Direct Marketing Curriculum
Managing Business, Financial and Legal Risks

University of Arkansas Division of Agriculture
Center for Agricultural and Rural Sustainability
The National Agricultural Law Center
Direct Marketing Curriculum

Introduction

In Arkansas and across the nation, local food marketing has expanded beyond the farmers’ markets and food stands. Local farmers are marketing directly to public schools, hospitals, and institutions of higher education as well as directly to food retailers. One group of resources gaining popularity with producers and consumers alike are electronic marketing networks that gather information from producers and potential customers and give farmers greater access to local and regional markets. Large retail chains are also exploring how these tools can be used to increase market share by meeting customer demands for fresher, local grown foods.

These new and emerging direct markets potentially offer benefits to producers by providing known and stable markets. However, before producers can realize the full potential of these new marketing avenues, several barriers must be overcome; marketing directly to retail and wholesale outlets presents additional issues that must be considered by producers.

This direct marketing curriculum was developed as a risk management education program for producers interested in direct marketing their products. The curriculum contains 21 lessons on various topics relating to marketing, legal, financial and business risks associated with direct marketing. Each lesson contains a lesson plan with a set of instructions, an accompanying presentation, handouts and a list of sources for additional information. For more information and to download these lessons visit: www.manageyourrisk.net.

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Fall 2009 Edition
# Direct Marketing Curriculum

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### Downloading Information

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Acknowledgements

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For more information, contact Bill Buchanan.
Section 1 - Marketing

Lesson 1.1  Marketing Basics
Lesson 1.2  Introduction to Direct Marketing
Lesson 1.3  Farmers Markets
Lesson 1.4  Value Added and Niche Marketing
Lesson 1.5  Establishing a Vendor Agreement with Walmart
Lesson 1.6  Marketing to Restaurants and Retailers
Lesson 1.7  MarketMaker Basics for Arkansas Producers
Lesson 1.8  Organic Marketing
Lesson 1.1: Marketing Basics

*Estimated time: One hour.*

**Overview**

Lesson 1.1 will teach participants the fundamental concepts of marketing agricultural products and services. Participants will understand marketing as the process of planning then executing pricing, promoting and distribution programs to satisfy customer needs. The lesson will teach participants to the importance of identifying markets, developing short- and long-term goals and teach them the various stages in the life cycle of products. They will understand that marketing is more than just selling a product or service; it is an essential part of the business.

**Objectives**

1. List the four essential elements of a successful business
2. Define marketing
3. Understand the 4 P's of marketing
4. Recognize the importance of short- and long-term goals
5. Become familiar with different marketing strategies
6. Complete the Marketing’s Four P’s handout

**Assessment**

Participants will view the presentation on basic marketing concepts and participate throughout with question and answers. The presenter will engage the audience to keep their interest and attention focused on the materials. Participants will take notes on provided handouts and will complete the Four P’s Worksheets.

**Equipment, Supplies, and Materials**

1. Power Point presentation Lesson 1.1
2. Notes pages Lesson 1.1
3. Handout - Steps to Marketing Your Product
4. Handout - Marketing’s Four P’s
5. Four P’s Worksheets
References


Classroom Procedures

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
</table>
| Lead discussion to assess previous knowledge. | • How would you define marketing?  
• What is the key to marketing your farm/business products and services? |
| Slides 2-3: Introduction | Give a quick overview of the topics to be addressed and the objectives of the presentation |
| Slide 4: A Successful Business | • There are four key ingredients to running a successful business  
• You must have the technical knowhow to compete in your industry  
• Your strategy and financial outlook must be well planned by forming a business plan  
• You must be determined to reach your business goals  
• And you must have a base level of business management knowledge in order to be successful |
| Slides 5-7: Marketing Intro | • How would you define marketing?  
• Marketing is more than just promotion to sell your products or services.  
• Good marketing plans focus on satisfying customer needs and maximizing profits (rather than maximizing sales)  
• Give participants and overview of the topics to be covered: the 4 P’s of Marketing, Marketing Mix and Strategic Marketing |
### Classroom Procedures Continued

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
</table>
| Slides 8-19: The Four P’s of Marketing | • The 4 P’s represent the basic components of a marketing plan and each component will be discussed in detail  
• **Product** - A tangible object or an intangible service. Intangible products are often service based like the tourism industry & the hotel industry.  
• **Price** - The price is the amount a customer pays for the product. It is determined by a number of factors including market share, competition, material costs, product identity and the customer's perceived value of the product.  
• **Place** - Place represents the location where a product can be purchased. It is often referred to as the distribution channel. It can include any physical store as well as virtual stores on the Internet.  
• **Promotion** - Promotion represents all of the communications that a marketer may use in the marketplace. Promotion has four distinct elements - advertising, public relations, word of mouth and point of sale. |

| Slide 8: Extended 4 P’s | • People, Processes and Physical Evidence are three additional components that could be consider  
• People - all people who directly or indirectly influence the perceived value of the product or service, including knowledge workers, employees, management and consumers.  
• Process - procedures, mechanisms and flow of activities which lead to an exchange of value.  
• Physical evidence - the direct sensory experience of a product or service that allows a customer to measure whether he or she has received value. Examples: customer service or wait times, or the environment in which a product or service is delivered |
### Classroom Procedures Continued

