

Accounting for Hedging Transactions

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Paul Neiffer Bio

- Paul is an Agribusiness CPA and Principal with CliftonLarsonAllen LLP located in the Kennewick and Yakima, Washington offices. Paul writes a monthly column for Top Producer magazine called the “Farm CPA” and is the primary writer and editor for the nationally recognized farm blog “Farm CPA Today” (www.farmcpatoday.com).
- Paul gives numerous talks on various tax, accounting and succession planning topics to farmers, CPAs, attorneys, bankers and others each year. Paul currently serves as the treasurer for the Farm Financial Standards Council.
- Paul grew up on a wheat farm in Southeastern Washington State and still enjoys going home each summer to help operate the combine in wheat harvest. This is his idea of a vacation.
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Agenda

- **Background on the FFSC**
- **What is Hedging**
- **Accounting for Hedging**
 - Financial Treatment
 - Tax Treatment
- **Detailed Examples**



Farm Financial Standards Council Background

About the Farm Financial Standards Council (FFSC)

- **Comprised of producers, ag lenders (banks and farm credit), farm managers, accountants, consultants, academicians**
- **Two sets of guidelines**
 - **Financial Guidelines**
 - **Management Accounting Guidelines**

FFSC Mission

To provide education and a national forum to facilitate the development, review, communication and promotion of uniformity and integrity in both financial reporting and the analytical techniques useful for effective and realistic measurement of the financial position and the financial performance of agricultural producers.

FFSC Vision

To be recognized as the definitive resource of financial guidelines to benefit agricultural producers.

FFSC Goals

- **To establish recommended standards for format and content of financial reports of agricultural producers;**
- **To identify certain financial measures (usually ratios) common to all areas of the country and all sectors of agriculture and establish standardized methods of calculating those measures; and**
- **~~To encourage the development of an agricultural financial database.~~ In the process of being rewritten to address benchmarking.**

History of the FFSC

- **“Financial Guidelines for Agriculture Producers” Report**
 - Initial meeting January 22, 1989
 - Exposure draft released May 1990
 - Original report issued May 1991
 - Cash to accrual appendix issued in November 1993
 - Revised report issued in July 1995
 - Expanded report with “Disclosure by Notes” and glossary, December 1997
 - Revised report issued January 2008
 - Revised report issued April 2011
 - Revised report issued Jan 2014 (accounting for hedges)

History of the FFSC, cont.

- **“Management Accounting Guidelines for Agriculture Producers” Report**
 - November 1997, FFSC endorsed a recommendation to develop of uniform chart of accounts and management accounting guidelines
 - Began formal effort in summer 2000
 - Exposure draft issued December 2005
 - Final report approved December 2006
 - Final report issued January 2008

Key Recommendations: Departures from GAAP

- **Both Cost and Market Required, Either Can Be Primary Format**
 - **With Market Value as Primary B/S Format, Owner Equity Section Must Delineate at least Retained Capital and Valuation/Personal Asset Equity**
- **Inventory Valuation—Market Values Acceptable for Market Livestock**
- **Raised Breeding Livestock—Base Value Method Acceptable**
- **Capital Leases—Estimation Approach Acceptable**

Key Recommendations: Departures from Common Lender Practice

- **Cost and Market of Capital Assets**
- **Balance Sheet Format—Two Category**
- **Income Statement Format**
- **Separation of Personal Assets and Liabilities**
- **Treatment of Withdrawals and Non-Farm Income on the SCF and Income Statement**
- **Incorporation of Deferred Taxes and Capital Leases**
- **Depreciation—Book, Not % of Market or Tax**

Two Common Misconceptions About the FFSC Recommendations

1. GAAP Compliance

- **Myth: ...meant as a substitute for or replacement of GAAP**
- **Fact: ...based on the Conceptual Framework documents, and are largely consistent w/GAAP. Accountant opinions based on FFSC Recommendations are and will continue to be qualified.**

2. Credit Analysis

- **Myth: ...are meant as credit analysis recommendations**
- **Fact: Development of an effective credit process requires evaluation of numerous factors beyond the scope of the FFSC Recommendations.**



Hedging

What is Hedging?



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- It is a risk management strategy that provides price protection.
- Attempts to offset price movements of owned assets, planned production of a commodity or good, or planned purchases of commodity or good against a derivative instrument (which generally derives its value from an underlying physical commodity).
- It is not an attempt to make money.

What is Not Hedging?



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- **Speculation**

- Taking a futures or options position in a commodity not owned or produced.
- Taking the same position in the futures or options market as exists (or will exist) on the farm or ranch.

- **Forward contracts**

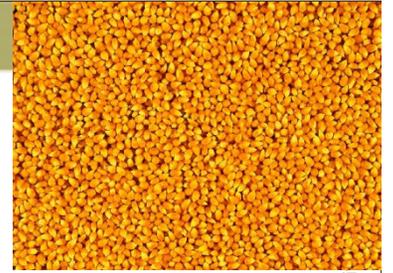
- Fixed price, delayed or deferred price contracts, basis contracts, installment sale contracts, etc.

Hedging Treatment and Types

- **Financial Statement treatment**
 - **Income Statement -- depends on the hedging type. May be included in net income or may be excluded from net income.**
 - **Balance Sheet -- No difference in presentation between the two methods.**
- **Three types of hedges**
 - **Fair value**
 - **Cash flow**
 - **Net investment hedge/Foreign currency transactions**

Fair Value Hedges

- **Used to protect the exposure to market value changes of an asset.**
- **Generally refers to stored inventory listed on balance sheet at market value (e.g., harvested crops valued at a readily determinable market value).**



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Cash Flow Hedges



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- **Used to reduce the risk of price fluctuations of forecasted transactions.**
- **Generally refers to items growing, being raised, unfinished, or yet to be produced, or purchased (e.g., growing crops, future crops, livestock that is being raised or will be raised, or feed to purchase).**

Terminology

- **Mark(ed)-to-market**
- **Derivative**
- **Realized gains or losses**
- **Recognized gains or losses**
- **Unrealized gains or losses**
- **Hedging effectiveness**
- **Other comprehensive income (OCI)**
- **Accumulated other comprehensive income (AOCI)**



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Financial Treatment



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FFSC Recommendations



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- **GAAP**
 - Recommended approach
 - Separate hedging gains and losses between earned (in the body of the Income Statement) and unearned (at the end of the Income Statement or on a separate “Statement of Comprehensive Income”).
- **Alternative**
 - Simplified method may be used
 - Ignore distinction between earned and unearned and include all hedging gains and losses in earnings.

Fair Value Hedge Approach

- **When underlying asset being hedged is available for sale or is valued on the balance sheet at its fair (or market) value.**
- **Marked-to-market gains or losses as of the date of financial statement are recognized with respect to net income and reported on the I/S as hedging gains or losses.**
 - **If the hedged item is normally sold in the course of business, the reported G/L is shown in the revenue section of the I/S.**
 - **If the hedged item is normally purchased in the course of business then the reported G/L is shown in the expense section of the I/S.**
 - ◇ **Generally hedged purchases are cash flow hedges, but if the purchased items, for instance feed, is valued at market, then the unrealized hedging gain or loss should be included with expenses and therefore will be included in net income.**

Cash Flow Hedge Approach

- The gain or loss associated with this type of hedge is not included in net income, but is included in “Other comprehensive income” and reported after net income.
- May be on the Income Statement or in a separate statement, “Statement of Comprehensive Income.”
- Gains and losses are accumulated in the equity section of the balance sheet in an account titled accumulated other comprehensive income.
 - Accordingly, all these unrealized gains and losses are considered unrecognized with respect to net income (i.e., they are not included in net income).
 - As these unrealized gains and losses are offset, previous accumulated gains or losses are removed from other comprehensive income and are reclassified in net income, which has the impact of moving the gain or loss in the equity section of the balance sheet from accumulated other comprehensive income to retaining earnings.

Fair Value Hedge – Futures Example

- **As of 1/3/13**
 - Assume producer has 100,000 bu of unpriced corn inventory on hand.
 - The forward price for May delivery is \$6.75/bu.
 - Producer sells (or goes short) 100,000 bu (or 20 contracts) of Jul '13 corn futures at \$6.85/bu.
- **On 5/2/13**
 - Producer sells 100,000 bu of corn inventory to local elevator for \$6.50/bu.
 - Producer buys (or goes long) 100,000 bu (or 20 contracts) of Jul '13 corn futures at \$6.60/bu.
- **Result**
 - Producer receives cash \$650,000 from elevator for corn.
 - The gain in the futures market is \$0.25/bu (\$6.85 - \$6.60) or \$25,000.
 - The net price received by the farmer is \$675,000.
- **At the end of each month, the futures position is marked-to-market and resulting gain or loss in the futures market is recognized in revenue as an offset to the fluctuating corn inventory valuation.**

Assumes constant basis, no commissions, no fees, and no interest on futures margin account.

Fair Value Hedge – Options Example

- **As of 1/3/13**
 - Assume producer has 100,000 bu of unpriced corn inventory on hand.
 - The forward price for May delivery is \$6.80/bu.
 - Producer buys (or goes long) 100,000 bu (or 20 contracts) of Jul '13 corn options with an out-of-the-money strike price of \$6.50/bu for \$0.35/bu, or \$35,000.
- **On 5/2/13**
 - Producer sells 100,000 bu of corn inventory to local elevator for \$6.50/bu.
 - Producer sells (or goes short) 100,000 bu (or 20 contracts) of the Jul '13 corn option for \$0.20/bu, or \$20,000.
- **Result**
 - Producer receives cash \$650,000 from elevator for corn.
 - The loss from the options premium is \$-0.11/bu ($\$0.20 - \0.35) or -\$15,000.
 - The net price received by the farmer is \$635,000.
- **At the end of each month, the options position is marked-to-market and resulting gain or loss in the options market is recognized in revenue as an offset to the fluctuating corn inventory valuation.**

Assumes constant basis, no commissions, no fees, and no interest on futures margin account.

Cash Flow Hedge – Futures Example

- **As of 1/3/12**
 - Assume producer wants to protect 100,000 bu of unplanted corn.
 - The forward price for Dec delivery is \$5.90/bu.
 - Producer sells (or goes short) 100,000 bu (or 20 contracts) of Dec '12 corn futures at \$5.90/bu.
- **On 11/23/12**
 - Producer sells 100,000 bu of corn to local elevator for \$7.40/bu.
 - Producer buys (or goes long) 100,000 bu (or 20 contracts) of Dec '12 corn futures at \$7.40/bu.
- **Result**
 - Producer receives cash \$740,000 from elevator for corn.
 - The loss in the futures market is -\$1.50/bu ($\$5.90 - \7.40) or -\$150,000.
 - The net price received by the farmer is \$590,000.
- **At the end of each month, the futures position is marked-to-market and resulting gain or loss in the futures market is recognized in other comprehensive income, until the crop is harvested and placed in inventory (at market value) at which point the unrealized gains and losses are used to offset to the fluctuating corn inventory valuation.**

Assumes constant basis, no commissions, no fees, and no interest on futures margin account.

