn't necessarily the only choice.

An exit strategy is traditionally used by entrepreneurs seeking venture capital. Because of the risks involved in investing in a start-up business, the early stage investors will demand a high rate of return. Achieving this return usually requires an exit strategy. Cash flow and dividends aren't enough.

A well thought-out exit strategy simply clarifies a future destination when you and your investors can expect to reach liquidity.

But what about the established family-owned business? When is an exit strategy really necessary? When the business is no longer profitable, or you just don't feel like running it anymore? Well, yes. But actually, an exit strategy is most effective if it is developed long before then as part of an overall business plan.

A business plan is the road map for your company, and a well thought-out exit strategy simply clarifies a future destination when you and your investors can expect to reach liquidity.

Because each business is different, a realistic exit plan should take into account your particular industry, business life cycle, man-

agement needs, as well as the competitive and political environment. It is also important to consider your personal and financial goals, and how they relate to the future of your business.

Begin by asking yourself why you are in business in the first place. Does it provide the quality of life you desire? Do you plan on passing on the business to the next generation, and if so, do their goals parallel yours?

Next, consider potential exit strategies:

EXIT STRATEGIES	
Merger	Join with an existing company
Acquisition	Business bought outright by an existing company
Sale	Business bought by other individuals
Buyout	One or more stockholders buy out the others
IPO	Sell the shares of the company to the public to be traded on the stock exchange
Franchise	Sell business concept to others to replicate
Succession	Hand down the business to another family member
Liquidate	Sell off the assets

If you are unsure of which exit strategy best fits with your financial goals, it is possible to have your business professionally appraised to determine what its potential value would be, given several different exit scenarios. Of course, tax and estate planning (under current law) should be included in your exit valuation.

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WHAT ARE YOUR FINANCIALS SAYING ABOUT YOU?

by Rich Featherstone, CPA, ABFA

Many farm owners and managers often overlook the signs of trouble within their own financials.

Financial statements tell a lot about your company, ranch or farm. But did you know that as a farm or business manager, it directly reflects upon you? Net income or loss doesn't tell the whole story. If you have income and assets, but not enough cash, and you are always going to the bank or other lender for help, lenders may start asking questions. If you do not understand what your financial statements are saying about your business, you may not be able to answer some of these questions.

Many businesses that are growing quickly experience cash shortages. If you select the wrong type of financing for your operations, the financial statements will disclose that to the trained reader.

Many farm owners and managers often overlook the signs of trouble within their own financials. If you have substantial short-term debt and little long-term debt, in relationship to your short-term and long-term assets, you may end up in a cash crunch. When credit gets tight or expensive, you may be entering into the borrowing market at the wrong time.

Financial ratios for your industry or type of farm are useful when trying to recognize the signs. Are ratios of your competitors available to you? For example, if your type of farm operation has a working capital ratio of 2 to 1, but other farmers in your industry average 3 to 1, that may be revealing something about your profitability, or simply that you are financing your operation incorrectly.

Ratios for many types of ag businesses and farm commodities are available from several sources. If you need assistance in obtaining these comparative ratios, contact Nancy Ervin of our Agriculture Department. You may not only be able to recognize how you differ from the "norm," but possibly some of the reasons why.

Do you finance long-term assets with short-term debt? Do you finance short-term assets with long-term debt? If you do, you probably experience cash shortages or pay too much in interest expense. One of the most common debt structuring problems is the improper use of credit in these areas.

Check the brief "mini" balance sheet below. See if you recognize any problems:

Assets		Liabilities	
Cash	\$ 100,000	Accounts Payable	\$ 150,000
Crop Receivable	600,000	Bank Line of Credit	900,000
Deposits & Prepaids	<u>50,000</u>	Accrued Liabilities	<u>50,000</u>
Total Current Assets	750,000	Total Current Liabilities	1,100,000
Fixed Assets, Net	<u>800,000</u>	Long Term Debt	150,000
		Farmers Equity	<u>300,000</u>
Total Assets	\$1,550,000	Total Liabilities & Equity	\$1,550,000
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What problems do you see, if any? If there are problems, can they be corrected?