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
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</thead>
</table>
| Slides 13-15: Pricing Strategies    | - As a manager, you can follow a number of alternative pricing strategies  
- Your selection of a pricing strategy should be based on your product, customer demand, the competitive environment, and the other products you will offer |
| Slides 16-18: Pricing Aspects       | - The amount of money you will actually receive may be complicated by other pricing aspects that will decrease (or increase) the actual amount of money you receive.  
- Price is the one “P” that generates revenue, while the other three “P’s” incur costs  
- Effective pricing is important to the success of your business. |
| Slide 20: Marketing Mix             | - The 'marketing mix' is a set of controllable, tactical marketing tools that work together to achieve company's objectives  
- The intersection of the 4 P’s or the strategic implementation of the 4 P’s of marketing |
| Slides 21-22: Long-Term Business Goals | - These goals provide direction to the business. The key characteristics of goals are that they are general, observable, challenging and not timed.  
- D-R-I-V-E is an acronym used to describe long-term goals. These goals are characterized by being directional, reasonable, inspiring, visible, and eventual.  
- Long-term business goals tend to be: broad in scope and without a time frame, help achieve the vision, and provide a roadmap |
| Slides 23-24: Short-Term Objectives | - Our short-term objectives are specific. S-M-A-R-T is the acronym to describe these.  
- For these objectives, there is a specific result that is identified with a specific deadline.  
- We know when they have been achieved. Example: Reduce weed control cost this year by 10% from last year's level.  
- Specific: Focused on herbicide costs  
- Measurable: 10% reduction  
- Attainable: Herbicides and production practices are available to make this occur  
- Rewarding: Helps lower production costs  
- Timed: Going to do it this year |
### Classroom Procedures Continued

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
</table>
| Slides 23-24: Short-Term Objectives (Cont.) | - Setting short-term objectives are important to a business  
  1. Provide specific direction  
  2. They provide mechanism for control. Objectives are typically broken down into standards of performance.  
  3. They provide a way of keeping score.  
  5. They motivate those who are assigned the task of accomplishing them. |
| Slides 26-30: Marketing Strategy | - Strategy is about finding a unique way to put the company’s activities (buying, selling, producing, hiring, firing, etc.) together that is hard or impossible for competitors to replicate and is valuable to customers.  
- Requires the company to focus resources on the activities that create competitive advantage.  
- **Penetration**: Why? To dominate market. How? To increase usage or get new customers; reduce price; expand distribution or increase promotional activities. When? When market is growing  
- **Market Development**: Why? To venture into new markets. How? Sell existing products in new markets; modify product; use different distribution; use different advertising/sales strategy. When? Present market is saturated  
- **Product Development**: Why? To satisfy buyer’s need How? New or improved product; innovate or augment product. When? Customer has a need or a problem; or firm is looking to enter new markets  
Classroom Procedures Continued

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
</table>
| Slides 26-30: Marketing Strategy (cont.) | • The next step is to assess how business development will occur.  
• Done by plotting the product to be sold versus the type of customer focus (Growth Options Matrix).  
• Products are either ones currently produced by the firm (old) or ones that business has never produced before (new). Customers are either current customers (old) or ones the business has not reached before (new).  
• Market penetration: Increase market share among existing customers  
• Market development: Attract new customers to existing products  
• Product Development: Create new products for present markets  
• Diversification: Introduce new products into new markets |
| Handout: The 4 P's of Marketing | Suggest that participants take the time to complete the worksheets to help them understand and tailor their marketing mix to their customers' needs.  
Suggest that participants read the additional marketing materials provided as printouts as well as the links to websites. | The presentation is only intended as an introduction to basic marketing concepts; the additional reading materials and links are a good start for participants interested in learning more. |
Sources of Additional Information

   http://www.agmrc.org/business_development/operating_a_business/marketing/understanding_marketing.cfm
   http://www.sba.gov/smallbusinessplanner/manage/marketandprice/SERV_UNDMARKETING.html
   http://www.sba.gov/smallbusinessplanner/manage/marketandprice/SERV_MARKBASICS.html
   https://www.agecon.purdue.edu/cab/research/articles/Marketing_Glossary.pdf
7. From Supply Push to Demand Pull: Agribusiness Strategies for Today’s Consumers.  
   Amber Waves, November 2003.  
   http://www.ers.usda.gov/amberwaves/november03/Features/supplypushdemandpull.htm

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Four P’s Worksheets

Developed from: Ehmke, Fulton and Lusk (2005)

**Instructions:** The following set of worksheets will help you understand and tailor your marketing mix to your customers’ needs. The four sections relate to the four P’s of product, price, place, and promotion. In the first part of each section, you will complete a table to help you gain a better understanding of what you are offering and what your competitors are offering. In the “Further Assessment” part of each section, you will answer questions to help you tailor your marketing mix to your customers’ needs.

1. **Product**

Describe your product’s characteristics in the first column and the characteristics of your competitors’ product in the second column.

<table>
<thead>
<tr>
<th></th>
<th>Your Product</th>
<th>Your Competitors’ Product</th>
</tr>
</thead>
<tbody>
<tr>
<td>Product (e.g., fresh fruit beverage)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Product Variety</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Product Appearance</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Product Quality</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Product Features</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Product Functionality</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Services</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Brand Name</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Packaging</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Warranties</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
**Further Assessment**

1. What features are considered basic features by your customers (ones that must be offered?)

2. What features are missing from the existing product/service choices in the market place? How can your product/service address this gap?

3. What are the key features/benefits of your product and service, especially as they compare to what your competitors are supplying?

4. How can your product give you an advantage in the marketplace?

| 2. Place |
|---|---|
| In the first column, describe how your product is distributed. Describe your competitors' product distribution in the second column. |

<table>
<thead>
<tr>
<th>Your Product</th>
<th>Your Competitors’ Product</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Direct Sales</strong></td>
<td></td>
</tr>
<tr>
<td><strong>Reseller Sales</strong> (Sales Through an Intermediary)</td>
<td></td>
</tr>
<tr>
<td><strong>Market Coverage</strong> (distribution strategy)</td>
<td></td>
</tr>
</tbody>
</table>
**Further Assessment**

<table>
<thead>
<tr>
<th>Question</th>
<th>Answer</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. What is the best way to sell your product? Direct selling? Through a reseller? Will this be a competitive advantage or disadvantage?</td>
<td></td>
</tr>
<tr>
<td>2. How will your plan for coverage and other place decisions compare to those of your competitors? Will this be a competitive advantage or disadvantage?</td>
<td></td>
</tr>
</tbody>
</table>

### 3. Price

For each of the following pricing strategies, describe the advantages and disadvantages of using that method for your product. Which is the best one for you to use?