Cash Flow Hedge – Options Example

- **As of 1/3/12**
 - Assume producer wants to protect 100,000 bu of unplanted corn.
 - The forward price for Dec delivery is \$5.90/bu.
 - Producer buys (or goes long) 100,000 bu (or 20 contracts) of Dec '12 corn options with an at-the-money strike price of \$6.00/bu for \$0.70/bu, or \$70,000.
- **On 11/23/12**
 - Producer sells 100,000 bu of corn inventory to local elevator for \$7.40/bu.
 - Producer allows the option to expire worthless.
- **Result**
 - Producer receives cash \$740,000 from elevator for corn.
 - The loss from the options premium is \$-0.70/bu (\$0.70 - \$0.00) or -\$70,000.
 - The net price received by the farmer is \$670,000.
- **At the end of each month, the options position is marked-to-market and resulting gain or loss in the options market is recognized in other comprehensive income until the crop is harvested and placed in inventory (at market value) at which point the unrealized gains and losses are used to offset to the fluctuating corn inventory valuation.**



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Alternative Approach

- **The simplified method of accounting for hedges treats all hedges as fair value, thus all hedging gains and losses are marked-to-market and recognized on the Income Statement.**
- **There is no distinction between hedges of commodities on hand (fair value) vs. planned or in-process production (cash flow) with this approach.**

Summary

- **Gain and losses from hedging transactions may be significant items for an agricultural producer. Proper treatment and presentation in the financial statements are important to be sure earnings are measured accurately.**
- **The recommended approach is to:**
 - **Treat hedging transactions as fair value hedges when inventories are valued at market (stored grain or livestock available for sale). This treatment has the impact of showing in net income the gain and losses from hedging transactions.**
 - **Treat hedging transactions as cash flow hedges when inventories are value at cost (growing crops or livestock) or production is planned (has not begun). This treatment has the impact of showing in other comprehensive income the gain and losses from hedging transactions, and keeping these amounts out of net income.**



Tax Treatment



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Income Tax Treatment



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- **May be different from GAAP**
- **An agricultural producer normally reports hedging gains or losses when the hedge is closed.**
- **However, if the producer meets certain requirements, they can elect to report all hedging gains and losses on a mark-to-market basis (i.e. usually pick up the 1099 reported net gain or loss) [Reg. 1.446-4(e)(1)(ii)].**
 - **This simplified method allows producers to simply report the gains and losses from the Broker's statement form 1099B.**
 - **Care must be taken in reviewing form 1099B from brokerage companies if options are used since many brokers will show a purchase of an option as a realized loss and any outstanding option value at year-end as unrealized gain.**
 - **This may result in reported gains or losses that are materially different from actual gains or losses.**

Example

- **Farmer Duroc grows pigs and opens an hedging account. On December 31, 20xx, he purchases 15 June 20xx hog put options at a cost of \$35,000.**

When he receives the 1099-B from the brokerage company, he notices that there is a realized loss of \$35,000 and unrealized gain of \$35,000 with a net profit of zero.

Although the 1099-B shows a realized loss of \$35,000, no loss has been incurred and no hedging gain or loss should be shown for the year.

Tax Treatment



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- **Hedging transactions**

- Treated as ordinary income or expense and reported on schedule F.
- Detailed rules and documentation requirements must be met to qualify a futures transaction as a hedge.
- Generally, for cash-basis tax payers, only the gains or losses from closed hedging transactions are recognized in taxable income, and this is almost always different from the amount of gains or losses recognized from an accounting perspective.
- IRS guidelines suggest showing all gains and losses in Schedule F “Other income.”

Identification and Recordkeeping

- **Taxpayer who enters into a hedge, must clearly identify it as a hedging transaction before the close of the day of the transaction**
 - A separate hedging account is one method
 - Making notations or other identifying marks within the books and records, such as notations on trading tickets, purchase orders or confirmations
- **Additionally, the taxpayer must identify the item or risk being hedged in a substantial contemporaneous manner. This must happen within 35 days of entering into the hedge transaction**

Example

- **Art, a hog feeder, anticipates a large purchase of soybean meal to be used as hog feed in November. Currently in June, however, he is concerned about a possible price increase in the soybean meal market. Accordingly, he enters into a current long position in soybean meal futures to lock in the current low price, with the intent of removing the futures contract in November when he will actually purchase the soybean meal.**

On the day of entering into the futures transaction in June, Art must identify this in his records as a hedge, and within 35 days he must identify in his records that the soybean meals futures contract is a hedge against the price risk of the soybean meal to be purchased in November.

Hedging Must Be Performed by Proper Entity

- **Another entity, even if under identical ownership (other than consolidated group) cannot hedge a commodity for the other entity.**
 - Taxpayer was one of three C corporations with a common shareholder, but not part of a consolidated group. The transaction was a capital loss and not a hedging transaction. Taxpayer was ruled to be separate and distinct from its shareholders even though a shareholder maintained one account for all three corporation's hedging transactions [*Pine Creek Farms, Ltd v. Comm. TC Memo 2001-176*].
 - An individual who was an employee and significant shareholder of an S corporation which was engaged in the dairy business couldn't attribute that business to himself for purposes of treating his own purchases and sales of grain contract (at a net loss) as hedging [PLR 199720003].
 - A C corporation could not deduct ordinary losses on the sale of hog futures as hedging transactions, because it was not engaged in hog production. Even though the corporation sold corn and soybeans to other corporations with common ownership who did produce hogs, these activities could not be imputed to the taxpayer [*Pine Creek Farms, Ltd v. Comm. TC Memo 2001-176*].

Additional Criteria

- **The futures or options contract must be in commodities which are purchased or raised by the farmer, and be within the range of production**
 - Raise a 100,000 bushels of corn, can't hedge a million bushels
- **The futures or options contract must be opposite the farmer's physical position in farm commodities on hand or to be acquired, so as to constitute a price hedge**
 - Can't sell the crop and "buy the board"
 - If farmer grows a crop or raises livestock, the purchase of a put or going short futures will qualify as a hedge
 - If the farmer raises livestock and needs to purchase grain, the purchase of a call or going long futures will qualify as a hedge
- **A farmer can enter into additional hedging transactions to counteract all or any part of the risk from a previous hedging transaction [Reg. 1.1221-2(d)(3)].**

Other Provisions

- A farmer may hedge all or any portion of a risk for all or any part of the period during which it is exposed to the risk including crops that may not yet be planted for multiple years [Reg. 1.1221-2(d)(7)(i)]
- The regulations acknowledge that the frequency of a taxpayer's entering into and terminating positions is not relevant to whether these transactions are in hedging status, noting that a taxpayer hedging the risk associated with an asset or liability might frequently establish and terminate positions that hedge that risk, depending on the extent to which the taxpayer wished to be hedged [Reg. 1.1221-2(d)(7)(ii)].
- A hedge gain or loss should only be reported which the hedge crop is actually purchased or sold.
 - Example – Farmer Bean enters into a hedge of 10,000 bushels of soybeans on November 1, 20XX. He closes the hedge out on December 28, 20XX for a loss of \$25,000. He sells the soybeans on January 12, 20XX+1. He should not recognize the \$25,000 loss until January 12, 20XX+1.

Speculative Transactions



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- **Tax Treatment**

- Any futures or option transaction not treated as hedging will be considered speculative [Reg. 1.1221-2(g)(2); Sec. 1256(e)(1)].
- Reporting of speculative transactions
 - ◇ Speculative contracts are reported under a “marked-to-market” approach, which treats the contract as sold on the last day of the tax year [Sec. 1256(a)(1)].
 - ◇ Speculative contracts are reported on form 6781, *Gains or Losses from Section 1256 Contracts and Straddles*. The capital gain or loss is treated, by statute, as 40% short-term and 60% long-term.

Speculative Transactions - Continued

- **Net Sec. 1256 speculation losses can be carried back three years to offset any net Sec. 1256 gains in those years [Sec. 1212(c)(1)]. This election is not available to corporations, trusts or estates.**
- **Since C corporations do not have favorable capital gains or loss treatment and to ensure the availability of Sec. 1256 loss carry backs, care must be taken to make sure that all speculative transactions are done personally or in a pass-through entity.**

Pitfalls

- If the transaction was originally identified as hedge and is actually speculative, gain is ordinary and loss is capital [Reg. 1.1221-2(g)(1)(i)]
- If the transaction was inadvertently identified as hedge and is actually speculative, gain or loss is capital [Reg. 1.1221-2(g)(1)(ii)]
- If the transaction was not identified as a hedge, gain or loss is capital, even if it would otherwise be a hedge [Reg. 1.1221-2(g)(d)]
- If the taxpayer purposely does not make an identification (i.e. wants capital gains treatment), the gain is ordinary [Reg. 1.1221-2(g)(iii)]



Recommended Approaches

Fair Value Hedges (Finished Goods Inventory)

| Event | Tax Treatment | Other Comprehensive Income | Net Income |
|---------------------------------|------------------|----------------------------|---------------------------|
| Open Positions Marked-To-Market | N/A ¹ | N/A ² | Unrealized but Recognized |
| Closed Positions | Realized | N/A ² | Realized and Recognized |

¹Unless elected by taxpayer to recognize gains and losses on a marked-to-market basis. For tax purposes there is no distinction between fair value and cash flow hedges.

²Technically, fair value hedges are reflected in both net income and comprehensive income.

Cash Flow Hedges (Work in Process Inventory and Planned Production)

| Event | Tax Treatment | Other Comprehensive Income | Net Income |
|---------------------------------|------------------|--|--|
| Open Positions Marked-To-Market | N/A ¹ | Unrealized but Recognized ² | Unrealized and Unrecognized ³ |
| Closed Positions | Realized | Realized and Recognized ² | Realized but Unrecognized ³ |

¹Unless elected by taxpayer to recognize gains and losses on a marked-to-market basis. For tax purposes there is no distinction between fair value and cash flow hedges.

²Effective portion of hedge may remain in other comprehensive income.

³Ineffective portion of hedge should be reported in net income, the effective portion is unrecognized with respect to net income unless entity has elected to recognize hedging gains and losses in net income.

Alternative Approach¹ All Hedges

| Event | Tax Treatment | Net Income |
|------------------------------------|------------------|------------------------------|
| Open Positions Marked-To-Market | N/A ² | Unrealized but Recognized |
| Closed Positions | Realized | Realized and Recognized |

¹The impact on net income with the alternative approach is the same as the fair value approach, however, note that the concept of other comprehensive income does not exist using the alternative approach.

²Unless elected by taxpayer to recognize gains and losses on a marked-to-market basis.

Hedging Examples

- Crop operation produces corn and uses the futures market to hedge the price of corn.
- Hog operation produces lean hogs (and buys weaned pigs and feed) and uses the futures and options market to hedge the price of lean hogs and purchased price of corn.



