

SAMPLE DAIRY
FINANCIAL STATEMENTS
AND
INDEPENDENT ACCOUNTANTS' REVIEW REPORT
DECEMBER 31, 2018

SAMPLE DAIRY
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SAMPLE DAIRY
FINANCIAL HIGHLIGHTS

	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>	<u>2018</u>
<u>Milk production statistics</u>					
Pounds of whole milk produced	46,136,000	49,786,000	52,897,260	59,573,475	65,864,250
Average butterfat test	3.50%	3.55%	3.56%	3.61%	3.78%
Average solids-non-fat test	5.77%	5.76%	5.75%	5.76%	5.79%
Average protein test	3.13%	3.07%	3.09%	3.03%	3.07%
Average daily pounds per milking cow	79	80	78	81	80
Average daily EC pounds per milking cow	81	82	80	83	82
<u>Dairy herd statistics</u>					
Average herd size:					
Milking cows	1,600	1,705	1,858	2,015	2,250
Dry cows	200	225	252	283	294
Heifers	1,553	1,637	1,841	1,905	2,041
Purchase of cows and bulls:					
Number of head	9	95	20	51	22
Total amount paid	\$ 16,967	\$ 180,975	\$ 36,000	\$ 89,352	\$ 33,000
Average per head	\$ 1,885	\$ 1,905	\$ 1,800	\$ 1,752	\$ 1,500
Heifers transferred to milking herd	706	808	835	951	887
Sale of cows and bulls:					
Number of head	357	489	510	568	642
Total amount received	\$ 400,003	\$ 526,776	\$ 403,954	\$ 360,182	\$ 367,940
Average per head	\$ 1,120	\$ 1,077	\$ 792	\$ 634	\$ 573
Number of dead and condemned cows	183	109	102	236	223
Herd turnover rate	30%	31%	29%	35%	34%
Average feed cost per cow per day	\$ 7.74	\$ 6.33	\$ 5.73	\$ 5.75	\$ 5.44
<u>Product price</u>					
Average price received per cwt of milk shipped	\$ 25.99	\$ 18.05	\$ 16.99	\$ 17.29	\$ 15.85
<u>Summarized dairy operations</u>					
<u>per cwt of milk shipped</u>					
Total income	\$ 26.76	\$ 19.11	\$ 17.48	\$ 17.61	\$ 16.12
Operating expenses:					
Feed	11.02	8.96	8.36	8.11	7.67
Herd replacement cost	1.11	1.12	1.64	1.72	1.62
Other operating expenses	7.83	8.32	8.34	8.00	6.77
Total operating expenses	19.96	18.40	18.34	17.83	16.06
Income (loss) from operations	\$ 6.80	\$ 0.71	\$ (0.86)	\$ (0.22)	\$ 0.06

See independent accountants' Review report.

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Independent Accountants' Review Report

To the Partners
Sample Dairy
Brookings, South Dakota

We have reviewed the accompanying financial statements of Sample Dairy, which comprise the balance sheet as of December 31, 2018, and the related statements of partners' capital, income and cash flows for the year then ended, and the related notes to the financial statements. A review includes primarily applying analytical procedures to management's financial data and making inquiries of company management. A review is substantially less in scope than an audit, the objective of which is the expression of an opinion regarding the financial statements as a whole. Accordingly, we do not express such an opinion.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement whether due to fraud or error.

Accountants' Responsibility

Our responsibility is to conduct the review engagement in accordance with Statements on Standards for Accounting and Review Services promulgated by the Accounting and Review Services Committee of the AICPA. Those standards require us to perform procedures to obtain limited assurance as a basis for reporting whether we are aware of any material modifications that should be made to the financial statements for them to be in accordance with accounting principles generally accepted in the United States of America. We believe that the results of our procedures provide a reasonable basis for our conclusion.

Accountants' Conclusion

Based on our review, we are not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in accordance with accounting principles generally accepted in the United States of America.

Supplementary Information

The supplementary information included in the Financial Highlights, Schedule 1 and per hundredweight (cwt) of milk, per hundredweight (cwt) of energy-corrected (EC) milk and per cow columns on the Statement of Income is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information is the responsibility of management. We have not audited or reviewed such information and we do not express an opinion, a conclusion, nor provide any form of assurance on it.