<table>
<thead>
<tr>
<th>Pricing Strategy</th>
<th>Advantages and Disadvantages for Your Product</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost-Plus</td>
<td></td>
</tr>
<tr>
<td>Value-Based</td>
<td></td>
</tr>
<tr>
<td>Competitive</td>
<td></td>
</tr>
<tr>
<td>Going-Rate</td>
<td></td>
</tr>
<tr>
<td>Skimming</td>
<td></td>
</tr>
<tr>
<td>Discount</td>
<td></td>
</tr>
<tr>
<td>Loss-Leader</td>
<td></td>
</tr>
<tr>
<td>Psychological</td>
<td></td>
</tr>
</tbody>
</table>
For each of the following pricing aspects, describe the advantages and disadvantages for your product in the first column. In the second column, describe to what extent your competitors are following that approach.

<table>
<thead>
<tr>
<th></th>
<th>Advantages and Disadvantages for Your Product</th>
<th>To What Extent Are Your Competitors Using This Policy for Their Products?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Payment Period</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Allowance</td>
<td></td>
<td></td>
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<tr>
<td>Seasonal Allowances</td>
<td></td>
<td></td>
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<tr>
<td>Bundling of Products/Services</td>
<td></td>
<td></td>
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<tr>
<td>Trade Discounts</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Price Flexibility</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Price Differences Among Target Customer Groups</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Price Differences Among Geographic Areas</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Volume Discounts and Wholesale Pricing</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash and Early Payment Discounts</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Credit Terms</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Further Assessment

<table>
<thead>
<tr>
<th>Question</th>
<th>Answer</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. How sensitive is your target market to changes in prices?</td>
<td></td>
</tr>
<tr>
<td>2. How does your expected pricing compare to your competition's pricing?</td>
<td></td>
</tr>
<tr>
<td>3. Will pricing make your business special?</td>
<td></td>
</tr>
<tr>
<td>4. How will your products/services provide a better price-performance balance than your competitors' products/services?</td>
<td></td>
</tr>
</tbody>
</table>
4. Promotion

Describe your product’s promotion in the first column and your competitors’ promotion in the second.

<table>
<thead>
<tr>
<th></th>
<th>Your Product</th>
<th>Your Competitors’ Product</th>
</tr>
</thead>
<tbody>
<tr>
<td>Advertising</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Radio</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Television</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Print</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Electronic</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Word of Mouth</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Generic</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Public Relations</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Personal Selling</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sales Promotion</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Further Assessment

1. What promotion efforts are most effective for your target market?

2. How can your promotion strategy give you an advantage in the marketplace?
Marketing Basics

Lesson 1.1

Overview

- Learn fundamental concepts of marketing agricultural products and services
- Understanding marketing as the process of planning then executing pricing, promoting and distribution programs to satisfy customer needs
- Identifying markets, developing short- and long-term goals and the various stages in the life cycle of products
- Marketing is more than just selling a product or service; it is an essential part of the business

Objectives

1) List the four essential elements of a successful business
2) Define marketing
3) Understand the 4 P’s of marketing
4) Recognize the importance of short- and long-term goals
5) Become familiar with different marketing strategies
Four Essential Elements (successful businesses)

1) Technical skills (competencies) for your industry
2) Creating a Practical Business Plan
3) Dedication & Willingness to Reach Business Goals
4) Mastering a “Basic” Knowledge of business management areas

Marketing

- Any activity or performance of an activity that involves the flow of products/services from the initial point of production/creation to the hands of consumers.
- Marketing is the flow of products and services to consumers and the transactions that facilitate or manage that flow.

Marketing

Marketing is based on the importance of customers to a business and has two important principles:

- All company policies and activities should be directed toward satisfying customer needs
- Profitable sales volume is more important than maximum sales volume
Marketing Basics

Understanding your marketing plan and determining your marketing strategy:

- 4Ps of marketing
- Marketing Mix
- Strategic marketing

4 P’s of Marketing

Basic Components of a marketing plan:
- Product
- Place (and Time)
- Price
- Promotion

Additional 3 marketing areas:
- People
- Processes
- Physical Evidence

Product

Product: What product/service(s) will I sell? Includes branding and packaging. Also the level of service (quality, dependability, guarantees, etc.).

Product strategies may include concentrating on a narrow product line, developing a highly specialized product or service, or providing a product-service package containing unusually high-quality service.
Place

- **Place (and Time)**: Method used to get the product to your target market, i.e., transportation, marketing channel utilized, market location.

- Working through established distributors or manufacturers' agents generally is easiest for small manufacturers. Small retailers should consider cost and traffic flow in site selection, especially since advertising and rent can be reciprocal: A low-cost, low-traffic location means spending more on advertising to build traffic.

Place

- Direct Sales
- Reseller Sales: Through and Intermediary
- Market Coverage
  - Intensive: widespread distribution
  - Selective: distribution to a few businesses
  - Exclusive: a single reseller

Price

- **Price**: The price of the product involving factors such as cost of production, competitors' prices, volume/quality issues, standard practices.

- The right price is crucial for maximizing total revenue. Generally, higher prices mean lower volume and vice-versa; however, small businesses can often command higher prices because of their personalized service.
Pricing Strategy

- Cost-plus: Adds a standard percentage of profit above the cost of producing a product. Accurately assessing fixed and variable costs is an important part of this pricing method.

- Value-based: Based on the buyer’s perception of value (rather than on your costs). The buyer’s perception depends on all aspects of the product, including non-price factors such as quality, healthfulness, and prestige.

Pricing Strategy

- Competitive: Based on prices charged by competing firms for competing products. This pricing structure is relatively simple to follow because you maintain your price relative to your competitors' prices.

- Going-rate: A price charged that is the common or going-rate in the marketplace. Going-rate pricing is common in markets where most firms have little or no control over the market price.