Problems:

- This business has relied on its bank line of credit too much. Long-term assets have been acquired, but acquisition debt must be paid off in a year or less to their bank.
- The business has negative working capital. This entity has \$400,000 of debt due in a year or less, which is in excess of the assets that will turn into cash in the same period. The cash won't be available when it is needed.
- The relationship of long-term debt to long-term assets may be an indication that the current lender is unwilling to finance this entity on a long-term basis.

Solution:

In this brief example, there is one simple solution—refinance the long-term assets. This may include finding an alternative lender. The solution should solve cash flow and debt structuring difficulties.

If you are paying attention to your financial statements, you can better plan your future capital, debt and cash requirements. You may even avoid higher cost financing, limitations on getting new debt, and relying on short-term liabilities to manage your cash flow.

Our staff at Baker Peterson & Franklin, LLP can assist you in recognizing problems revealed by your financial statements and analyzing potential solutions.

If you are paying attention to your financial statements, you can better plan your future capital, debt and cash requirements.

CALENDAR

June 16 – Community Salute honoring Sid Cox. Smittcamp Alumni House, CSUF. Ticket information (559) 278-4266

June 21 – Fresno City and County Historical Society summer lecture series, “Valley Voices.” A panel of West Side farmers, including Jack Woolf, Al Dingle, Price Giffen and Jack Stone will share stories of farming on the West Side. Fresno Art Museum, Bonner Auditorium, 7 – 8:30 p.m.

July 19 – Fresno City and County Historical Society summer lecture series, “Valley Voices.” Dr. Jeronima Echeverria, Associate Provost and Professor of History at CSUF, will discuss Basque culture in the Central Sierra, including oral history studies that focus on Basque sheep ranching in Fresno County beginning in the 1870s. Fresno Art Museum, Bonner Auditorium, 7 – 8:30 p.m.

September 9 – Ag Boosters’ Barbecue. Coombs Ranch, Madera. Ticket information (559) 432-2346 or (559) 278-4266

September 19 – Neil Harl Ag Estate Planning and Business Planning Seminar. Reservation information (559) 432-2346

October 4 – Ag One Fresno-Madera Alumni and Friends Wine Tasting, Smittcamp Alumni House. Ticket information (559) 278-4266.

October 25 – 20th Annual Agribusiness Management Conference, sponsored by California State University, Fresno and Bank of America. Reservation information (559)278-4055.

November 13-15 – AgFresno Farm Equipment Exposition

November 13 – Great Raisin Industry Pancake Breakfast

November 14 – Fresno Chamber of Commerce Ag Awards Luncheon honoring the Agriculturalist of the Year and the Baker, Peterson & Franklin Ag Business Award winner. Ticket information (559) 495-4800.

November 15 – Fresno County Farm Bureau BBQ, 237-0263.

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HIRING A CONTROLLER

by Adrienne L. Cantrell, CPA

Do you know whether you need a bookkeeper, an accountant or a controller?

Are you thinking about hiring an accountant for your ag business? Do you know whether you need a bookkeeper, an accountant or a controller? How do you decide? What are the criteria for structuring your accounting department? All of these questions can be intimidating and confusing; especially for people who are not accountants! As a business owner or manager, your expertise is most likely aligned with your specific industry, as it should be. As such, you may need some guidance in developing the best structure for your accounting department.

Defining and filling an accounting position can be a daunting task, but with an organized approach, you can turn it into a manageable and rewarding one, both for yourself and your business. Hiring an accountant not only relieves some of the pressures of your day-to-day operations, but with the right choice, it can potentially bring an insightful and fresh approach to running your business.

Step 1:

What does your business need?

The process begins with determining what your needs are. Do you need a controller or a bookkeeper? What level of education and background are required? Depending upon the size and complexity of your business, the answers to these questions can be very different. By illustrating the differences between a controller and a full-charge bookkeeper, we hope to give practical examples to help you make these types of choices.

A full-charge bookkeeper is responsible for maintaining a general ledger, which is the basis for preparing financial reports, including tax returns and financial statements. They typically do not prepare tax returns or financial statements, but simply ensure that the underlying

accounts are in balance and timely maintained. The full-charge bookkeeper, depending upon the size of the company and the number of supporting staff, would be responsible for accounts payable and receivable, payroll, bank account reconciliation, and other general ledger account maintenance such as inventory and fixed assets. These duties vary greatly depending upon the type and size of business involved. Education requirements can range from technical experience to a two-year degree in accounting combined with three to five years of bookkeeping experience.