March 21, 2019
Salida, California

Genske, Mulder & Co., LLP

GENSKE, MULDER & CO., LLP
Certified Public Accountants

SAMPLE DAIRY
BALANCE SHEET
DECEMBER 31, 2018

ASSETS

CURRENT ASSETS, pledged:

Cash and cash equivalents	\$	45,368
Accounts receivable, Dairymans Cooperative Inc.		463,173
Inventories:		
Hay - 3,016 tons	\$	238,440
Silage - 35,783 tons		1,206,507
Investment in growing crops		38,723
Total inventories		1,483,670
Prepaid expenses		190,895
Total current assets		2,183,106

DAIRY HERD, pledged:

2,544 Cows		3,945,744
2,041 Heifers		1,696,071
Total		5,641,815
Accumulated depreciation		(1,429,728)
Dairy herd, net		4,212,087

DAIRY FARM AND EQUIPMENT, pledged:

Land - 325 acres		1,446,487
Buildings and improvements		7,261,795
Machinery and equipment		1,823,488
Autos and trucks		166,831
Total		10,698,601
Accumulated depreciation		(5,788,995)
Dairy farm and equipment, net		4,909,606

OTHER ASSETS:

Cooperative retains		26,907
Total other assets		26,907
Total assets	\$	11,331,706

See accompanying notes and independent accountants' Review report.

SAMPLE DAIRY
BALANCE SHEET
DECEMBER 31, 2018

LIABILITIES AND PARTNERS' CAPITAL

CURRENT LIABILITIES:

Accounts payable, feed dealers	\$	555,738
Other trade payables		465,086
Accrued interest payable		18,803
Wages and payroll taxes payable		52,146
Farmers Bank, line of credit, secured by inventories and dairy herd, variable payments monthly plus 4.7% interest, matures September 2019		2,414,350
Estimated current portion of long-term debt		<u>286,000</u>
Total current liabilities		3,792,123

LONG-TERM DEBT:

Notes and loans payable:		
Farmers Bank, secured by real estate and equipment:		
Payable \$15,025 monthly including 3.45% interest, matures January 2021	\$	360,600
Payable \$4,800 monthly including 3.38% interest, matures December 2023		278,208
Payable \$9,395 monthly including 3.35% interest, matures January 2027		865,840
Payable \$10,000 monthly including 3.72% interest, matures January 2030		1,267,200
John Deere Financial, secured by equipment,		
payable \$5,000 monthly, non-interest bearing, matures February 2020		70,000
GM Financial, secured by equipment,		
payable \$1,500 monthly including 3.98% interest, matures June 2022		63,000
Estimated current portion		<u>(286,000)</u>
Long-term debt, net		2,618,848

SAMPLE DAIRY, PARTNERS' CAPITAL:

Balance at December 31, 2018		<u>4,920,735</u>
Total liabilities and members' equity	\$	<u><u>11,331,706</u></u>

See accompanying notes and independent accountants' Review report.

SAMPLE DAIRY

**STATEMENT OF PARTNERS' CAPITAL
FOR THE YEAR ENDED DECEMBER 31, 2018**

Balance at December 31, 2017	\$	4,969,242
Net loss		<u>(36,724)</u>
Subtotal		4,932,518
Distributions		<u>(11,783)</u>
Balance at December 31, 2018	\$	<u>4,920,735</u>

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See accompanying notes and independent accountants' Review report.