Pricing Strategy

- Skimming: Involves the introduction of a product at a high price for affluent consumers. Later, the price is decreased as the market becomes saturated.

- Discount: Based on a reduction in the advertised price. A coupon is an example of a discounted price.

- Loss-leader: Based on selling at a price lower than the cost of production to attract customers to the store to buy other products.

- Psychological: Based on a price that looks better, for example, $4.99 per pound instead of $5.00 per pound.
Pricing Aspects

- Payment period: Length of time before payment is due.
- Allowance: Price reductions given when a retailer agrees to undertake some promotional activity for you.
- Seasonal allowances: Reductions given when an order is placed during seasons that typically have low sales.
- Bundling of products/services: Offering an array of products together.

Pricing Aspects

- Trade discounts: Payments to distribution channel members for performing some function such as warehousing and shelf stocking.
- Price flexibility: Ability of salesperson or reseller to modify price.
- Price differences among target customer groups

Pricing Aspects

- Price differences among geographic areas
- Volume discounts and wholesale pricing
- Early payment discounts: Policies to speed payment
- Credit terms: Policies that allow customers to pay for products at a later date.
Promotion

- **Promotion**: Communicating to your customer about the product, place and price of your product.

- Promotion strategies include advertising and direct customer interaction. Good salesmanship is essential for small businesses because of their limited ability to spend on advertising.

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Marketing Mix

- **Product**
- **Place**
- **Price**
- **Promotion**

---

Long-Term Business Goals

- Directional – Move you toward the general objectives of our vision statement
- Reasonable – Are practical and obtainable; not extreme
- Inspiring – Are challenging; affect you positively
- Visible – Are easy to visualize
- Eventual – Will be fulfilled at a future time
Long-Term Business Goals

- Examples of goals might be:
  - Maintain a profitable operation
  - Be considered the top producer in the county
  - Be on the cutting edge of technology
  - Be the premier supplier in the region
  - Create employment for family members

Short-Term Objectives are:

- Specific – The objective achieves a particular, detailed result.
- Measurable – There is a means to determine the objective.
- Attainable – They are within economic and physical capabilities.
- Rewarding – They are profitable and self-satisfying.
- Timed – They have a specific timeline and/or deadline.

Short-term Objectives

- Examples of objectives might be:
  - To increase gross revenues 5 percent each year
  - To achieve 12-15 percent return on equity within 4 years
  - To reduce fixed expenses by 7 percent within 3 years
Importance of Goals

...the purpose of goals is to focus your attention and give you direction, not to identify a final destination.

...if a goal is good, it will provide you direction.

John C. Maxwell

What is strategy?

- Competitive strategy is about being different
- Strategy is the creation of a unique and valuable position in your industry or marketplace
- Activities are the basic units of competitive advantage
- Strategy is about choosing what not to do

Marketing Strategies

“Identify Your Competitive Advantage”

Existing Markets

Existing

New Products & Services

New Product Development

Related Diversification

Market Penetration

Market Development

Section 1-22
Market Penetration

- Why? To dominate your existing market.
- How? Increase current customer product usage or get new customers. Firms either reduce price, expand distribution, or increase promotional activities.
- When? When market is growing.

Market Development

- Why? To venture into new markets.
- How? Sell existing products in new markets; modify product; use different distribution; use different advertising/sales strategy.
- When? Present market is saturated.

New Product Development

- Why? To satisfy buyer’s needs
- How? New or improved product; through innovation or augmentation of a product
- When? Customer has a need or a problem; or firm is looking to enter new markets
Diversification

- Why? Growth opportunities outside of current business
- How? New products for new markets
- When? Distinctive competencies are available. Firm possesses an advantage over competitors

Marketing Strategies?

1) Notice your own buying strategies
2) Take an idea that works in one industry and use it in another
3) Be Specific, quantify your claims
4) Develop an Ability to see Your Customer’s Perspective
5) Innovation
6) Systemization
Summary

- **Marketing** is everything that you do to “communicate” your product/service to your target market.

- Business philosopher Jim Rohn said,
  - First, have something good to say;
  - Second, say it well;
  - Third, say it often.

Summary

- Know your customer! Research and identify your marketing options and incorporate marketing plans into your business plan.

- Utilize available resources available through government agencies, university, trade publications, and other sources.

- Develop a well defined “marketing strategy” with a focus on creating value through differentiated product & service development.

References

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Marketing’s Four P’s: First Steps for New Entrepreneurs. [Link]

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of any information disclosed in this document.
Most agricultural producers are used to marketing their products by taking them to the local elevator, grain terminal, or livestock market. Price may be established through a cash sale, forward cash contract or using some other marketing tool available to the commodity markets. The concept of marketing a product directly to the consumer is an entirely different process.

The marketing plan must begin early as you determine what you are going to produce. You are no longer selling your product on the open market. You need to focus on what are your customer needs and how you will deliver a product that the customer wants.

Complete a market analysis

This step is the research phase that will help you determine the opportunities and challenges for your product. Many good products fail because the market analysis step was either overlooked or not extensive enough? Some of these products are later successful for other entrepreneurs due to sufficient market analysis. This step is where you define the target market at which you will focus your marketing efforts. It is where you need to find answers to lots of questions. Some of which are:

- What is the market potential for organic strawberries (your product) in the area?
- How fast is the fee hunting (your product) market growing?
- What does your typical customer look like?
- Where are your customers located?

Demographic data and Psychographic data help identify the target market. Demographic data indicate the location, age, income level, spending habits and family composition of the potential customer. Psychographic data deal with their hobbies, beliefs and lifestyles. Using this type of information helps determine the marketing strategies of price, promotion and placement.

Another important part of the market analysis is the competitive analysis. This is where you identify your competition and determine their strengths and weaknesses. You determine if the market is already saturated. It helps you identify what it is about what you offer that is better than the competition. The competitive analysis will provide you with information to help you produce a better product so it will have a greater chance for success in the marketplace.