In contrast, a controller is typically responsible for overseeing the day-to-day operation of the accounting department as a whole. They would hire and supervise accounting staff, including clerks and bookkeepers. They may review information returns such as for payroll tax, sales tax, and income tax.

Most distinctively, they are typically responsible for financial statement reporting to bankers, stockholders and other external users. In order for these statements to be prepared in accordance with these users' expectations, a controller must be current on the latest accounting standards and pronouncements. The best candidates for a controller's position will have a bachelor's degree in accounting with three to five years experience in either public or private industry accounting. Many controllers are also CPAs, which may be a very desirable combination.

In addition to external reporting requirements, controllers are also heavily relied upon to supply the business owner or other executive management with internal reports. These may include budgets, internal financial statements, gross margin and sales analysis, inventory analysis, and daily cash reporting. Controllers

It is much easier to screen applicants when you know what your ultimate objectives are!

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are also responsible for the organization and operation of the entire accounting department. These duties include establishing sound accounting policies and procedures, monitoring performance of supporting staff, creating and maintaining effective internal controls and providing a strong example of leadership and work ethic. The controller must possess excellent oral and written communication skills to effectively interface with supporting staff and management as well as external contacts such as stockholders, lenders, vendors, and customers.

Depending on the size of your business, an accountant may be the most appropriate option. An accountant generally has more training than a bookkeeper, but lacks the experience and skills of a controller. An accountant may be valuable for a business large enough to require more than one or two bookkeepers, but not large enough to justify the services of a controller. This type of entity generally uses outside professionals to supplement the accounting staff.

Step 2:

Who is the best person for the job?

Once you have determined whether you need a controller, accountant or bookkeeper, how do you find the right person to fit the need? The first step is to determine your expectations. What do you expect from this position? What specific duties and responsibilities will you require of this person? In other words, write a detailed job description. This step is very important! Without a clear objective in mind, you and your company will most likely be disappointed with the results of your personnel search. In addition, once you have made the hiring decision, you will have a clear, written representation of your expectations to pass on to your new employee. As a result, you will be able to move forward with a minimum of ambiguity about the company's goals. As we continue working through the process, let's assume, for illustrative purposes, you have chosen to hire a controller.

In addition to mapping out the controller's job description for future implementation, the same job description will be of great use during the interview and selection process. It is much easier to screen applicants and ask meaningful interview questions when you know what your ultimate objectives are! The individuals who interview for the position will also respect and appreciate that their potential employer has devoted a good deal of thought and time to the hiring process. Remember, it is equally important to find the right controller for your business and to be sure that your business is the right fit for the candidate.

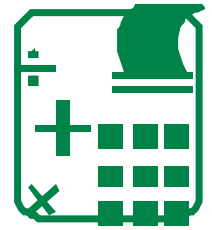
Step 3:

Where do I find the right candidate?

The search for a controller can be conducted in many different ways. There may be qualified candidates within your existing organization, or you may wish to hire from the outside. There are Internet ads, newspaper ads, headhunters and consultants. Let's look at each briefly in terms of pros and cons.

If you have qualified candidates internally, there are advantages and disadvantages to promoting from within. The learning curve is greatly reduced when a new controller has already been with the company for several years in a subordinate position. The dynamics of your office would play a big part in deciding if this possibility is right for your company. The costs of promoting from within are lower than hiring from the outside, as the cost of advertising, interviewing, and training are greatly reduced. However, you may lose the opportunity to have the fresh perspective that someone from the outside might bring to your business. Also, if hiring a controller is simultaneously creating a new position in your company, an outsider may be viewed as more credible in the eyes of your other staff. Either way, hiring from within or without is a decision which must be tailored to best fit your business.

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Hiring a controller from the outside may be more credible in the eyes of other staff members.



With the continuing evolution of the Internet, effective job placement services have become increasingly popular. When compared to newspaper ads, they offer many advantages. Unless your search is intended to be limited to the circulation of your local newspaper, the Internet offers nearly unlimited exposure at a lower cost. For less than the cost of a classified ad, you can post your position with an Internet job placement service and scan their database of posted resumes. For additional information on Internet personnel services, see www.monster.com or www.hotjobs.com.