SAMPLE DAIRY

**STATEMENT OF INCOME
FOR THE YEAR ENDED DECEMBER 31, 2018**

	AMOUNT	PER CWT OF MILK	PER CWT EC MILK	PER COW
INCOME FROM OPERATIONS:				
Milk	\$ 10,439,484	\$ 15.85	\$ 15.52	\$ 4,148
Calves	93,444	0.14	0.14	37
Patronage dividends	10,423	0.02	0.02	4
Agricultural program payments	45,240	0.07	0.07	18
Farming, net, Schedule 1	(12,169)	(0.02)	(0.02)	(5)
Other	38,819	0.06	0.06	15
Total income from operations	<u>10,615,241</u>	<u>16.12</u>	<u>15.79</u>	<u>4,217</u>
OPERATING EXPENSES:				
Feed:				
Hay	751,971	1.14	1.12	299
Grain and commodities	3,416,058	5.19	5.08	1,357
Silage	1,100,041	1.67	1.64	437
Heifer and dry cow raising	1,323,476	2.01	1.97	526
Cost of feeding heifers	<u>(1,540,251)</u>	<u>(2.34)</u>	<u>(2.29)</u>	<u>(612)</u>
Total feed	<u>5,051,295</u>	<u>7.67</u>	<u>7.51</u>	<u>2,007</u>
Herd replacement cost:				
Depreciation - cows	901,166	1.37	1.34	358
Loss on sale of cows	<u>162,689</u>	<u>0.25</u>	<u>0.24</u>	<u>65</u>
Total herd replacement cost	<u>1,063,855</u>	<u>1.62</u>	<u>1.58</u>	<u>423</u>
Other operating expenses:				
Interest	206,765	0.31	0.31	82
Labor	1,151,292	1.75	1.71	457
Partners salary	147,150	0.22	0.22	58
Depreciation - other	692,404	1.05	1.03	275
Milk hauling	9,251	0.01	0.01	4
Industry assessments	116,013	0.18	0.17	46
Supplies	550,290	0.84	0.82	219
Bedding	246,851	0.37	0.37	98
Repairs and maintenance	299,859	0.46	0.45	119
Utilities	229,994	0.35	0.34	91
Taxes and licenses	118,884	0.18	0.18	47
Insurance	170,625	0.26	0.25	68
Fuel and oil	151,360	0.23	0.23	60
Professional fees	20,773	0.03	0.03	8
Veterinary and breeding	264,361	0.40	0.39	105
Testing and trimming	104,961	0.16	0.16	42
Miscellaneous	38,830	0.06	0.06	15
Cost of raising heifers	<u>(58,685)</u>	<u>(0.09)</u>	<u>(0.09)</u>	<u>(23)</u>
Total other operating expenses	<u>4,460,978</u>	<u>6.77</u>	<u>6.64</u>	<u>1,771</u>
Total operating expenses	<u>10,576,128</u>	<u>16.06</u>	<u>15.73</u>	<u>4,201</u>
Income from operations	39,113	\$ <u>0.06</u>	\$ <u>0.06</u>	\$ <u>16</u>
OTHER EXPENSES:				
Loss on sale of assets	<u>(75,837)</u>			
Net loss	\$ <u>(36,724)</u>			

See accompanying notes and independent accountants' Review report.

SAMPLE DAIRY

**STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED DECEMBER 31, 2018**

CASH FLOW FROM OPERATING ACTIVITIES:

Net loss	\$	(36,724)
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The following is a reconciliation of net loss to net cash provided by operating activities:

Non-cash patronage dividends	\$	(2,545)
Depreciation		1,625,207
Loss on sale of cows		162,689
Proceeds from sale of cows		367,940
Purchase of heifers		(15,875)
Purchase of replacement cows and bulls		(10,500)
Capitalized cost of growing heifers		(1,598,936)
Loss on sale of assets		75,837
Increase in accounts receivable		(23,662)
Decrease in inventories		248,856
Decrease in investment in growing crops		14,261
Increase in prepaid expenses		(179,524)
Increase in accounts payable and accrued expenses		507,422
Total adjustments		<u>1,171,170</u>
Net cash provided by operating activities		1,134,446

CASH FLOW FROM INVESTING ACTIVITIES:

Purchase of fixed assets	(975,936)	
Return of cooperative capital	<u>809</u>	
Net cash used in investing activities		(975,127)

CASH FLOW FROM FINANCING ACTIVITIES:

Borrowing of short-term debt	3,450,367	
Repayment of short-term debt	(3,940,972)	
Borrowing of long-term debt	945,734	
Repayment of long-term debt	(602,665)	
Distributions	<u>(11,783)</u>	
Net cash used in financing activities		<u>(159,319)</u>

Net decrease in cash and cash equivalents		-
Cash and cash equivalents balance at December 31, 2017		<u>-</u>
Cash and cash equivalents balance at December 31, 2018	\$	<u><u>-</u></u>

See accompanying notes and independent accountants' Review report.

SAMPLE DAIRY

NOTES TO THE FINANCIAL STATEMENTS

1. Summary of significant accounting policies

This summary of significant accounting policies of Sample Dairy (“Company”) is presented to assist in understanding the Company’s financial statements. These financial statements and notes are representations of the Company’s management who is responsible for their integrity and objectivity.

Date of management’s review

Management has evaluated subsequent events through March 21, 2019, the date on which the financial statements were available to be issued.