Develop a marketing strategy

The marketing strategy is that part of the planning process where you determine the action steps to overcome the challenges identified in the market analysis. Here you build on the 4 P’s of marketing: Product, Price, Promotion and Placement.

Product – All information regarding your product must be familiar to you. The benefits, features and unique characteristics that set it apart from the competition. To help the consumer identify with your product you may want to use a catchy name so that it is easily remembered by the consumer.

Price - Pricing a product is a new concept for a former commodity producer. Most are used to being a price taker or in other words getting told the price they receive for their product. Now you are the price maker. When you market your product, it is now up to you to determine the asking price. You must price your product at an amount high enough to generate a profit. However, you must also make the price attractive.
enough to encourage customers and generate sales. Pricing is an art, not a science. You must be constantly alert to changes in the marketplace and changes in your business that could signal a need to adjust the product price.

Promotion – Everything you do with your customer to encourage them to purchase your product is promotion. It is not merely advertising but includes public relations and networking. One way of encouraging consumers to purchase your product (if it is a food item) is to provide easy to make, appetizing recipes. You can network with your customers at point of purchase locations by offering samples of your food product. The whole concept of promotion is to catch and hold the public’s attention and get them to buy your product. The Internet has created another avenue for promotion and more questions to answer like: Are you going to develop a web site? What search engines are you going to register with? Are you going to cross link with other related web pages?

Placement – Getting your product to the customer when and where they want it is placement. This is often referred to as distribution. Distribution often represents 15% to 50% of the final price of the product. Often businesses do not have the resources to individually deliver the product to the customer. They must therefore rely on an established distribution channels made up of retailers, wholesalers, distributors, agents, brokers or cooperatives. You must determine the distribution partner that best fills your needs and your customer’s needs. Some non-traditional distribution channels are: u-pick operations, farmers markets, classified ads, consignment selling, community-supported agriculture and restaurant supported agriculture.

Many books have been written on marketing strategy. The information here just touches on a few of the basics to give you a flavor of the mindset changes that need to take place when moving from “selling a commodity” to “marketing your product”.

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Marketing’s Four P’s: First Steps for New Entrepreneurs

Cole Ehmke, Joan Fulton, and Jayson Lusk
Department of Agricultural Economics

Marketing your business is about how you position it to satisfy your market’s needs. There are four critical elements in marketing your products and business. They are the four P’s of marketing.

1. **Product.** The right product to satisfy the needs of your target customer

2. **Price.** The right product offered at the right price.

3. **Place.** The right product at the right price available in the right place to be bought by customers.

4. **Promotion.** Informing potential customers of the availability of the product, its price and its place.

Each of the four P’s is a variable you control in creating the marketing mix that will attract customers to your business. Your marketing mix should be something you pay careful attention to because the success of your business depends on it. As a business manager, you determine how to use these variables to achieve your profit potential. This publication introduces the four P’s of marketing and includes worksheets that will help you determine the most effective marketing mix for your business.

**Product**

“Product” refers to the goods and services you offer to your customers. Apart from the physical product itself, there are elements associated with your product that customers may be attracted to, such as the way it is packaged. Other product attributes include quality, features, options, services, warranties, and brand name. Thus, you might think of what you offer as a bundle of goods and services. Your product’s appearance, function, and support make up what the customer is actually buying. Successful managers pay close attention to the needs their product bundles address for customers.

Your product bundle should meet the needs of a particular target market. For example, a luxury product should create just the right image for “customers who have everything,” while many basic products must be positioned for price-conscious consumers. Other important aspects of product may include an appropriate product range, design, warranties, or a brand name.

Customer research is a key element in building an effective marketing mix. Your knowledge of your target market and your competitors will allow you to offer a product that will appeal to customers and avoid costly mistakes.
If you are considering starting a new business or adding a new product, then make sure the product bundle will fit your business’s strengths and weaknesses, and that it will provide an acceptable risk/return tradeoff. For instance, if your business is very good at timely response to customers, then timely service should be an important part of your product bundle.

Think long term about your venture by planning for the ways you can deepen and broaden your product bundle. For instance, you may be able to take advantage of opportunities to add value through processing, packaging, and customer service. Other future growth may allow you to offer your product to different customers. Start-up businesses are most successful when they concentrate their efforts on one product or one market, like a restaurant or a car service center does. Later growth may occur in the same location or may be in different geographic regions.

A different type of growth would be a diversification of products, with your business offering related products. Offering a whole range of products is most successful if the raw materials, production processes, and distribution methods are similar, which means you do not have to acquire new suppliers, skills and equipment, and distribution methods.

**Price**

“Price” refers to how much you charge for your product or service. Determining your product’s price can be tricky and even frightening. Many small business owners feel they must absolutely have the lowest price around. So they begin their business by creating an impression of bargain pricing. However, this may be a signal of low quality and not part of the image you want to portray. Your pricing approach should reflect the appropriate positioning of your product in the market and result in a price that covers your cost per item and includes a profit margin. The result should neither be greedy nor timid. The former will price you out of the market; pricing too low will make it impossible to grow.

As a manager, you can follow a number of alternative pricing strategies. In the next column are eight common pricing strategies. Some price decisions may involve complex calculation methods, while others are intuitive judgments. Your selection of a pricing strategy should be based on your product, customer demand, the competitive environment, and the other products you will offer.