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Detailed Crop Example

- **Included in Appendix H (Hedging Transactions) of the FFSC's Financial Guidelines for Agriculture**
- **Corn production operation**

Q1 Hedge Statement, 3/31/X2

Your activity this period:

| <u>Date</u> | <u>Long bushels</u> | <u>Short bushels</u> | <u>Contract Description</u> | <u>Price</u> | <u>Debit</u> | <u>Credit</u> | <u>Amount</u> |
|-------------|---------------------|----------------------|-----------------------------|--------------|--------------|---------------|---------------|
| 1/1/X2 | | | Wire receipt (Margin call) | | | \$ 45,000.00 | \$ 45,000.00 |
| 1/1/X2 | | 100,000 | Jul 'X2 CBOT corn | \$ 5.80 | | | \$ 45,000.00 |
| 2/1/X2 | | | Wire receipt (Margin call) | | | \$ 10,000.00 | \$ 55,000.00 |
| 2/15/X2 | | | Wire receipt (Margin call) | | | \$ 10,000.00 | \$ 65,000.00 |
| 3/1/X2 | | | Wire receipt (Margin call) | | | \$ 10,000.00 | \$ 75,000.00 |
| 3/12/X2 | | | Wire receipt (Margin call) | | | \$ 10,000.00 | \$ 85,000.00 |

Positions in your account:

| <u>Date</u> | <u>Long bushels</u> | <u>Short bushels</u> | <u>Contract Description</u> | <u>Price</u> | <u>Debit</u> | <u>Credit</u> | <u>Amount</u> |
|-------------|---------------------|----------------------|-----------------------------|--------------|--------------|---------------|----------------|
| 1/1/X2 | | 100,000 | Jul 'X2 CBOT corn | \$ 5.80 | \$ 20,000.00 | | \$ (20,000.00) |
| | | | Close | \$ 6.00 | | | |

Period Recap

| | | | |
|---------------------------|----------|----|-------------------------|
| Beginning balance | 12/31/X1 | \$ | - |
| This periods activity | | \$ | <u>85,000.00</u> |
| Ending Balance | 3/31/X2 | \$ | 85,000.00 |
| Futures open trade equity | | \$ | <u>(20,000.00)</u> |
| Account value at Market | 3/31/X2 | \$ | <u><u>65,000.00</u></u> |

Q1 Balance Sheet, as of 3/31/X2

| Assets | | | |
|---------------------------------------|--------------|-------------------|----------------------------|
| Current assets: | | | |
| Cash | | | \$ 40,000 |
| | Cash | Market adjustment | |
| Hedge account, see Note 1 | 85,000 | (20,000) | 65,000 |
| | Quantity, bu | Price, \$/bu | |
| Grain inventory | 200,000 | \$ 5.80 | 1,160,000 |
| Investment in growing crops | | | - |
| Total current assets | | | <u>1,265,000</u> |
| Fixed assets | | | <u>3,000,000</u> |
| Total assets | | | <u><u>\$ 4,265,000</u></u> |
| Liabilities & Equity | | | |
| Current liabilities: | | | |
| Accounts payable | | | \$ 40,000 |
| Short-term debt | | | <u>200,000</u> |
| Total current liabilities | | | <u>240,000</u> |
| Long-term debt | | | <u>500,000</u> |
| Total liabilities | | | <u>740,000</u> |
| Total equity | | | <u>3,525,000</u> |
| Total liabilities & equity | | | <u><u>\$ 4,265,000</u></u> |

Q1 Income Statement, 3/31/X2

| Income: | <u>Quarter ended</u> | <u>Year-to-date</u> |
|---|----------------------|---------------------|
| Income from grain: | | |
| Cash sale of grain | - | \$ - |
| Beginning inventory | (1,120,000) | (1,120,000) |
| Ending inventory | 1,160,000 | 1,160,000 |
| Hedge gain (loss), see Note 2 | <u>(20,000)</u> | <u>(20,000)</u> |
| Total income from grain | <u>20,000</u> | <u>20,000</u> |
| Expenses: | | |
| Input cost | - | - |
| Interest | - | - |
| Depreciation | - | - |
| General and administrative (G&A) | 5,000 | 5,000 |
| Hedge gain (loss) | - | - |
| Accrual adjustments (investment in growing crops) | <u>-</u> | <u>-</u> |
| Total expenses | <u>5,000</u> | <u>5,000</u> |
| Net income (loss) | <u>15,000</u> | <u>15,000</u> |
| Other comprehensive income (loss):* | | |
| Unrealized cash flow hedge gain (loss) | - | - |
| Realized fair value hedge loss (gain) | <u>-</u> | <u>-</u> |
| Total other comprehensive income (loss) | <u>-</u> | <u>-</u> |
| Total comprehensive income (loss) | <u>\$ 15,000</u> | <u>\$ 15,000</u> |

Q2 Hedge Statement, 6/30/X2

Your activity this period:

| <u>Date</u> | <u>Long bushels</u> | <u>Short bushels</u> | <u>Contract Description</u> | <u>Price</u> | <u>Debit</u> | <u>Credit</u> | <u>Amount</u> |
|-------------|---------------------|----------------------|-----------------------------|--------------|--------------|---------------|---------------|
| 4/1/X2 | | | Wire receipt (Margin call) | | | \$ 5,000.00 | \$ 90,000.00 |
| 4/30/X2 | | | Wire receipt (Margin call) | | | \$ 5,000.00 | \$ 95,000.00 |
| 5/15/X2 | | | Wire receipt (Margin call) | | | \$ 5,000.00 | \$ 100,000.00 |
| 5/31/X2 | | | Wire receipt (Margin call) | | | \$ 15,000.00 | \$ 115,000.00 |
| 6/10/X2 | 100,000 | | Jul 'X2 CBOT corn | \$ 6.20 | \$ 40,000.00 | | \$ 75,000.00 |
| 6/15/X2 | | | Wire disbursement | | \$ 30,000.00 | | \$ 45,000.00 |

Positions in your account:

| <u>Date</u> | <u>Long bushels</u> | <u>Short bushels</u> | <u>Contract Description</u> | <u>Price</u> | <u>Debit</u> | <u>Credit</u> | <u>Amount</u> |
|-------------|---------------------|----------------------|-----------------------------|--------------|--------------|---------------|---------------|
| | | | | | | | \$ - |

Period Recap

| | | |
|---------------------------|---------|---------------------|
| Beginning balance | 3/31/X2 | \$ 85,000.00 |
| This periods activity | | \$ (40,000.00) |
| Ending Balance | 6/30/X2 | \$ 45,000.00 |
| Futures open trade equity | | \$ - |
| Account value at Market | 6/30/X2 | \$ <u>45,000.00</u> |

Q2 Balance Sheet, as of 6/30/X2

| Assets | | | |
|---------------------------------------|--------------|-------------------|---------------------|
| Current assets: | | | |
| Cash | | | \$ 955,000 |
| | Cash | Market adjustment | |
| Hedge account, see Note 1 | 45,000 | - | 45,000 |
| | Quantity, bu | Price, \$/bu | |
| Grain inventory, see Note 2 | - | \$ - | - |
| Investment in growing crops | | | 300,000 |
| Total current assets | | | 1,300,000 |
| Fixed assets | | | 3,000,000 |
| Total assets | | | \$ 4,300,000 |
| Liabilities & Equity | | | |
| Current liabilities: | | | |
| Accounts payable | | | \$ 40,000 |
| Short-term debt | | | 200,000 |
| Total current liabilities | | | 240,000 |
| Long-term debt | | | 500,000 |
| Total liabilities | | | 740,000 |
| Total equity | | | 3,560,000 |
| Total liabilities & equity | | | \$ 4,300,000 |

Q2 Income Statement, 6/30/X2

| Income: | <u>Quarter ended</u> | <u>Year-to-date</u> |
|---|----------------------|---------------------|
| Income from grain: | | |
| Cash sale of grain | \$ 1,240,000 | 1,240,000 |
| Beginning inventory | (1,160,000) | (1,120,000) |
| Ending inventory | - | - |
| Hedge gain (loss), see Note 3 | <u>(20,000)</u> | <u>(40,000)</u> |
| Total income from grain | <u>60,000</u> | <u>80,000</u> |
| Expenses: | | |
| Input cost | 300,000 | 300,000 |
| Interest | - | - |
| Depreciation | - | - |
| General and administrative (G&A) | 5,000 | 10,000 |
| Hedge gain (loss) | - | - |
| Accrual adjustments (investment in growing crops) | <u>(300,000)</u> | <u>(300,000)</u> |
| Total expenses | <u>5,000</u> | <u>10,000</u> |
| Net income (loss) | 55,000 | 70,000 |
| Other comprehensive income (loss): | | |
| Unrealized cash flow hedge gain (loss) | - | - |
| Realized fair value hedge loss (gain) | - | - |
| Total other comprehensive income (loss) | <u>-</u> | <u>-</u> |
| Total comprehensive income (loss) | <u>\$ 55,000</u> | <u>\$ 70,000</u> |

Q3 Hedge Statement, 9/30/X2

Your activity this period:

| <u>Date</u> | <u>Long bushels</u> | <u>Short bushels</u> | <u>Contract Description</u> | <u>Price</u> | <u>Debit</u> | <u>Credit</u> | <u>Amount</u> |
|-------------|---------------------|----------------------|-----------------------------|--------------|--------------|---------------|---------------|
| 7/1/X2 | | 80,000 | Dec 'X2 CBOT corn | \$ 6.00 | | | \$ 45,000.00 |
| 7/30/X2 | | | Wire receipt (Margin call) | | | 30,000.00 | \$ 75,000.00 |
| 8/31/X2 | | | Wire receipt (Margin call) | | | 25,000.00 | \$ 100,000.00 |

Positions in your account:

| <u>Date</u> | <u>Long bushels</u> | <u>Short bushels</u> | <u>Contract Description</u> | <u>Price</u> | <u>Debit</u> | <u>Credit</u> | <u>Amount</u> |
|-------------|---------------------|----------------------|-----------------------------|--------------|--------------|---------------|----------------|
| 7/1/X2 | | 80,000 | Dec 'X2 CBOT corn | \$ 6.00 | \$ 48,000.00 | | \$ (48,000.00) |
| | | | Close | \$ 6.60 | | | |

Period Recap

| | | |
|---------------------------|---------|-----------------------|
| Beginning balance | 6/30/X2 | \$ 45,000.00 |
| This periods activity | | \$ <u>55,000.00</u> |
| Ending Balance | 9/30/X2 | \$ 100,000.00 |
| Futures open trade equity | | \$ <u>(48,000.00)</u> |
| Account value at Market | 9/30/X2 | \$ <u>52,000.00</u> |

Q3 Balance Sheet, as of 9/30/X2

| Assets | | | |
|---------------------------------------|---------------------|---------------------|----------------------------|
| Current assets: | | | |
| Cash | | | \$ 875,000 |
| | Cash | Market adjustment | |
| Hedge account, see Note 1 | 100,000 | (48,000) | 52,000 |
| | <u>Quantity, bu</u> | <u>Price, \$/bu</u> | |
| Grain inventory | - | \$ - | - |
| Investment in growing crops | | | <u>300,000</u> |
| Total current assets | | | <u>1,227,000</u> |
| Fixed assets | | | <u>3,000,000</u> |
| Total assets | | | <u><u>\$ 4,227,000</u></u> |
| Liabilities & Equity | | | |
| Current liabilities: | | | |
| Accounts payable | | | \$ 40,000 |
| Short-term debt | | | <u>200,000</u> |
| Total current liabilities | | | <u>240,000</u> |
| Long-term debt | | | <u>500,000</u> |
| Total liabilities | | | <u>740,000</u> |
| Total equity | | | <u>3,487,000</u> |
| Total liabilities & equity | | | <u><u>\$ 4,227,000</u></u> |