Nature of operations

Sample Dairy is primarily engaged in the dairy and farming business in Brookings, South Dakota. The principal source of revenue is from the production and subsequent sale of milk, all of which is shipped to Dairymans Cooperative Inc., an organization that transports, processes and sells the resulting milk products. Costs of production are dominated by purchases of hay and grain commodities, and profitability can be greatly affected by the Company’s ability to obtain adequate amounts and quality of such commodities at a favorable price.

Income taxes

The Company is operated as a partnership which is not a taxpaying entity for federal and state income tax purposes; therefore, no income tax expense has been recorded in the financial statements. Income from the Company is taxed to the partners on their individual income tax returns. The partners may occasionally make estimated tax payments towards their personal income tax liability from the Company’s bank account. These payments are treated as withdrawals of capital. The Company reports income earned from the partnership on the cash basis accounting method for tax purposes and on the accrual basis accounting method for financial statement purposes.

The Company believes that its income tax filing positions as a pass-through entity will be sustained upon examination, and accordingly, has not recorded any reserves or related accruals for interest and penalties at December 31, 2018 for uncertain tax positions. The Company has a policy under which, if required to be recognized in the future, it will classify interest and related penalties in interest expense in the income statement. The Company believes it is no longer subject to federal income tax examinations for the years prior to 2015 and state income tax examinations for the years prior to 2014.

Cash and cash equivalents

For purposes of these financial statements, the Company considers all highly liquid investments with a maturity of three months or less to be cash equivalents.

Accounts receivable

Accounts receivable are primarily the result of milk being shipped. Receivables are reported at net realizable value, the amount management expects to collect from outstanding balances. Management believes the risk of loss on these receivables is very small and, accordingly, no allowance for doubtful accounts has been included. Should management determine there is a risk of non-collection in the future, an estimated allowance for doubtful accounts will be recorded. Receivables will be written off against the allowance as management determines they are uncollectible.

Inventories

Inventories are stated at the lower of cost or net realizable value and based on estimated quantities. Cost is determined by using the average cost and the first-in, first-out method.

The investment in growing crops at December 31, 2018 represents the estimated costs of fertilizer, seed, labor, utilities and various other farming costs which have been incurred and are expected to produce future crops.

SAMPLE DAIRY

NOTES TO THE FINANCIAL STATEMENTS

Dairy herd

Purchased cows are stated at cost. Self-raised dairy animals are stated at a value which is based upon the estimated cost to raise them to their respective ages.

Expenses reported within the income statement include those of raising heifers to their maturity. Raising expenses include feed, labor, veterinary, interest, death loss and various overhead costs. For presentation on the income statement, an estimated portion is allocated to reduce feed expense and other operating expenses.

Accumulated estimated costs are capitalized until the animal reaches maturity and is transferred into the milking herd. This cost is then depreciated over the useful life of the animal and deducted against dairy operations. Any remaining costs are written off when the animal is sold or dies. Dairy cows are retired on a first-in, first-out method. Depreciation is computed primarily on the straight-line method over an estimated useful life of 2-5 years.

Dairy farm and equipment

Land, buildings and improvements, equipment, autos and trucks are stated at cost. Depreciation is computed primarily on the straight-line method over an estimated useful life of 15-39 years for buildings and improvements, 7-10 years for equipment and 5 years for autos and trucks.

Repairs and maintenance are charged to expense in the period incurred. Major improvements and new assets are capitalized and depreciated.

Carrying value of dairy herd, dairy farm and equipment

The Company reviews the carrying value of the dairy herd, dairy farm and equipment for impairment whenever events and circumstances indicate that the carrying value of an asset may not be recoverable from the estimated future cash flows expected to result from its use and eventual disposition. In cases where undiscounted expected future cash flows are less than the carrying value, an impairment loss is recognized equal to an amount by which the carrying value exceeds the fair value of assets. The factors considered by management in performing this assessment include current operating results, trends and prospects, the manner in which the property is used, and the effects of obsolescence, demand, competition, and other economic factors. Based on this assessment there was no impairment at December 31, 2018.

Cooperative retains

In accordance with U.S. generally accepted accounting principles, investments in agricultural cooperatives are accounted for at cost.

Fair value of financial instruments

Carrying values of financial instruments, other than the cooperative retains also described in Note 1, including cash and cash equivalents, receivables, accounts payable, accrued expenses, current maturities of long-term obligations and long-term debt, approximate fair value. Estimated fair value amounts have been determined by the Company using available market information and appropriate valuation methodologies. Considerable judgment is necessarily required in interpreting market data to develop the estimates of fair value, and, accordingly, the estimates are not necessarily indicative of the amounts that the Company could realize in a current market exchange.