- **Cost-plus:** Adds a standard percentage of profit above the cost of producing a product. Accurately assessing fixed and variable costs is an important part of this pricing method.
- **Value-based:** Based on the buyer’s perception of value (rather than on your costs). The buyer’s perception depends on all aspects of the product, including non-price factors such as quality, healthfulness, and prestige.
- **Competitive:** Based on prices charged by competing firms for competing products. This pricing structure is relatively simple to follow because you maintain your price relative to your competitors’ prices. In some cases, you can directly observe your competitors’ prices and respond to any price changes. In other cases, customers will select vendors based on bids submitted simultaneously. In those cases, gathering information will be more difficult.
- **Going-rate:** A price charged that is the common or going-rate in the marketplace. Going-rate pricing is common in markets where most firms have little or no control over the market price.
- **Skimming:** Involves the introduction of a product at a high price for affluent consumers. Later, the price is decreased as the market becomes saturated.
- **Discount:** Based on a reduction in the advertised price. A coupon is an example of a discounted price.
- **Loss-leader:** Based on selling at a price lower than the cost of production to attract customers to the store to buy other products.
- **Psychological:** Based on a price that looks better, for example, $4.99 per pound instead of $5.00 per pound.

After you decide on your pricing strategy, the amount of money you will actually receive may be complicated by other pricing aspects that will decrease (or increase) the actual amount of money you receive. You will also have to decide how to determine:

- **Payment period:** Length of time before payment is received.
- **Allowance:** Price reductions given when a retailer
agrees to undertake some promotional activity for you, such as maintaining an in-store display.

- **Seasonal allowances**: Reductions given when an order is placed during seasons that typically have low sales volumes to entice customers to buy during slow times.

- **Bundling of products/services**: Offering an array of products together.

- **Trade discounts** (also called “functional discounts”): Payments to distribution channel members for performing some function such as warehousing and shelf stocking.

- **Price flexibility**: Ability of salesperson or reseller to modify price.

- **Price differences among target customer groups**: Pricing variance among target markets.

- **Price differences among geographic areas**: Pricing variance among geographic regions.

- **Volume discounts and wholesale pricing**: Price reductions given for large purchases.

- **Cash and early payment discounts**: Policies to speed payment and thereby provide liquidity.

- **Credit terms**: Policies that allow customers to pay for products at a later date.

The methods discussed here should be a base from which to construct your price. Your options will vary depending on how you choose to sell your product. For instance, if you make a product but don’t sell it directly to the customer, then you will want to know who sets the retail price and what margin they will require. Tracing the path of your product from production to final purchase is a useful exercise to discover this information. The research needed to understand the pricing along the distribution path will be more than worth the time it takes.

Whatever your price may be, ultimately it must cover your costs, contribute to your image by communicating the perceived value of your product, counter the competition’s offer, and avoid deadly price wars. Remember, price is the one “P” that generates revenue, while the other three “P’s” incur costs. Effective pricing is important to the success of your business.

### Place

“Place” refers to the distribution channels used to get your product to your customers. What your product is will greatly influence how you distribute it. If, for example, you own a small retail store or offer a service to your local community, then you are at the end of the distribution chain, and so you will be supplying directly to the customer. Businesses that create or assemble a product will have two options: selling directly to consumers or selling to a vendor.

### Direct Sales

As a producer, you must decide if supplying direct is appropriate for your product, whether it be sales through retail, door-to-door, mail order, e-commerce, on-site, or some other method. An advantage of direct sales would be the contact you gain by meeting customers face to face. With this contact you can easily detect market changes that occur and adapt to them. You also have complete control over your product range, how it is sold, and at what price.

Direct sales may be a good place to start when the supply of your product is limited or seasonal. For example, direct sales for many home-produced products can occur through home-based sales, markets, and stands.

However, direct sales require that you have an effective retail interface with your customers, which may be in person or electronic. If developing and maintaining this retail interface is not of interest to you or you are not good at it, you should consider selling through an intermediary.

### Reseller Sales (Sales Through an Intermediary)

Instead of selling directly to the consumer, you may decide to sell through an intermediary such as a wholesaler or retailer who will resell your product. Doing this may provide you with a wider distribution than selling direct while decreasing the pressure of managing your own distribution system. Additionally, you may also reduce the storage space necessary for inventory. One of the most important reasons for selling through an intermediary is access to customers. In many situations, wholesalers and retailers have customer connections that would not be possible to obtain on your own.

However, in selling to a reseller you may lose contact with
your end consumer. In some cases, you may also lose some of your company identity. For example, your distributor may request that your product be sold under the reseller’s brand name.

One factor that may influence whether you can find an intermediary to handle your product is production flow. Wholesalers want a steady year-round supply of product to distribute. If you can deliver a steady year-round supply that is of consistent quality, then selling through an intermediary may be a good strategy for you.

**Market Coverage**

No matter whether you sell your product direct or through a reseller, you must decide what your coverage will be in distributing your product. Will you pursue intensive, selective, or exclusive coverage?

**Intensive distribution** is widespread placement in as many places as possible, often at low prices. Large businesses often market on a nationwide level with this method. Convenience products—ones that consumers buy regularly and spend little time shopping for, like chewing gum—do better with intensive (widespread) distribution.

**Selective distribution** narrows distribution to a few businesses. Often, upscale products are sold through retailers that only sell high-quality products. With this option, it may be easier to establish relationships with customers. Products that people shop around for sell better with selective distribution.

**Exclusive distribution** restricts distribution to a single reseller. You may become the sole supplier to a reseller who, in turn, might sell only your product. You may be able to promote your product as prestigious with this method, though you might sacrifice sales volume. Specialty products tend to perform better with exclusive distribution.

**Other Place Decisions**

Product characteristics and your sales volumes will dictate what inventories to maintain and how best to transport your products. Additionally, the logistics associated with acquiring raw materials and ensuring that your final product is in the right place at the right time for the right customers can comprise a large percentage of your total costs and needs careful monitoring.

You may decide to have a combination of all the distribution methods. Whatever you decide, choose the method which you believe will work best for you.

**Promotion**

“Promotion” refers to the advertising and selling part of marketing. It is how you let people know what you’ve got for sale. The purpose of promotion is to get people to understand what your product is, what they can use it for, and why they should want it. You want the customers who are looking for a product to know that your product satisfies their needs.

