

# Profitable Porkers Case Study

## Objectives

- Discover the importance and benefits of accrual based financial statements
- Gain understanding of how to create an accrual balance sheet
- Become skilled at converting a cash basis income statement to an accrual basis income statement
- Learn how to construct a market value balance sheet

## Realizing the Benefits of Accrual Financial Statements

- **Trust your Numbers** – Accrual financial statements deliver an accurate picture of your operation’s actual income and expenses over a given time period. In contrast, cash basis statements only reflect cash activity over a given time period. As a result, profitability reported on cash basis statements can be dramatically different than profitability reported on accrual based statements.
- **Calculate Accurate Cost of Production** – Understanding your cost of production is the foundation for determining if you are viable, competitive and for marketing decisions.
- **Recognize Trends** – As you create accrual statements over multiple quarters and years, it will give you the ability to recognize relevant expense or income trends. With confidence in your financial numbers, you can pursue management changes to address negative trends or ensure that positive trends continue.
- **Gauge Effects of Management Changes** – Accrual financial statements give you a baseline to measure whether or not changes you made actually yielded the results you hoped for.
- **Measure Competitiveness** – How do you compare to the farm down the road, or across the state? Accrual statements allow you to compare your operation against industry benchmarks, which could help you identify your strengths and areas that need improvement.
- **Improve Planning** – Accurate numbers are especially important if you are budgeting or doing a cash flow projection. Accrual statements will give you confidence to plan for the future and subsequently identify variances between your plan and actual results.

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## Profitable Porkers, LLC Overview

In 2010, Paul started a swine operation called Profitable Porkers, LLC. In 2023, Paul decided to significantly alter his business model from a farrow-to-wean operation to a farrow-to-finish operation. Profitable Porkers now owns 1,400 breeding sows and sells its finished market hogs to a regional packing company. Profitable Porkers contracts out its finishing operation to independent finishing floor operators in the surrounding counties. The company leases its breeding and production facilities from Paul's father.

While transitioning to a farrow-to-finish operation definitely presented challenges, Paul felt like he did a good job of controlling expenses and managing the operation. However, both Paul and his lender were quite surprised and concerned when they reviewed Profitable Porkers' 2023 tax return. The tax return was showing a loss of \$1,060,000. Paul's lender requested that Paul create accrual financial statements to determine how the operation fared on an accrual basis. Profitable Porkers, LLC uses a cash accounting method.

## Instructions:

1. Complete the 12/31/23 accrual balance sheet using the following financial data for Profitable Porkers.
2. Calculate the difference between the 12/31/23 and 12/31/22 balance sheet accounts and record the amounts under the difference column.
3. Using the differences you calculated in instruction #2 and the following financial data, determine the adjustments that need to be made to the cash (tax) basis income statement to convert it to accrual basis.

## Financial Data for Profitable Porkers, LLC at 12/31/23:

1. In early January 2024, Paul received the December loan statements. The 12/31/23 balances were as follows:
  - a. 10-year term note payable: \$675,000
  - b. 15-year term note payable: \$550,000
2. In December 2024, Paul's feed company was offering large incentives for prepaying feed that would be delivered in 2023. Paul decided to prepay \$100,000.
3. In January 2024, Profitable Porkers received a check from their packing company for \$95,000. The payment was for hogs delivered in late December 2023.

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4. As the company ramped up its operations in 2023, \$25,000 in additional machinery and equipment needed to be purchased. Economic depreciation expense (used on accrual statements) was \$4,000 and tax depreciation expense was \$35,000. Both depreciation figures include depreciation on purchases made in previous years. Economic depreciation depreciates assets over their expected life, while the tax code dictates the asset life and accelerates depreciation for tax based depreciation.
5. In early January 2024, the company received a \$35,000 bill from the feed mill and a \$10,000 bill from one of their independent finishers for feed and services delivered in December 2023.
6. For his accrual financial statements, Paul has correctly decided to value his livestock at standard values. Standard values provide a consistent measurement of profitability and ensure that profitability isn't distorted by short-term market price swings. At 12/31/23 Paul thoroughly counted his livestock:

<b>Livestock</b>	<b>Quantity</b>	<b>Value/Head</b>	<b>Total Value</b>
<b>Farrowing</b>	1,950	\$25	\$48,750
<b>Nursery</b>	3,750	\$45	\$168,750
<b>Finishing</b>	10,800	\$85	\$918,000
<b>Sows</b>	1,400	\$350	\$490,000
<b>Replacement Gilts</b>	780	\$75	\$58,500
<b>Total Livestock</b>			\$1,684,000

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**Profitable Porkers, LLC  
Accrual Balance Sheets  
December 31 2023 and 2022**

	2023	2022	Difference
<b>Assets</b>			
Cash	25,000	75,000	
#3 Accounts Receivable	_____	20,000	_____
Inventories:			
Feed	85,000	40,000	
#6 Livestock	_____	650,000	_____
#2 Prepaid Expenses	_____	-	_____
#4 Machinery and Equipment	_____	20,000	
#4 Accumulated Depreciation	_____	(11,000)	_____
<b>Total Assets</b>	<b>_____</b>	<b>794,000</b>	<b>_____</b>
<b>Liabilities</b>			
Accounts Payable			
#5 Feed	_____	15,000	_____
#5 Independent Finishing	_____	-	_____
Rent	10,000	-	
Line of Credit	150,000	50,000	
#1 Long term Debt	_____	325,000	_____
<b>Total Liabilities</b>	<b>_____</b>	<b>390,000</b>	
<b>Owner's Equity</b>	<b>_____</b>	<b>404,000</b>	
<b>Total Liabilities and Owner's Equity</b>	<b>_____</b>	<b>794,000</b>	

# Profitable Porkers Case Study

**Profitable Porkers, LLC  
Income Statement  
For the Year Ended December 31 2023**

	<b>Cash (Tax)</b>	<b>Adjustments</b>	<b>Accrual</b>
<b>Sales</b>	1,560,000		
<b>Expenses</b>			
Purchased Feed	1,780,000		
Change in Feed Inventories	0		
Change in Livestock Inventories	0		
Breeding	60,000		60,000
Vet and Medicine	78,000		78,000
Independent Finishing	220,000		
Salaries and Wages	160,000		160,000
Other Labor Costs	30,000		30,000
Rent	110,000		
Real Estate Taxes	12,000		12,000
Repairs and Maintenance	6,000		6,000
Utilities	50,000		50,000
Insurance	14,000		14,000
Supplies	4,000		4,000
Fuel	6,000		6,000
Depreciation	35,000		
Interest	55,000		55,000
<b>Total Expenses</b>	<u>2,620,000</u>		
<b>Net Income (Loss)</b>	<u><b>(1,060,000)</b></u>		