Q3 Income Statement, 9/30/X2

| Income: | <u>Quarter ended</u> | <u>Year-to-date</u> |
|--|----------------------|---------------------|
| Income from grain: | | |
| Cash sale of grain | | \$ 1,240,000 |
| Beginning inventory | - | (1,120,000) |
| Ending inventory | - | - |
| Hedge gain (loss), see Note 2 | - | (40,000) |
| Total income from grain | <u>-</u> | <u>80,000</u> |
| Expenses: | | |
| Input cost | - | 300,000 |
| Interest | - | - |
| Depreciation | - | - |
| General and administrative (G&A) | 5,000 | 15,000 |
| Hedge gain (loss) | - | - |
| Accrual adjustments (investment in growing crops) | - | (300,000) |
| Total expenses | <u>5,000</u> | <u>15,000</u> |
| Net income (loss) | <u>(5,000)</u> | <u>65,000</u> |
| Other comprehensive income (loss): | | |
| Unrealized cash flow hedge gain (loss), see Note 3 | (48,000) | (48,000) |
| Realized fair value hedge loss (gain) | - | - |
| Total other comprehensive income (loss) | <u>(48,000)</u> | <u>(48,000)</u> |
| Total comprehensive income (loss) | <u>\$ (53,000)</u> | <u>\$ 17,000</u> |

Q4 Hedge Statement, 12/31/X2

Your activity this period:

| <u>Date</u> | <u>Long bushels</u> | <u>Short bushels</u> | <u>Contract Description</u> | <u>Price</u> | <u>Debit</u> | <u>Credit</u> | <u>Amount</u> |
|-------------|---------------------|----------------------|-----------------------------|--------------|--------------|---------------|---------------|
| 10/31/X2 | 20,000 | | Dec 'X2 CBOT corn | \$ 6.60 | \$ 12,000.00 | | \$ 88,000.00 |
| 10/31/X2 | | | Wire receipt (Margin call) | | | 25,000.00 | \$ 113,000.00 |
| 11/15/X2 | | 50,000 | Dec 'X3 CBOT corn | \$ 5.80 | | | \$ 113,000.00 |
| 12/1/X2 | 60,000 | | Dec 'X2 CBOT corn | \$ 6.40 | \$ 24,000.00 | | \$ 89,000.00 |
| 12/1/X2 | | 60,000 | Mar 'X3 CBOT corn | \$ 6.75 | | | \$ 89,000.00 |
| 12/15/X2 | | | Wire receipt (Margin call) | | | 25,000.00 | \$ 114,000.00 |

Positions in your account:

| <u>Date</u> | <u>Long bushels</u> | <u>Short bushels</u> | <u>Contract Description</u> | <u>Price</u> | <u>Debit</u> | <u>Credit</u> | <u>Amount</u> |
|-------------|---------------------|----------------------|-----------------------------|--------------|--------------|---------------|----------------|
| 11/15/X2 | | 50,000 | Dec 'X3 CBOT corn | \$ 5.80 | \$ 50,000.00 | | \$ (50,000.00) |
| | | | Close | \$ 6.80 | | | |
| 12/1/X2 | | 60,000 | Mar 'X3 CBOT corn | \$ 6.75 | \$ 6,000.00 | | \$ (56,000.00) |
| | | | Close | \$ 6.85 | | | |

Period Recap

| | | |
|---------------------------|----------|----------------|
| Beginning balance | 9/30/X2 | \$ 100,000.00 |
| This periods activity | | \$ 14,000.00 |
| Ending Balance | 12/31/X2 | \$ 114,000.00 |
| Futures open trade equity | | \$ (56,000.00) |
| Account value at Market | 12/31/X2 | \$ 58,000.00 |

Q4 Balance Sheet, as of 12/31/X2

| Assets | | | |
|---------------------------------------|--------------|-------------------|----------------------------|
| Current assets: | | | |
| Cash | | | \$ 127,000 |
| | Cash | Market adjustment | |
| Hedge account, see Note 1 | 114,000 | (56,000) | 58,000 |
| | Quantity, bu | Price, \$/bu | |
| Grain inventory, see Note 2 | 180,000 | \$ 6.85 | 1,233,000 |
| Investment in growing crops | | | - |
| Total current assets | | | <u>1,418,000</u> |
| Fixed assets | | | <u>2,920,000</u> |
| Total assets | | | <u><u>\$ 4,338,000</u></u> |
| Liabilities & Equity | | | |
| Current liabilities: | | | |
| Accounts payable | | | \$ 40,000 |
| Short-term debt | | | <u>200,000</u> |
| Total current liabilities | | | <u>240,000</u> |
| Long-term debt | | | <u>500,000</u> |
| Total liabilities | | | <u>740,000</u> |
| Total equity | | | <u>3,598,000</u> |
| Total liabilities & equity | | | <u><u>\$ 4,338,000</u></u> |

Q4 Income Statement, 12/31/X2

| Income: | <u>Quarter ended</u> | <u>Year-to-date</u> |
|--|----------------------|---------------------|
| Income from grain: | | |
| Cash sale of grain | \$ 132,000 | \$ 1,372,000 |
| Beginning inventory | - | (1,120,000) |
| Ending inventory | 1,233,000 | 1,233,000 |
| Hedge gain (loss), see Note 3 | <u>(42,000)</u> | <u>(82,000)</u> |
| Total income from grain | <u>1,323,000</u> | <u>1,403,000</u> |
| Expenses: | | |
| Input cost | - | 300,000 |
| Interest | 30,000 | 30,000 |
| Depreciation | 80,000 | 80,000 |
| General and administrative (G&A) | 780,000 | 795,000 |
| Hedge gain (loss) | - | - |
| Accrual adjustments (investment in growing crops) | <u>300,000</u> | <u>-</u> |
| Total expenses | <u>1,190,000</u> | <u>1,205,000</u> |
| Net income (loss) | <u>133,000</u> | <u>198,000</u> |
| Other comprehensive income (loss): | | |
| Unrealized cash flow hedge gain (loss), see Note 4 | (50,000) | (98,000) |
| Realized fair value hedge loss (gain), see Note 5 | <u>48,000</u> | <u>48,000</u> |
| Total other comprehensive income (loss) | <u>(2,000)</u> | <u>(50,000)</u> |
| Total comprehensive income (loss) | <u>\$ 131,000</u> | <u>\$ 148,000</u> |

Q4 Statement of Owner Equity

| | | As of 12/31/X2 | | |
|--------------|-----------------------------------|--------------------|---------------------|---------------------|
| | | Accumulated | | |
| | | Other | Retained | |
| | | Comprehensive | Capital | Total |
| | | Income | | |
| Quarter | Owner equity, 9/30/X2 | \$ (48,000) | \$ 3,535,000 | \$ 3,487,000 |
| | Total comprehensive Income (loss) | (2,000) | 133,000 | \$ 131,000 |
| | Owner (withdrawals) | - | (20,000) | \$ (20,000) |
| | Owner equity, 12/31/X2 | <u>\$ (50,000)</u> | <u>\$ 3,648,000</u> | <u>\$ 3,598,000</u> |
| Year-to-Date | Owner equity, 12/31/X1 | \$ - | \$ 3,530,000 | \$ 3,530,000 |
| | Total comprehensive Income (loss) | (50,000) | 198,000 | \$ 148,000 |
| | Owner (withdrawals) | - | (80,000) | \$ (80,000) |
| | Owner equity, 12/31/X2 | <u>\$ (50,000)</u> | <u>\$ 3,648,000</u> | <u>\$ 3,598,000</u> |

Q4 Financial Statement Notes

FINANCIAL STATEMENT NOTES

1 Lifted hedge on 20,000 bu Dec 'X2, rolled remaining 60,000 bu to Mar 'X3, and hedged 50,000 bu of planned 'X3 crop.

2 Produced 200,000 bu in 'X2, sold 20,000 spot market.

3 Note for Quarter: (\$12,000) realized loss, (\$24,000) realized loss from roll, (\$6,000) unrealized but recognized loss from roll. See Notes 5 and 6.

Note for Year: (\$12,000) realized loss, (\$24,000) realized loss from roll, (\$6,000) unrealized but recognized loss from roll, less \$60,000 realized loss from old crop.

Fair Value Hedge, 'X1 crop realized loss of (\$40,000).

Fair Value Hedge, 'X2 crop in inventory, (\$12,000) realized loss on sale, (\$24,000) realized loss from roll, (\$6,000) unrealized but recognized loss from roll.

4 Note for Quarter: (\$50,000) unrecognized and unrealized loss from 'X3 crop (cash flow hedge).

Note for Year: (\$98,000) unrecognized and unrealized loss from 'X3 crop (cash flow hedge).

5 \$48,000 realized fair value hedge loss from 'X2 crop, previously a cash flow hedge. Reversed because loss was converted to a realized fair value loss, see Note 3.

Summary Balance Sheets

| Summary Balance Sheets | 3/31/X2 | 6/30/X2 | 9/30/X2 | 12/31/X2 |
|-------------------------------|---------------------|---------------------|---------------------|---------------------|
| Cash | 40,000 | 955,000 | 875,000 | 127,000 |
| Hedge account | 65,000 | 45,000 | 52,000 | 58,000 |
| Inventories | 1,160,000 | - | - | 1,233,000 |
| Investment in growing crops | - | 300,000 | 300,000 | - |
| Fixed assets | <u>3,000,000</u> | <u>3,000,000</u> | <u>3,000,000</u> | <u>2,920,000</u> |
| Total assets | <u>\$ 4,265,000</u> | <u>\$ 4,300,000</u> | <u>\$ 4,227,000</u> | <u>\$ 4,338,000</u> |
| | | | | |
| A/P and S/T debt | 240,000 | 240,000 | 240,000 | 240,000 |
| Long-term debt | <u>500,000</u> | <u>500,000</u> | <u>500,000</u> | <u>500,000</u> |
| Total liabilities | <u>740,000</u> | <u>740,000</u> | <u>740,000</u> | <u>740,000</u> |
| | | | | |
| Retained capital | 3,525,000 | 3,560,000 | 3,535,000 | 3,648,000 |
| Other comprehensive income | <u>-</u> | <u>-</u> | <u>(48,000)</u> | <u>(50,000)</u> |
| Total capital | <u>3,525,000</u> | <u>3,560,000</u> | <u>3,487,000</u> | <u>3,598,000</u> |
| | | | | |
| Total liabilities and capital | <u>\$ 4,265,000</u> | <u>\$ 4,300,000</u> | <u>\$ 4,227,000</u> | <u>\$ 4,338,000</u> |