To be effective, your promotional efforts should contain a clear message targeted to a specific audience reached via an appropriate channel. Your target audience will be the people who use or influence the purchase of your product. You should focus your market research efforts on identifying these individuals. Your message must be consistent with your overall marketing image, get your target audience’s attention, and elicit the response you desire, whether it is to purchase your product or to form an opinion. The channel you select for your message will likely involve use of a few key marketing channels. Promotion may involve advertising, public relations, personal selling, and sales promotions.

A key channel is advertising. Advertising methods to promote your product or service include the following.

- **Radio**: Radio advertisements are relatively inexpensive ways to inform potential local customers about your business. Mid-to-late week is generally the best time to run your radio ad.

- **Television**: Television allows access to regional or national audiences, but may be more expensive than other options.

- **Print**: Direct mail and printed materials, including newspapers, consumer and trade magazines, flyers, and a logo, allow you to explain what, when, where, and why people should buy from you. You can send letters, fact sheets, contests, coupons, and brochures directly to new or old customers on local, regional, or national levels.

- **Electronic**: Company Web sites provide useful information to interested consumers and clients. Password-protected areas allow users to more
intimately interact with you. Advertisements allow broad promotion of your products. Direct e-mail contact is possible if you have collected detailed customer information.

- **Word of Mouth:** Word of mouth depends on satisfied customers (or dissatisfied customers) telling their acquaintances about the effectiveness of your products.

- **Generic:** Generic promotion occurs when no specific brand of product is promoted, but rather a whole industry is advertised. For instance, generic advertising is commonly found for milk, beef, and pork.

Public relations (PR) usually focuses on creating a favorable business image. Important components of a good public relations program include being a good neighbor, being involved in the community, and providing open house days. News stories, often initiated through press releases, can be good sources of publicity.

Personal selling focuses on the role of a salesperson in your communication plans. Salespeople can tailor communication to customers and are very important in building relationships. While personal selling is an important tool, it is costly. So you should make efforts to target personal selling carefully.

Sales promotions are special offerings designed to encourage purchases. Promotions might include free samples, coupons, contests, incentives, loyalty programs, prizes, and rebates. Other programs might focus on educating customers through seminars or reaching them through trade shows. Your target audience may be more receptive to one method than another. Additional sources of promotion may be attending or participating in trade shows, setting up displays at public events, and networking socially at civic and business organizations.

**Final Comment**

The four P’s—product, price, place, and promotion—should work together in your marketing mix. Often, decisions on one element will influence the choices available in others. Selecting an effective mix for your market will take time and effort, but these will pay off as you satisfy customers and create a profitable business. The worksheets that follow will help you construct your marketing plans.

Once you have a good marketing mix—the right product at the right price, offered in the right place and promoted in the right way—you will need to continue to stay on top of market changes and adopt your marketing mix as necessary. Marketing is a part of your venture that will never end.
Lesson 1.2: Introduction to Direct Marketing

Estimated time: One hour.

Overview

Lesson 1.2 is an introduction to direct marketing. First, you will learn how to analyze the potential market before entering into a new product offering. Then, you will learn to develop a marketing strategy based on the four P’s of marketing. Based on the marketing analysis, you will be more able to choose a direct marketing outlet and characterize your product in a way that makes it most appealing to your target audience.

Objectives

1. Be able to conduct a basic market analysis based on current market data in order to better estimate demand for your proposed product.
2. Understand marketing strategy based on the four P’s of marketing: product, price, promotion, and placement.
3. Understand how the four P’s apply to direct marketing venues.

Assessment

There is no homework or in-class example. Three handouts are given to students to highlight the subject matter. Students can learn more through the further reading documents.

Equipment, Supplies, and Materials

1. Power point presentation Lesson 1.2
2. Notes pages Lesson 1.2
3. Handout “Marketing Your Products Directly”
4. Handout “Direct Marketing Options For Small Farms”
References


Classroom Procedures

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
<tbody>
<tr>
<td>Slides 2-3: Overview and objectives</td>
<td>• Lead discussion to assess students’ previous knowledge of the subject.</td>
</tr>
<tr>
<td></td>
<td>• Go over objectives.</td>
</tr>
<tr>
<td>Slide 4: Market analysis</td>
<td>• Estimate market demand before going into a new venture</td>
</tr>
<tr>
<td></td>
<td>• Which direct marketing channel best suits your customers?</td>
</tr>
<tr>
<td></td>
<td>• First – identify customers and their location</td>
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<td></td>
<td>• Second – estimate unfulfilled demand and current market</td>
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<td></td>
<td>• Third – consider market competition</td>
</tr>
<tr>
<td>Slide 5: Marketing Strategy</td>
<td>• The four P’s are the basis of marketing — whether in direct channels or otherwise</td>
</tr>
<tr>
<td></td>
<td>• Even if you have the best product available, no one will buy it if they are not aware of it</td>
</tr>
</tbody>
</table>
### Classroom Procedures Continued

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
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</thead>
</table>
| Slide 6: Product                             | • Packaging – selling appealing sizes, selling products commonly consumed together packaged together at a discounted rate  
• Features – organic, Arkansas grown, special varieties  
• Brand name – branding what used to be only a commodity: Tyson chicken, Riceland rice |
| Slide 7-8: Own price elasticity              | • Work the example in slide 8.  
• Show how to take first order derivative of TC                                                                                          |
| Slide 9: Pricing                             | • Why is it difficult to increase price later in the season? See graph slide 13.                                                        |
| Slide 13: Supply and demand graph            | • A shift to the right in supply results when more sellers enter the market later in the season which results in customers demanding a higher quantity at a lower price. This is why you should not price low in the beginning of the season and expect to be able to raise prices later. |
| Slide 17: Arizona customer survey            | • Highlight that the best promotion and advertising comes from word-of-mouth and roadside signage                                       |
| Slide 18: Roadside signage                   | • Note that roadside signage is only effective if customers are already near your farm or outlet. Consider the location of your operation before investing in roadside signage.  
• Note that cutting prices is less effective than good advertising in direct markets – recall that customers may see a cheaper product as an inferior product. |
| Slides 19-22: Most common direct marketing channels | • This list is not exhaustive, but these methods are by far the most common. Slides highlight advantages and disadvantages to each outlet. |
Sources of Additional Information