As mentioned earlier, as a business owner or manager, your expertise probably does not lie in matters of the accounting world. As a result, you may feel ill-prepared to analyze and evaluate the qualifications of prospective applicants. This is where a headhunter or consulting firm can be of great assistance in your search for a controller. Your CPA can also be an excellent resource in helping you plan and follow through with the screening and hiring process. At Baker, Peterson and Franklin, our consulting department has a great deal of experience in assisting our clients with filling their accounting personnel needs. We can also help develop job descriptions, policies and procedures, and internal controls. Please call

our Business Consulting Group with your ideas and questions, and they will be ready to help wherever needed.

**Step 4:
Make them an offer!**

Now that you have taken the steps to determine your needs and find the right person, it's time to close the deal. An important part of filling your accounting department needs revolves around your budget and expectations. You cannot be fully equipped to develop a strategic plan for molding an effective accounting department without current and accurate salary information. There are many different criteria involved in deciding how much to pay your new controller. Critical factors pertaining to salary include: the size of your company; industry standards; the job description; the level of education and experience required; and the going rates for the area. Robert Half, Inc. publishes an excellent salary guide each year for the accounting profession. It provides sample ranges of salaries for various accounting positions and all sizes of companies. A brief excerpt for controllers and full-charge bookkeepers is shown in the illustration.

Now you are ready to make an offer and take "control" of your business!

Salary Ranges			
Position	Company \$ Volume (in millions)	Salary Range (low)	Salary Range (high)
Controllers	250+	\$96,000	\$150,250
	50 to 250	\$79,250	\$104,750
	10 to 50	\$64,500	\$ 84,750
	Under 10	\$53,500	\$ 72,500
Full-charge bookkeepers	25 to 250	\$31,750	\$ 39,000
	Under 25	\$29,750	\$ 36,750

LIKE-KIND EXCHANGES (“REVERSE STARKER”)

by Dennis M. Veeh, CPA

Most of us are aware of the technique of deferring income tax when disposing of farmland by entering into a like-kind exchange. A 1979 decision, in “Starker vs. United States,” paved the way for taxpayers to use like-kind exchanges by allowing the replacement property to be acquired months, or even years, after the sale of the property disposed of in the exchange. Congress, since that decision in Starker, has tightened the rules on the amount of time that is allowed in identifying and acquiring replacement property. The current rules require identifying replacement property within 45 days of relinquishing the property given up in the exchange and actually acquiring the replacement property within 180 days of when the seller relinquishes the property.

However, what happens if you find replacement property that needs to be acquired prior to the disposition of your property? Can we have a so-called “Reverse Starker?”

Neither Congress nor the I.R.S. had officially addressed the possibility of such an exchange until the publication of Revenue Procedure

2000-37 in September 2000. This revenue procedure now provides a “safe harbor” for reverse like-kind exchanges which involves acquiring the replacement property before relinquishing the property to be disposed of in the exchange. The exchange involves “parking” the desired replacement property with an accommodation party until such time that the taxpayer arranges for the sale of his relinquished property. Once a buyer is found, the taxpayer transfers his property to the accommodation party in exchange for the replacement property. The accommodation party then transfers the relinquished property to the ultimate buyer.

The “safe harbor” rules indicate that the I.R.S. will not challenge the transaction as a qualified like-kind exchange as long as the property is held in a “qualified exchange accommodation arrangement” (QEAA). There are various requirements that need to be met under Revenue Procedure 2000-37. Before entering into a reverse like-kind exchange, taxpayers should review all the requirements outlined in Revenue Procedure 2000-37.

The current rules require identifying replacement property within 45 days.

The exchange involves “parking” the desired replacement property with an accommodation party.

Exit Strategy, continued

Finally, incorporate your exit strategy into your existing business. For instance, if your long-range plan is to find a strategic partner to acquire your company, you may want to develop your business in such a way as to make it more “attractive” to other companies. Or, if you plan to liquidate someday, consider what steps might need to be taken in the near future, such as zoning changes.

Whether you are just starting out and trying to raise some capital, or you are in a third generation business, incorporating a variety of well thought-out exit strategies is typically the best approach for dealing with diversity and building owner confidence.

For more information about developing exit strategies, contact the BP&F Business Consulting Group at (559) 432-2346.



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EXIT STRATEGY • HIRING A CONTROLLER • YOUR FINANCIALS • LIKE-KIND EXCHANGES