Summary Income Statements

| Summary Income Statements | | 1st Quarter | Year-to-Date | 2nd Quarter | Year-to-Date | 3rd Quarter | Year-to-Date | 4th Quarter | Year-to-Date |
|---------------------------|--------------------------|-------------------|------------------|-------------------|------------------|--------------------------|------------------|---------------------------|-------------------|
| Sales | Bushels | - | - | 200,000 | 200,000 | - | 200,000 | 20,000 | 220,000 |
| | Avg price per bu | - | - | 6.20 | 6.20 | - | 6.20 | 6.60 | 6.24 |
| | Cash | - | - | 1,240,000 | 1,240,000 | - | 1,240,000 | 132,000 | 1,372,000 |
| | Inventory adjustment | 40,000 | 40,000 | (1,160,000) | (1,120,000) | - | (1,120,000) | 1,233,000 | 113,000 |
| | Hedging G/L | (20,000) <i>A</i> | (20,000) | (20,000) <i>B</i> | (40,000) | - | (40,000) | (42,000) <i>C+D+F</i> | (82,000) |
| | Income | <u>20,000</u> | <u>20,000</u> | <u>60,000</u> | <u>80,000</u> | <u>-</u> | <u>80,000</u> | <u>1,323,000</u> | <u>1,403,000</u> |
| Expenses | Input costs | - | - | 300,000 | 300,000 | - | 300,000 | - | 300,000 |
| | Interest | - | - | - | - | - | - | 30,000 | 30,000 |
| | Depreciation | - | - | - | - | - | - | 80,000 | 80,000 |
| | Other | 5,000 | 5,000 | 5,000 | 10,000 | 5,000 | 15,000 | 780,000 | 795,000 |
| | Inv. in growing crop adj | - | - | (300,000) | (300,000) | - | (300,000) | 300,000 | - |
| | Expenses | <u>5,000</u> | <u>5,000</u> | <u>5,000</u> | <u>10,000</u> | <u>5,000</u> | <u>15,000</u> | <u>1,190,000</u> | <u>1,205,000</u> |
| Net income (loss) | | 15,000 | 15,000 | 55,000 | 70,000 | (5,000) | 65,000 | 133,000 | 198,000 |
| Other comp. income | Hedging G/L | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>(48,000) <i>C</i></u> | <u>(48,000)</u> | <u>(2,000) <i>E-C</i></u> | <u>(50,000)</u> |
| Total comp. income | Hedging G/L | <u>\$ 15,000</u> | <u>\$ 15,000</u> | <u>\$ 55,000</u> | <u>\$ 70,000</u> | <u>\$ (53,000)</u> | <u>\$ 17,000</u> | <u>\$ 131,000</u> | <u>\$ 148,000</u> |

Summary Financial Statement Notes:

- A The \$20,000 loss relates to a fair value hedge for 'X1 crop (in storage). Because the hedge is fair value, the marked-to-market loss is recognized on the Income Statement in the revenue section, essentially a reduction to the increase in the value of the inventory, even though the hedge is still open.
- B The \$20,000 loss relates to a fair value hedge for the 'X1 crop that was sold during the quarter. The loss is recognized on the Income Statement in the revenue section and offset the increased cash price on the hedged production.
- C Cash flow on 'X2 growing crop is marked-to-market as of Sep 30, 'X2 and the hedging loss is included in other comprehensive income.
- D Of the 80,000 bushel cash flow hedge placed in the third quarter, 20,000 bushels were sold leaving a 60,000 bushel hedge outstanding at year-end, which is now fair value hedge because the 'X2 crop has been harvested and is now in inventory. The 20,000 bushels were sold on 10/31/X2 and incurred a (\$12,000) loss which is recognized on the quarter 4 Income Statement. However, the \$12,000 loss was included as other comprehensive loss in quarter 3, so this amount needs removed from other comprehensive income in quarter 4 and added as a hedging loss.
- E The \$(50,000) hedging loss from the 'X3 crop is a cash flow hedge related to planned production next year. The 50,000 bushels hedged had a \$1/bu price movement resulting in the (\$50,000) loss which is reflected in other comprehensive income.
- F The \$12,000 gain results from a reversal of the (\$48,000) other comprehensive loss from the third quarter. This was included in the futures open trade equity as of 9/30/X2. However, 20,000 bushels were sold resulting in a hedge loss of \$12,000, and the remaining 60,000 bushels were rolled from Dec 'X2 to Mar 'X3. The roll results in recognition of a \$24,000 loss and the sum of these two losses become realized in net income. In order to offset the \$48,000 loss from the prior period, a change in the gain/loss realized of \$12,000 is recognized. On the fourth quarter income statement, the (\$42,000) hedging loss recognized in revenue is the results of (\$48,000) plus (\$6,000 plus \$12,000).

Overall Summary

| Hedging, Brokerage and Inventory | | 3/31/X2 | 6/30/X2 | 9/30/X2 | 12/31/X2 |
|----------------------------------|--------------------------------|------------|------------|------------|--------------|
| Corn Hedged | Quantity, bu | 100,000 | | | |
| X1 Crop | Short Hedge Price, \$/bu | \$ 5.80 | | | |
| | MTM (Long) Hedge Price, \$/bu | \$ 6.00 | | | |
| | Hedge G/L, \$/bu | \$ (0.20) | | | |
| | Hedge G/L, \$ | (20,000) A | | | |
| Corn Hedged | Quantity, bu | | | 80,000 | 60,000 |
| X2 Crop | Short Hedge Price, \$/bu | | | \$ 6.00 | \$ 6.75 |
| | MTM (Long) Hedge Price, \$/bu | | | \$ 6.60 | \$ 6.85 |
| | Hedge G/L, \$/bu | | | \$ (0.60) | \$ (0.10) |
| | Hedge G/L, \$ | | | (48,000) C | (6,000) D |
| Corn Hedged | Quantity, bu | | | | 50,000 |
| X3 Crop | Short Hedge Price, \$/bu | | | | \$ 5.80 |
| | MTM (Long) Hedge Price, \$/bu | | | | \$ 6.80 |
| | Hedge G/L, \$/bu | | | | \$ (1.00) |
| | Hedge G/L, \$ | | | | (50,000) E |
| Brokerage | Beginning Balance | - | 65,000 | 45,000 | 52,000 |
| Account | Cash Deposited | 85,000 | 30,000 | 55,000 | 50,000 |
| | Cash Withdrawn | - | (70,000) | - | - |
| | Change in Gain/(Loss) Realized | - | (20,000) B | - | 12,000 F |
| | Cash Balance | 85,000 | 45,000 | 100,000 | 114,000 |
| | MTM Adjustment | (20,000) A | - | (48,000) C | (56,000) D+E |
| | Ending Balance | 65,000 | 45,000 | 52,000 | 58,000 |
| Grain | X1 Bushels | 200,000 | - | - | |
| Inventory | \$/Bu | \$ 5.80 | \$ 6.40 | \$ 6.60 | |
| | Value, \$ | 1,160,000 | - | - | |
| | X2 Bushels | | | | 180,000 |
| | \$/Bu | | | | \$ 6.85 |
| | Value, \$ | | | | 1,233,000 |

Alternative Method

| Hedging account | 3 mon ending Mar 'X2 | 6 mon ending Jun 'X2 | 9 mon ending Sep 'X2 | 12 mon ending Dec 'X2 |
|---------------------|-------------------------|-------------------------|-------------------------|--------------------------|
| Beginning balance | \$ - | \$ - | \$ - | \$ - |
| Ending balance | \$ 65,000.00 | \$ 45,000.00 | \$ 52,000.00 | \$ 58,000.00 |
| Deposits | \$ 85,000.00 | \$ 115,000.00 | \$ 170,000.00 | \$ 220,000.00 |
| Withdrawals | \$ - | \$ 30,000.00 | \$ 30,000.00 | \$ 30,000.00 |
| Hedging gain/(loss) | <u>\$ (20,000.00)</u> | <u>\$ (40,000.00)</u> | <u>\$ (88,000.00)</u> | <u>\$ (132,000.00)</u> |

Detailed Livestock Example

- **Included in Appendix H (Hedging Transactions) of the FFSC's Financial Guidelines for Agriculture**
- **Only hog hedging statements shown.**
- **Corn hedging positions for the hog operation are the opposite of the corn example**

Q1 Hedge Statement, 3/31/X2

Your activity this period:

| <u>Date</u> | <u>Pounds</u> | | <u>Contracts</u> | | <u>Contract Description</u> | <u>Price / cwt</u> | <u>Debit</u> | <u>Credit</u> | <u>Amount</u> |
|-------------|---------------|----------------|------------------|-------------|--------------------------------|--------------------|---------------|---------------|---------------|
| | <u>Long #</u> | <u>Short #</u> | <u>Bought</u> | <u>Sold</u> | | | | | |
| 1/1/X2 | | | | | Wire receipt (Margin call) | | | \$ 75,000.00 | \$ 75,000.00 |
| 1/1/X2 | | 1,000,000 | | 25 | Apr 'X2 CME Lean Hogs | \$ 82.550 | | | \$ 75,000.00 |
| 1/24/X2 | 800,000 | | 20 | | Jun 'X2 CME Lean Hogs \$94 Put | \$ 3.090 | \$ 24,720.00 | | \$ 50,280.00 |
| 2/15/X2 | | | | | Wire receipt (Margin call) | | | \$ 160,000.00 | \$ 210,280.00 |
| 3/25/X2 | 1,000,000 | | 25 | | Apr 'X2 CME Lean Hogs | \$ 102.680 | \$ 201,300.00 | | \$ 8,980.00 |
| 3/27/X2 | | 1,480,000 | | 37 | Jul 'X2 Lean Hogs | \$ 102.580 | | | \$ 8,980.00 |

Positions in your account:

| <u>Date</u> | <u>Pounds</u> | | <u>Contracts</u> | | <u>Contract Description</u> | <u>Price</u> | <u>Debit</u> | <u>Credit</u> | |
|-------------|---------------|----------------|------------------|-------------|--------------------------------|--------------|--------------|---------------|----------------|
| | <u>Long #</u> | <u>Short #</u> | <u>Bought</u> | <u>Sold</u> | | | | | |
| 3/27/X2 | | 1,480,000 | | 37 | Jul 'X2 Lean Hogs | \$ 102.580 | \$ 17,316.00 | | \$ (17,316.00) |
| | | | | | Close | \$ 103.750 | | | |
| 1/24/X2 | 800,000 | | 20 | | Jun 'X2 CME Lean Hogs \$94 Put | \$ 3.090 | \$ 24,720.00 | | |
| | 800,000 | | 20 | | Close | \$ 4.150 | | \$ 33,200.00 | \$ 33,200.00 |

Period Recap

| | | |
|---------------------------|----------|--------------|
| Beginning balance | 12/31/X1 | \$ - |
| This periods activity | | \$ 8,980.00 |
| Ending Balance | 3/31/X2 | \$ 8,980.00 |
| Futures open trade equity | | \$ 15,884.00 |
| Account value at Market | 3/31/X2 | \$ 24,864.00 |

