

Statement of Work Option 1: Cost of production

Important Information

- The cost of production Farm Financial Assessment (FFA) includes up to four working days of service provided by the Advisor.
- A minimum of one farm visit is required.
- A follow-up review is available one year after the completion of the initial report.

1. Work to be completed by the Advisor

The Advisor will:

- Before starting work, obtain from the farm business income tax returns for a minimum of two consecutive years as well as any other relevant financial information. In the case of First Nation Farmers and where Income Tax records are not available, the Advisor will try to collect any and all income- and expense-related information relevant to the completion of a financial statement.
- Collect all the data required to complete the analysis and reporting shown in Part 2 of this document.
- Prepare a written report in plain language that the farm business owner can understand. The report will include all of the information shown in Part 2 of this document that applies to this farm business.
- Review and discuss with the farm business the FFA results and make sure that it meets the objectives of the farm business for undertaking the FFA.
- Give a copy of the final FFA report to the farm business.
- Submit the final FFA report to Ontario Soil and Crop Improvement Association (OSCIA) using the Secure Uploading Document System. (Contact OSCIA for instructions and to obtain your username and password.)

2. Farm Financial Assessment report requirements

a) Business Overview (maximum 1 page)

- The name and address of the farm business.
- A brief description of the operation outlining:
 - The type (for example: dairy, grains & oilseeds, grains & livestock, hog farrow to finish or weaner, poultry & fruit), quota holdings, and
 - Size (for example: total acres cultivated, size of herd) of enterprises
- A short statement explaining the farm business's key goals for undertaking the FFA.

b) Financial summary of profitability/viability of the farm operation (in plain language that the farm business owner can understand) including:

- Net worth.
- Net farm income.
- An explanation in plain language of the significance of ratios to the farm business and how the ratios relate to this farming operation.

• Financial plan:

- Assessment of the present profitability/viability of the operation.
- Analysis of the operation's ability to achieve the identified goals in the farm business Action Plan.

c) Farm financial statements

- Opening current market value balance sheet (current and long-term assets and liabilities, and net worth) for the month of the Advisor's initial farm visit. Include detailed assets and liabilities worksheets to support the balance sheet.
- Revenue and expense statement for the previous two consecutive years¹ using filed income tax statement information (from T2042, T1, T2 or CAIS/AgriStability forms.).

¹These requirements may be optional for beginning farmers.

- A current year² revenue and expense projection for 12 consecutive months that will serve as the base year statement to compare with the previous years' statements. (If you find that this information is not available due to extraordinary circumstances, contact OSCIA for an exemption or direction.)
- A current year revenue and expense statement² on an accrual basis for 12 consecutive months providing for accrual adjustments in revenues, sales, inventory changes, and prices and accrual adjustments in variable and fixed expenses.

d) Farm business ratio analysis: six required ratios

The six mandatory ratios are: asset turnover, current ratio, operating profit margin ratio, return on assets, debt to equity ratio, debt repayment capacity ratio.

The Advisor will use these ratios to complete analysis of the following issues:

- **Financial efficiency: assesses how effective the business is in using its assets to generate income**
Asset Turnover = gross farm sales divided by total farm assets
- **Liquidity: assesses the business's ability to pay their bills as they come due**
Current Ratio = current assets divided by current liabilities
- **Profitability: measures how well the business is able to generate a profit**
Operating profit margin ratio = (net farm income + interest expense – unpaid labour and return to management) divided by gross farm sales
Return on assets = (net farm income + interest expense – unpaid labour and return to management) divided by total farm assets
- **Solvency: determines how much the business is relying on debt to finance the business**
Debt to equity ratio = total liabilities divided by equity
- **Repayment capacity: measures the ability of a borrower to repay term farm debt from farm and non-farm income**
Debt servicing capacity ratio = amount available to service debt divided by debt payment requirements

The farm business and Advisor may agree to use additional ratios if appropriate.

e) Financial plan: analysis of detailed cost of production for main enterprises

To complete the financial plan, the Advisor will:

- Identify the main enterprises of the farm business and the expected or historical production/yield results for each enterprise.
- Allocate whole farm revenue and individual expenses to the enterprises (current year and past two years).
- Calculate main margins for each enterprise on a per unit produced basis:
Gross margin = gross enterprise revenue minus total variable costs
Profit margin = gross enterprise revenue minus total costs
- Calculate the breakeven points for each enterprise:
 1. The minimum price to cover variable costs:
Breakeven price to cover variable costs = total variable costs divided by expected (or historical) yield = \$ / unit produced
 2. The minimum price to cover all costs:
Breakeven price to cover total costs = total costs divided by expected (or historical) yield = \$ / unit produced
 3. The minimum yield needed to cover all costs.
Breakeven yield = total costs divided by expected price = unit produced
- Assess and discuss the profitability/viability of each enterprise. Determine if each enterprise is contributing to the profitability/viability of the farm business

² Current year – If a farm business is more than six (6) months into their current fiscal year at the time of the initial visit with the Advisor, the current year for the revenue and expense statement refers to either (a) a financial analysis and input beginning in the first month of their current fiscal year and running forward to the ending month of their current fiscal year, OR (b) projections for 12 consecutive months beginning with the statement date of the balance sheet assuming no operational or financial changes. If the farm business is less than six (6) months into their current fiscal year at the time of the initial visit with the Advisor, the previous fiscal year will be accepted as the current year (unless otherwise agreed to and approved by OSCIA).