Revenue recognition

The Company recognizes revenue when milk is shipped to Dairymans Cooperative Inc.. Payment is made twice monthly, approximately one month after production. All milk received by Dairymans Cooperative Inc. is reconciled at month end and revenue and accounts receivable are recorded for any unpaid amounts.

Shipping and handling costs

The Company records milk income at gross amount and records the related hauling charges deducted by Dairymans Cooperative Inc. as a component of operating expenses.

SAMPLE DAIRY

NOTES TO THE FINANCIAL STATEMENTS

Use of estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

2. Concentrations

The Company shipped milk to one customer during the year ended December 31, 2018. Accounts receivable and sales to this customer as of December 31, 2018 were \$463,173 and \$10,439,484, respectively.

The Company maintains its cash in bank deposit accounts, which at times may exceed the \$250,000 federally insured limit. The Company has not experienced any losses in such accounts.

Management believes there is minimal risk associated with these concentrations.

3. Major customer

A substantial part of the Company's business is done with one entity, Dairymans Cooperative Inc.. The following is a schedule of income received from Dairymans Cooperative Inc. for the year ended December 31, 2018:

	AMOUNT	PER CWT
Base income	\$ 9,303,637	\$ 14.07
Quality bonus	174,051	0.27
Volume premium	306,756	0.48
Grade A bonus	417,136	0.65
Extra butterfat	237,904	0.37
	<hr/>	<hr/>
Gross milk income	10,439,484	15.85
Hauling charges	(9,251)	(0.01)
Industry assessments	(116,013)	(0.18)
	<hr/>	<hr/>
Net milk income	\$ <u>10,314,220</u>	\$ <u>15.65</u>

SAMPLE DAIRY

NOTES TO THE FINANCIAL STATEMENTS

4. Notes and loans payable

The Company is subject to restrictive covenants as part of their loan agreements. As of December 31, 2018, management is not aware of any violations of these covenants.

The notes payable to Farmers Bank are cross-collateralized and classified based on their primary security.

Operating line of credit

Sample Dairy has a revolving line of credit with Farmers Bank for the financing of its feed inventories and dairy herd. This line has an available limit of \$2,750,000 and an outstanding balance of \$2,414,350 as of December 31, 2018. This loan matures on September 1, 2019 and has a variable rate of interest which is calculated as 2.25% over the 30-day LIBOR rate.

The following are the estimated annual maturities for the consolidated long-term debt for each of the next five years ending December 31:

2019	\$	286,000
2020		245,000
2021		596,000
2022		245,000
2023		239,000
Thereafter		<u>1,293,848</u>
Total	\$	<u>2,904,848</u>

Total interest cost for the year ended December 31, 2018 was \$206,765, all of which was charged as expense against dairy operations.

5. Related party transactions

Bob Smith a member of the immediate family of the owners of Sample Dairy. Bob Smith sells supplies to the company. Sales from Bob Smith to the Company for the year ended December 31, 2018 were \$52,681.

Management considers the full value of the related party receivables to be collectible.

6. Lease obligations

The Company also leases farm ground on an annual basis for which the current annual cost is \$66,000.

Total rent expense for the year ended December 31, 2018 was \$66,000.

7. Supplemental disclosure of cash flow information

Cash paid during the year ended December 31, 2018 for interest is \$203,885. The Company paid no income tax since it is not a tax paying entity for federal and state income tax purposes.

SAMPLE DAIRY

SCHEDULE 1

**SCHEDULE OF FARMING
FOR THE YEAR ENDED DECEMBER 31, 2018**

FARMING INCOME:

*Transfer of crops grown to inventory at estimated
fair market value:*

Corn silage	-	14,024 tons		\$ 476,820
Hay	-	732 tons		<u>57,840</u>
Total farming income				534,660

FARMING EXPENSES:

Investment in growing crops, December 31, 2017		\$ 52,984		
Custom hire		190,969		
Rent		66,000		
Repairs and maintenance		60,790		
Seed		82,348		
Manure management		52,678		
Fertilizer and chemicals		35,575		
Depreciation		31,637		
Fuel and oil		12,571		
Investment in growing crops, December 31, 2018		<u>(38,723)</u>		
Total farming expenses				<u>546,829</u>
Net loss from farming				<u><u>\$ (12,169)</u></u>

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See independent accountants' Review report.