Q1 Balance Sheet, as of 3/31/X2

| Assets | | | |
|---------------------------------------|--------|-------------------|---------------------|
| Current assets: | | | |
| Cash | | | \$ 214,690 |
| | Cash | Market adjustment | |
| Hedge account | | | |
| Corn account | 20,000 | 40,000 | 60,000 |
| Hog account | 8,980 | 15,884 | 24,864 |
| Net hedge accounts | | | 84,864 |
| Grain inventory, see Note 1 | | | 143,750 |
| Hogs inventory, see Note 2 | | | 3,072,000 |
| Total current assets | | | 3,515,304 |
| Fixed assets | | | 1,125,000 |
| Total assets | | | \$ 4,640,304 |
| Liabilities & Equity | | | |
| Current liabilities: | | | |
| Accounts payable | | | \$ 40,000 |
| Short-term debt | | | 1,700,000 |
| Total current liabilities | | | 1,740,000 |
| Long-term debt | | | 771,875 |
| Total liabilities | | | 2,511,875 |
| Total equity | | | 2,128,429 |
| Total liabilities & equity | | | \$ 4,640,304 |

Q1 Income Statement, 3/31/X2

| Income: | <u>Quarter ended</u> | <u>Year to date</u> |
|---|----------------------|---------------------|
| Income from hogs: | | |
| Cash sale of hogs | \$ 2,029,840 | \$ 2,029,840 |
| Beginning inventory | (2,850,000) | (2,850,000) |
| Ending inventory | 3,072,000 | 3,072,000 |
| Hedge gain (loss) | <u>(201,300)</u> | <u>(201,300)</u> |
| Total income from hogs | <u>2,050,540</u> | <u>2,050,540</u> |
| Expenses: | | |
| Feed costs | 1,293,750 | 1,293,750 |
| Hedge (gain) loss on feed corn | - | - |
| Accrual adjustments (change in grain inventory) | <u>(116,500)</u> | <u>(116,500)</u> |
| Net feed costs | <u>1,177,250</u> | <u>1,177,250</u> |
| Weaned pig costs | 385,000 | 385,000 |
| Other input costs | 100,000 | 100,000 |
| Interest | 31,400 | 31,400 |
| Depreciation | 25,000 | 25,000 |
| General and administrative (G&A) | <u>15,000</u> | <u>15,000</u> |
| Total expenses | <u>1,733,650</u> | <u>1,733,650</u> |
| Net income (loss) | 316,890 | 316,890 |
| Other comprehensive income (loss): | | |
| Hedge gain (loss): | | |
| Corn | 40,000 | 40,000 |
| Hog | <u>(8,836)</u> | <u>(8,836)</u> |
| Total other comprehensive income (loss) | <u>31,164</u> | <u>31,164</u> |
| Total comprehensive income (loss) | <u>\$ 348,054</u> | <u>\$ 348,054</u> |

Q2 Hedge Statement, 6/30/X2

Your activity this period:

| <u>Date</u> | <u>Pounds</u> | | <u>Contracts</u> | | <u>Contract Description</u> | <u>Price / cwt</u> | <u>Debit</u> | <u>Credit</u> | <u>Amount</u> |
|-------------|---------------|----------------|------------------|-------------|-----------------------------|--------------------|---------------|---------------|---------------|
| | <u>Long #</u> | <u>Short #</u> | <u>Bought</u> | <u>Sold</u> | | | | | |
| 4/1/X2 | | | | | Wire receipt (Margin call) | | \$ 5,000.00 | \$ 13,980.00 | |
| 4/30/X2 | | | | | Wire receipt (Margin call) | | \$ 5,000.00 | \$ 18,980.00 | |
| 5/15/X2 | | | | | Wire receipt (Margin call) | | \$ 5,000.00 | \$ 23,980.00 | |
| 5/31/X2 | | | | | Wire receipt (Margin call) | | \$ 15,000.00 | \$ 38,980.00 | |
| 6/10/X2 | 1,480,000 | | | 37 | Jul 'X2 Lean Hogs | \$ 93.230 | \$ 138,380.00 | \$ 177,360.00 | |
| 6/10/X2 | | 2,240,000 | | 56 | Oct 'X2 Lean Hogs | \$ 85.800 | | \$ 177,360.00 | |
| 6/15/X2 | | | | | Wire disbursement | | \$ 125,000.00 | \$ 52,360.00 | |

Positions in your account:

| <u>Date</u> | <u>Pounds</u> | | <u>Contracts</u> | | <u>Contract Description</u> | <u>Price</u> | <u>Debit</u> | <u>Credit</u> | |
|-------------|---------------|----------------|------------------|-------------|-----------------------------|--------------|--------------|---------------|--|
| | <u>Long #</u> | <u>Short #</u> | <u>Bought</u> | <u>Sold</u> | | | | | |
| 6/10/X2 | | 2,240,000 | | 56 | Oct 'X2 Lean Hogs | \$ 85.800 | \$ 41,440.00 | 41,440.00 | |
| | | | | | Close | \$ 83.950 | | | |

Period Recap

| | | |
|---------------------------|---------|--------------|
| Beginning balance | 3/31/X2 | \$ 8,980.00 |
| This periods activity | | \$ 43,380.00 |
| Ending Balance | 6/30/X2 | \$ 52,360.00 |
| Futures open trade equity | | \$ 41,440.00 |
| Account value at Market | 6/30/X2 | \$ 93,800.00 |

Q2 Balance Sheet, as of 6/30/X2

| Assets | | | |
|---------------------------------------|-------------|------------------------------|---------------------|
| Current assets: | | | |
| Cash | | | \$ 412,402 |
| | <u>Cash</u> | <u>Market adjustment</u> | |
| Hedge account | | | |
| Corn account | 25,000 | - | 25,000 |
| Hog account | 52,360 | 41,440 | <u>93,800</u> |
| Net hedge accounts | | | <u>118,800</u> |
| Grain inventory, see Note 1 | | | 104,688 |
| Hogs inventory, see Note 2 | | | <u>3,128,250</u> |
| Total current assets | | | <u>3,764,140</u> |
| Fixed assets | | | 1,100,000 |
| Total assets | | | <u>\$ 4,864,140</u> |
| Liabilities & Equity | | | |
| Current liabilities: | | | |
| Accounts payable | | | \$ 40,000 |
| Short-term debt | | | <u>1,775,000</u> |
| Total current liabilities | | | 1,815,000 |
| Long-term debt | | | <u>754,375</u> |
| Total liabilities | | | <u>2,569,375</u> |
| Total equity | | | <u>2,294,765</u> |
| Total liabilities & equity | | | <u>\$ 4,864,140</u> |



Q2 Income Statement, 6/30/X2

| Income: | <u>Quarter ended</u> | <u>Year to date</u> |
|---|----------------------|---------------------|
| Income from hogs: | | |
| Cash sale of hogs | \$ 2,141,700 | \$ 4,171,540 |
| Beginning inventory | (3,072,000) | (2,850,000) |
| Ending inventory | 3,128,250 | 3,128,250 |
| Hedge gain (loss) | <u>113,660</u> | <u>(87,640)</u> |
| Total income from hogs | <u>2,311,610</u> | <u>4,362,150</u> |
| Expenses: | | |
| Feed costs | 1,562,500 | 2,856,250 |
| Hedge (gain) loss on feed corn | (60,000) | (60,000) |
| Accrual adjustments (change in grain inventory) | <u>39,062</u> | <u>(77,438)</u> |
| Net feed costs | <u>1,541,562</u> | <u>2,718,812</u> |
| Weaned pig costs | 414,000 | 799,000 |
| Other input costs | 105,000 | 205,000 |
| Interest | 33,988 | 65,388 |
| Depreciation | 25,000 | 50,000 |
| General and administrative (G&A) | <u>16,000</u> | <u>31,000</u> |
| Total expenses | <u>2,135,550</u> | <u>3,869,200</u> |
| Net income (loss) | 176,060 | 492,950 |
| Other comprehensive income (loss): | | |
| Hedge gain (loss): | | |
| Corn | (40,000) | - |
| Hog | <u>50,276</u> | <u>41,440</u> |
| Total other comprehensive income (loss) | <u>10,276</u> | <u>41,440</u> |
| Total comprehensive income (loss) | <u>\$ 186,336</u> | <u>\$ 534,390</u> |

Q3 Hedge Statement, 9/30/X2

Your activity this period:

| <u>Date</u> | <u>Pounds</u> | | <u>Contracts</u> | | <u>Contract Description</u> | <u>Price / cwt</u> | <u>Debit</u> | <u>Credit</u> | <u>Amount</u> |
|-------------|---------------|----------------|------------------|-------------|-----------------------------|--------------------|--------------|---------------|---------------|
| | <u>Long #</u> | <u>Short #</u> | <u>Bought</u> | <u>Sold</u> | | | | | |
| 7/30/X2 | | | | | Wire receipt (Margin call) | | | \$ 25,000.00 | 77,360.00 |
| 8/31/X2 | | | | | Wire receipt (Margin call) | | | \$ 50,000.00 | \$ 127,360.00 |
| 9/15/X2 | 2,240,000 | | | 56 | Oct 'X2 Lean Hogs | \$ 84.400 | | \$ 31,360.00 | \$ 158,720.00 |
| 9/20/X2 | | 2,400,000 | | 60 | Dec 'X2 Lean Hogs | \$ 87.300 | | - | \$ 158,720.00 |

Positions in your account:

| <u>Date</u> | <u>Pounds</u> | | <u>Contracts</u> | | <u>Contract Description</u> | <u>Price</u> | <u>Debit</u> | <u>Credit</u> | |
|-------------|---------------|----------------|------------------|-------------|-----------------------------|--------------|---------------|---------------|-----------------|
| | <u>Long #</u> | <u>Short #</u> | <u>Bought</u> | <u>Sold</u> | | | | | |
| 9/20/X2 | | 2,400,000 | | 60 | Dec 'X2 Lean Hogs | \$ 87.300 | \$ 102,720.00 | | \$ (102,720.00) |
| | | | | | Close | \$ 91.580 | | | |

Period Recap

| | | |
|---------------------------|---------|-----------------|
| Beginning balance | 6/30/X2 | \$ 52,360.00 |
| This periods activity | | \$ 106,360.00 |
| Ending Balance | 9/30/X2 | \$ 158,720.00 |
| Futures open trade equity | | \$ (102,720.00) |
| Account value at Market | 9/30/X2 | \$ 56,000.00 |

Q3 Balance Sheet, as of 9/30/X2

| Assets | | | |
|---------------------------------------|-------------|------------------------------|---------------------|
| Current assets: | | | |
| Cash | | | \$ 443,980 |
| | <u>Cash</u> | <u>Market adjustment</u> | |
| Hedge account | | | |
| Corn account | 25,000 | 48,000 | 73,000 |
| Hog account | 158,720 | (102,720) | <u>56,000</u> |
| Net hedge accounts | | | <u>129,000</u> |
| Grain inventory, see Note 1 | | | 110,550 |
| Hogs inventory, see Note 2 | | | <u>3,111,500</u> |
| Total current assets | | | <u>3,795,030</u> |
| Fixed assets | | | 1,075,000 |
| Total assets | | | <u>\$ 4,870,030</u> |
| Liabilities & Equity | | | |
| Current liabilities: | | | |
| Accounts payable | | | \$ 40,000 |
| Short-term debt | | | <u>1,950,000</u> |
| Total current liabilities | | | 1,990,000 |
| Long-term debt | | | <u>734,375</u> |
| Total liabilities | | | <u>2,724,375</u> |
| Total equity | | | <u>2,145,655</u> |
| Total liabilities & equity | | | <u>\$ 4,870,030</u> |



Q3 Income Statement, 9/30/X2

| Income: | <u>Quarter ended</u> | <u>Year to date</u> |
|---|----------------------|---------------------|
| Income from hogs: | | |
| Cash sale of hogs | \$ 2,214,857 | \$ 6,386,397 |
| Beginning inventory | (3,128,250) | (2,850,000) |
| Ending inventory | 3,111,500 | 3,111,500 |
| Hedge gain (loss) | 31,360 | (56,280) |
| Total income from hogs | <u>2,229,467</u> | <u>6,591,617</u> |
| Expenses: | | |
| Feed costs | 1,637,500 | 4,493,750 |
| Hedge (gain) loss on feed corn | - | (60,000) |
| Accrual adjustments (change in grain inventory) | (5,862) | (83,300) |
| Net feed costs | <u>1,631,638</u> | <u>4,350,450</u> |
| Weaned pig costs | 444,000 | 1,243,000 |
| Other input costs | 110,000 | 315,000 |
| Interest | 34,779 | 100,167 |
| Depreciation | 25,000 | 75,000 |
| General and administrative (G&A) | 17,000 | 48,000 |
| Total expenses | <u>2,262,417</u> | <u>6,131,617</u> |
| Net income (loss) | (32,950) | 460,000 |
| Other comprehensive income (loss): | | |
| Hedge gain (loss): | | |
| Corn | 48,000 | 48,000 |
| Hog | (144,160) | (102,720) |
| Total other comprehensive income (loss) | <u>(96,160)</u> | <u>(54,720)</u> |
| Total comprehensive income (loss) | <u>\$ (129,110)</u> | <u>\$ 405,280</u> |

Q4 Hedge Statement, 12/31/X2

Your activity this period:

| Date | Pounds | | Contracts | | Contract Description | Price / cwt | Debit | Credit | Amount |
|----------|-----------|-----------|-----------|------|----------------------------------|-------------|--------------|--------------|---------------|
| | Long # | Short # | Bought | Sold | | | | | |
| 10/30/X2 | | | | | Wire receipt (Margin call) | | | \$ 25,000.00 | \$ 183,720.00 |
| 10/30/X2 | 1,600,000 | | | 40 | Jul 'X3 CME Lean Hogs \$100 Put | \$ 7.430 | 118,880.00 | | \$ 64,840.00 |
| 10/30/X2 | | 1,600,000 | | 40 | Jul 'X3 CME Lean Hogs \$90 Put | \$ 3.350 | | 53,600.00 | \$ 118,440.00 |
| 10/30/X2 | | 1,600,000 | | 40 | Jul 'X3 CME Lean Hogs \$110 Call | \$ 2.180 | | 34,880.00 | \$ 153,320.00 |
| 12/15/X2 | 2,400,000 | | | 60 | Dec 'X2 Lean Hogs | \$ 85.430 | | 44,880.00 | \$ 198,200.00 |
| 12/15/X2 | | 1,800,000 | | 45 | Apr 'X3 Lean Hogs | \$ 88.130 | | | \$ 198,200.00 |
| 12/15/X2 | | 1,200,000 | | 30 | Dec 'X3 Lean Hogs | \$ 78.130 | | | \$ 198,200.00 |
| 12/15/X2 | | | | | Wire disbursement | | \$ 25,000.00 | | \$ 173,200.00 |

Positions in your account:

| Date | Pounds | | Contracts | | Contract Description | Price | Debit | Credit | Amount |
|----------|-----------|-----------|-----------|------|----------------------------------|-----------|---------------|---------------|---------------------|
| | Long # | Short # | Bought | Sold | | | | | |
| 12/15/X2 | | 1,800,000 | | 45 | Apr 'X3 Lean Hogs | \$ 88.130 | | \$ 7,740.00 | \$ 7,740.00 |
| | | | | | Close | \$ 87.700 | | | |
| 12/15/X2 | | 1,200,000 | | 30 | Dec 'X3 Lean Hogs | \$ 78.130 | \$ 18,240.00 | | (18,240.00) |
| | | | | | Close | \$ 79.650 | | | |
| 10/30/X2 | 1,600,000 | | | 40 | Jul 'X3 CME Lean Hogs \$100 Put | \$ 7.430 | | \$ 118,880.00 | |
| | 1,600,000 | | | 40 | Close | \$ 8.450 | \$ 135,200.00 | | 135,200.00 |
| 10/30/X2 | | 1,600,000 | | 40 | Jul 'X3 CME Lean Hogs \$90 Put | \$ 3.350 | \$ 53,600.00 | | |
| | | 1,600,000 | | 40 | Close | \$ 3.450 | \$ 55,200.00 | | (55,200.00) |
| 10/30/X2 | | 1,600,000 | | 40 | Jul 'X3 CME Lean Hogs \$110 Call | \$ 2.180 | \$ 34,880.00 | | |
| | | 1,600,000 | | 40 | Close | \$ 1.030 | \$ 16,480.00 | | (16,480.00) |
| | | | | | | | | | <u>\$ 53,020.00</u> |

Period Recap

| | | |
|---------------------------|----------|---------------|
| Beginning balance | 9/30/X2 | \$ 158,720.00 |
| This periods activity | | \$ 14,480.00 |
| Ending Balance | 12/31/X2 | \$ 173,200.00 |
| Futures open trade equity | | \$ 53,020.00 |
| Account value at Market | 12/31/X2 | \$ 226,220.00 |



Q4 Balance Sheet, as of 12/31/X2

| Assets | | | |
|---------------------------------------|---------|----------------------|---------------------|
| Current assets: | | | |
| Cash | | | \$ 274,495 |
| | Cash | Market adjustment | |
| Hedge account | | | |
| Corn account | 61,000 | 23,500 | 84,500 |
| Hog account | 173,200 | 53,020 | 226,220 |
| Net hedge accounts | | | <u>310,720</u> |
| Grain inventory, see Note 1 | | | 192,672 |
| Hogs inventory, see Note 2 | | | <u>3,180,963</u> |
| Total current assets | | | <u>3,958,850</u> |
| Fixed assets | | | 1,050,000 |
| Total assets | | | <u>\$ 5,008,850</u> |
| Liabilities & Equity | | | |
| Current liabilities: | | | |
| Accounts payable | | | \$ 40,000 |
| Short-term debt | | | <u>2,050,000</u> |
| Total current liabilities | | | 2,090,000 |
| Long-term debt | | | <u>711,875</u> |
| Total liabilities | | | <u>2,801,875</u> |
| Total equity | | | <u>2,206,975</u> |
| Total liabilities & equity | | | <u>\$ 5,008,850</u> |

Q4 Income Statement, 12/31/X2

| Income: | Quarter ended | Year to date |
|---|------------------|-------------------|
| Income from hogs: | | |
| Cash sale of hogs | \$ 2,086,425 | \$ 8,472,822 |
| Beginning inventory | (3,111,500) | (2,850,000) |
| Ending inventory | 3,180,963 | 3,180,963 |
| Hedge gain (loss) | <u>44,880</u> | <u>(11,400)</u> |
| Total income from hogs | <u>2,200,768</u> | <u>8,792,385</u> |
| Expenses: | | |
| Feed costs | 1,687,500 | 6,181,250 |
| Hedge (gain) loss on feed corn | (36,000) | (96,000) |
| Accrual adjustments (change in grain inventory) | <u>(82,122)</u> | <u>(165,422)</u> |
| Net feed costs | <u>1,569,378</u> | <u>5,919,828</u> |
| Weaned pig costs | 456,000 | 1,699,000 |
| Other input costs | 115,000 | 430,000 |
| Interest | 36,910 | 137,077 |
| Depreciation | 25,000 | 100,000 |
| General and administrative (G&A) | <u>18,000</u> | <u>66,000</u> |
| Total expenses | <u>2,220,288</u> | <u>8,351,905</u> |
| Net income (loss) | <u>(19,520)</u> | <u>440,480</u> |
| Other comprehensive income (loss): | | |
| Hedge gain (loss): | | |
| Corn | (24,500) | 23,500 |
| Hog | <u>125,340</u> | <u>22,620</u> |
| Total other comprehensive income (loss) | <u>100,840</u> | <u>46,120</u> |
| Total comprehensive income (loss) | <u>\$ 81,320</u> | <u>\$ 486,600</u> |

Q4 Statement of Owner Equity

As of 12/31/X2

| | | Accumulated | | |
|--------------|-----------------------------------|------------------|---------------------|---------------------|
| | | Other | Retained | |
| | | Comprehensive | Capital | Total |
| | | Income | | |
| Quarter | Owner equity, 9/30/X2 | \$ (54,720) | \$ 2,200,375 | \$ 2,145,655 |
| | Total comprehensive Income (loss) | 100,840 | (19,521) | \$ 81,319 |
| | Owner (withdrawals) | - | (20,000) | \$ (20,000) |
| | Owner equity, 12/31/X2 | <u>\$ 46,120</u> | <u>\$ 2,160,855</u> | <u>\$ 2,206,975</u> |
| Year-to-Date | Owner equity, 12/31/X1 | \$ - | \$ 1,800,375 | \$ 1,800,375 |
| | Total comprehensive Income (loss) | 46,120 | 440,480 | \$ 486,600 |
| | Owner (withdrawals) | - | (80,000) | \$ (80,000) |
| | Owner equity, 12/31/X2 | <u>\$ 46,120</u> | <u>\$ 2,160,855</u> | <u>\$ 2,206,975</u> |

Summary Balance Sheets

| Summary Balance Sheets | 3/31/X2 | 6/30/X2 | 9/30/X2 | 12/31/X2 |
|-------------------------------|---------------------|---------------------|---------------------|---------------------|
| Cash | \$ 214,690 | \$ 412,402 | \$ 443,980 | \$ 274,495 |
| Hedge accounts: | | | | |
| Corn | 60,000 | 25,000 | 73,000 | 84,500 |
| Hogs | 24,864 | 93,800 | 56,000 | 226,220 |
| Inventories | | | | |
| Corn | 143,750 | 104,688 | 110,550 | 192,672 |
| Hogs | 3,072,000 | 3,128,250 | 3,111,500 | 3,180,963 |
| Fixed assets | 1,125,000 | 1,100,000 | 1,075,000 | 1,050,000 |
| Total assets | <u>\$ 4,640,304</u> | <u>\$ 4,864,140</u> | <u>\$ 4,870,030</u> | <u>\$ 5,008,850</u> |
| A/P and S/T debt | \$ 1,740,000 | 1,815,000 | 1,990,000 | 2,090,000 |
| Long-term debt | 771,875 | 754,375 | 734,375 | 711,875 |
| Total liabilities | <u>2,511,875</u> | <u>2,569,375</u> | <u>2,724,375</u> | <u>2,801,875</u> |
| Retained capital | 2,097,265 | 2,253,325 | 2,200,375 | 2,160,855 |
| Other comp. income | 31,164 | 41,440 | (54,720) | 46,120 |
| Total capital | <u>2,128,429</u> | <u>2,294,765</u> | <u>2,145,655</u> | <u>2,206,975</u> |
| Total liabilities and capital | <u>\$ 4,640,304</u> | <u>\$ 4,864,140</u> | <u>\$ 4,870,030</u> | <u>\$ 5,008,850</u> |

Summary Income Statements

| Summary Income Statements | | 1st Quarter | | Year-to-Date | | 2nd Quarter | | Year-to-Date | | 3rd Quarter | | Year-to-Date | | 4th Quarter | | Year-to-Date | |
|---------------------------|------------------------|-------------|------------------|--------------|------------------|-------------|------------------|--------------|------------------|-------------|------------------|--------------|------------------|-------------|------------------|--------------|------------------|
| Sales | Pounds | | 2,887,500 | | 2,887,500 | | 3,025,000 | | 5,912,500 | | 3,162,500 | | 9,075,000 | | 3,300,000 | | 12,375,000 |
| | Ave. price per cwt | \$ | 93.7300 | \$ | 93.7300 | \$ | 94.4000 | \$ | 94.0728 | \$ | 93.3800 | \$ | 93.8314 | \$ | 84.3000 | \$ | 91.2897 |
| | Cash | \$ | 2,029,840 | \$ | 2,029,840 | \$ | 2,141,700 | \$ | 4,171,540 | \$ | 2,214,857 | \$ | 6,386,397 | \$ | 2,086,425 | \$ | 8,472,822 |
| | Accrual Adjustment | | 222,000 | | 222,000 | | 56,250 | | 278,250 | | (16,750) | | 261,500 | | 69,463 | | 330,963 |
| | Hedging G/L | | (201,300) | | (201,300) | | 113,660 | | (87,640) | | 31,360 | | (56,280) | | 44,880 | | (11,400) |
| | Income | | <u>2,050,540</u> | | <u>2,050,540</u> | | <u>2,311,610</u> | | <u>4,362,150</u> | | <u>2,229,467</u> | | <u>6,591,617</u> | | <u>2,200,768</u> | | <u>8,792,385</u> |
| Expenses | Feed costs | | 1,293,750 | | 1,293,750 | | 1,562,500 | | 2,856,250 | | 1,637,500 | | 4,493,750 | | 1,687,500 | | 6,181,250 |
| | Feed inventory adj. | | (116,500) | | (116,500) | | 39,063 | | (77,438) | | (5,863) | | (83,300) | | (82,122) | | (165,422) |
| | Hedging (gains) losses | | - | | - | | (60,000) | | (60,000) | | - | | (60,000) | | (36,000) | | (96,000) |
| | Net feed costs | | <u>1,177,250</u> | | <u>1,177,250</u> | | <u>1,541,563</u> | | <u>2,718,813</u> | | <u>1,631,638</u> | | <u>4,350,450</u> | | <u>1,569,378</u> | | <u>5,919,828</u> |
| | Starter pig costs | | 385,000 | | 385,000 | | 414,000 | | 799,000 | | 444,000 | | 1,243,000 | | 456,000 | | 1,699,000 |
| | Other input costs | | 100,000 | | 100,000 | | 105,000 | | 205,000 | | 110,000 | | 315,000 | | 115,000 | | 430,000 |
| | Interest | | 31,400 | | 31,400 | | 33,988 | | 65,388 | | 34,779 | | 100,167 | | 36,910 | | 137,077 |
| | Depreciation | | 25,000 | | 25,000 | | 25,000 | | 50,000 | | 25,000 | | 75,000 | | 25,000 | | 100,000 |
| | Other | | 15,000 | | 15,000 | | 16,000 | | 31,000 | | 17,000 | | 48,000 | | 18,000 | | 66,000 |
| | Expenses | | <u>1,733,650</u> | | <u>1,733,650</u> | | <u>2,135,551</u> | | <u>3,869,201</u> | | <u>2,262,417</u> | | <u>6,131,617</u> | | <u>2,220,288</u> | | <u>8,351,905</u> |
| Net income (loss) | | 316,890 | | 316,890 | | 176,060 | | 492,950 | | (32,950) | | 460,000 | | (19,521) | | 440,480 | |
| Comprehensive | Hedging G/L | | <u>31,164</u> | | <u>31,164</u> | | <u>10,276</u> | | <u>41,440</u> | | <u>(96,160)</u> | | <u>(54,720)</u> | | <u>100,840</u> | | <u>46,120</u> |
| Total comp. income | Hedging G/L | \$ | <u>348,054</u> | \$ | <u>348,054</u> | \$ | <u>186,336</u> | \$ | <u>534,390</u> | \$ | <u>(129,110)</u> | \$ | <u>405,280</u> | \$ | <u>81,319</u> | \$ | <u>486,600</u> |

Alternative Method

Corn Hedging Account

| Hedging account | 3 mon ending Mar 'X2 | 6 mon ending Jun 'X2 | 9 mon ending Sep 'X2 | 12 mon ending Dec 'X2 |
|---------------------|-------------------------|-------------------------|-------------------------|--------------------------|
| Beginning balance | \$ - | \$ - | \$ - | \$ - |
| Ending balance | \$ 60,000.00 | \$ 25,000.00 | \$ 73,000.00 | \$ 84,500.00 |
| Deposits | \$ 30,000.00 | \$ 30,000.00 | \$ 30,000.00 | \$ 30,000.00 |
| Withdrawals | \$ 10,000.00 | \$ 65,000.00 | \$ 65,000.00 | \$ 65,000.00 |
| Hedging gain/(loss) | \$ 40,000.00 | \$ 60,000.00 | \$ 108,000.00 | \$ 119,500.00 |

Hog Hedging Account

| Hedging account | 3 mon ending Mar 'X2 | 6 mon ending Jun 'X2 | 9 mon ending Sep 'X2 | 12 mon ending Dec 'X2 |
|---------------------|-------------------------|-------------------------|-------------------------|--------------------------|
| Beginning balance | \$ - | \$ - | \$ - | \$ - |
| Ending balance | \$ 24,864.00 | \$ 93,800.00 | \$ 56,000.00 | \$ 226,220.00 |
| Deposits | \$ 235,000.00 | \$ 265,000.00 | \$ 340,000.00 | \$ 365,000.00 |
| Withdrawals | \$ - | \$ 125,000.00 | \$ 125,000.00 | \$ 150,000.00 |
| Hedging gain/(loss) | \$ (210,136.00) | \$ (46,200.00) | \$ (159,000.00) | \$ 11,220.00 |

1099-B Corn

| | | | | | | | |
|--|--|--|--|---|---|---|--|
| PAYER'S name, street address, city, state, ZIP code, and telephone Corn Purchases | | 1a Date of sale or exchange | | OMB No. 1545-0715 2012 Form 1099-B | Proceeds From Broker and Barter Exchange Transactions | | |
| | | 1b Date of acquisition | | | | | |
| | | 1c Type of gain or loss Short-term <input type="checkbox"/> Long-term <input type="checkbox"/> | | | | | |
| PAYER'S federal identification number | | RECIPIENT'S identification number | | 1d Stock of other symbol | 1e Quantity sold | | |
| RECIPIENT'S name | | 2a Stocks, bonds, etc. \$ - | | Reported to IRS } <input type="checkbox"/> Sales price Sales price less <input type="checkbox"/> commissions and option premiums | 2b If box checked, loss based on amount in 2a is not allowed <input type="checkbox"/> | | |
| Street address (including apt. no.) | | 3 Cost or other basis \$ - | | | | | |
| City, state, and ZIP code | | 7 Bartering \$ - | | Copy B For Recipient This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if this income is taxable and the IRS determines that it has not been reported. | | | |
| Account number (see instructions) | | 2nd TIN not. <input type="checkbox"/> | | | | 4 Federal income tax withheld \$ - | |
| CUSIP number | | 9 Profit or (loss) realized in 'X2 on closed contracts \$ 96,000.00 | | | | 6 Check if: a <input type="checkbox"/> Noncovered security b <input type="checkbox"/> Basis reported to IRS | |
| | | 11 Unrealized profit or (loss) on open contracts - 12/31/X2 \$ 23,500.00 | | 10 Unrealized profit or (loss) on open contracts - 12/31/X1 \$ - | | | |
| | | | | 12 Aggregate profit or (loss) on contracts \$ 119,500.00 | | | |
| | | | | 13 State 14 State identification no. 15 State tax withheld \$ | | | |

Form 1099-B

(keep for your records)

Department of the Treasury - Internal Revenue Service



1099-B Hogs

| | | | | | |
|--|--|--|--|---|--|
| PAYER'S name, street address, city, state, ZIP code, and telephone Hog Production | | 1a Date of sale or exchange | | OMB No. 1545-0715 2012 Form 1099-B | Proceeds From Broker and Barter Exchange Transactions |
| | | 1b Date of acquisition | | | |
| | | 1c Type of gain or loss Short-term <input type="checkbox"/> Long-term <input type="checkbox"/> | | | |
| PAYER'S federal identification number RECIPIENT'S identification number | | 1d Stock of other symbol | | 1e Quantity sold | |
| | | 2a Stocks, bonds, etc. | | 2b If box checked, loss based on amount in 2a is not allowed <input type="checkbox"/> | |
| RECIPIENT'S name | | \$ - | | Reported to IRS <input type="checkbox"/> Sales price less commissions and option premiums | |
| | | 3 Cost or other basis | | 4 Federal income tax withheld | |
| Street address (including apt. no.) | | \$ - | | Copy B For Recipient This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction may be imposed on you if this income is taxable and the IRS determines that it has not been reported. | |
| | | 5 Wash sale loss disallowed | | | |
| City, state, and ZIP code | | \$ - | | <input type="checkbox"/> Noncovered security | |
| | | 7 Bartering | | <input type="checkbox"/> Basis reported to IRS | |
| Account number (see instructions) | | 2nd TIN not. <input type="checkbox"/> | | 9 Profit or (loss) realized in 'X2 on closed contracts | |
| | | 9 Profit or (loss) realized in 'X2 on closed contracts | | 10 Unrealized profit or (loss) on open contracts - 12/31/X1 | |
| CUSIP number | | \$ (11,400.00) | | \$ - | |
| | | 11 Unrealized profit or (loss) on open contracts - 12/31/X2 | | 12 Aggregate profit or (loss) on contracts | |
| | | \$ 22,620.00 | | \$ 11,220.00 | |
| | | | | 13 State | |
| | | | | 14 State identification no. | |
| | | | | 15 State tax withheld | |
| | | | | \$ CliftonLarsonAllen | |



Conclusion

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