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Introduction to Direct Marketing

Lesson 1.2

Overview

- Learn how to analyze the potential market before entering into a new product offering
- Develop a marketing strategy based on the four P's of marketing
- Based on the marketing analysis, you will be more able to choose a direct marketing outlet and characterize your product in a way that makes it most appealing to your target audience

Objectives

1) Be able to conduct a basic market analysis based on current market data in order to better estimate demand for your proposed product.
2) Understand marketing strategy based on the four P's of marketing: product, price, promotion, and placement.
3) Understand how the four P's apply to direct marketing venues.
Market Analysis
- Estimate marketing and production costs
- Identify your target market
- Identify your customers' location
- Estimate your marketing area
- Assess the level of unfulfilled demand among consumers
- Estimate the market growth for your product
- Identify prices customers are currently paying
- Identify your competition's strengths and weaknesses
- Identify differentiating characteristics of your product

Develop a Marketing Strategy
- Product – be familiar with your product's differentiating characteristics and help the consumer identify with your product
- Price – price high enough to generate a profit, but low enough to be competitive and attract customers
- Promotion – advertising, customer relations, networking. This could include samples, recipes, a website, etc.
- Placement – getting your product to the customer; distribution. The direct marketing venues.

Characterization of The Product
- The definition of product includes
  - The actual product
  - Packaging
  - Quality
  - Features
  - Brand name
- Conveys an image appealing to the target audience
Own Price Elasticity

- The estimated own price elasticity for many agricultural products can be found at http://www.ers.usda.gov/Data/Elasticities/Query.aspx
- \( \epsilon \) = own price elasticity of demand

\[ P^* = \frac{MC}{1 + |\epsilon|} \]

\[ MC = \frac{\partial TC}{\partial Q} \]

\[ TC = TVC + TFC \]

Own Price Elasticity Example

- Given
  - \( \epsilon \) of apples = -0.4
  - TVC = 2.8Q
  - TFC = 200
  - \( TVC + TFC = TC = 2.8Q + 200 \)
  - \( \frac{\partial TC}{\partial Q} = MC = 2.8 \)
  - \( P^* = 2.8/1+0.4 = $2 \)

- Pricing your goods based on your total cost assures that you cover your production costs

Pricing Your Products

- Pricing represents the value of your product
  - A price too low gives customers the impression your good is inferior
  - A price too high will price many customers out of the market
- Do not set your price too low at the beginning of a season when competition is low and demand is high – it proves difficult to increase prices later in the season
Pricing Your Products

- Prices can be higher when demand is high but supply is low, such as early crops or specialty products, such as organically grown produce.
- Price competitively based on other producers’ prices.

Demand

- A change in quantity demanded is movement along the demand curve and is only caused by changes in price.
- A change in demand is a shift in the demand curve and is caused by changes in:
  - The prices of substitutes or complements
  - Consumer income
  - Number of consumers
  - Tastes and preferences

Supply

- A change in quantity supplied is movement along the supply curve and is only caused by changes in price.
- A change in supply is a shift in the supply curve (illustrated in next slide) and is caused by changes in:
  - Input costs
  - Government policies
  - Price expectations
  - Weather or disease
  - Technology
  - Size of industry

Section 1-42
Supply and Demand

Types of Pricing Schemes
- Relative pricing
  - Based on prices of your competitors
  - Easier method, but may not be most profitable
  - Local produce can command a higher price than imported due to freshness differences
- Cost oriented pricing
  - Must know your costs of production (fixed and variable costs)
  - Must determine your break even price (price per unit at which variable costs are returned)
  - Must price above break even price to return a profit

Promoting Your Product
- Even if you have the best product on the market, no one will know it exists unless you advertise
- Advertising informs your customers of
  - The availability of the product
  - The seasonality of the product
  - Your location
  - Differentiating characteristics of your product
- Promotion maintains customers during the season
- Promotion early in the season attracts new customers
Promoting Your Product

- Advertising and promotion may not be as effective in direct markets as in other sales outlets.
- Promotion is more effective when products are:
  - Clearly differentiated
  - Of very high quality
  - Especially seasonal
  - A novelty
- Differentiating your product with a name that makes customers feel like they have a personal relationship with you, the producer, is a low cost and effective promotional strategy.

Arizona Extension Customer Survey

**How did you learn about this fresh farm outlet?**

<table>
<thead>
<tr>
<th>Arizona</th>
<th>Michigan</th>
</tr>
</thead>
<tbody>
<tr>
<td>Word-of-mouth; from friends or family</td>
<td>45.4%</td>
</tr>
<tr>
<td>Newspaper articles</td>
<td>14.6%</td>
</tr>
<tr>
<td>Roadside signage</td>
<td>10.6%</td>
</tr>
<tr>
<td>Media advertising</td>
<td>9.3%</td>
</tr>
<tr>
<td>“Fresh Farm produce” brochure</td>
<td>3.4%</td>
</tr>
<tr>
<td>Travel information centers</td>
<td>n.a.</td>
</tr>
<tr>
<td>From other producers/businesses</td>
<td>4.2%</td>
</tr>
</tbody>
</table>

**Have you seen/heard the following advertisements?**

<table>
<thead>
<tr>
<th>Arizona</th>
</tr>
</thead>
<tbody>
<tr>
<td>Roadside signage</td>
</tr>
<tr>
<td>Newspaper articles</td>
</tr>
<tr>
<td>Newspaper advertising</td>
</tr>
<tr>
<td>“Fresh Farm produce” brochure</td>
</tr>
<tr>
<td>Radio advertising</td>
</tr>
<tr>
<td>T.V. coverage</td>
</tr>
</tbody>
</table>

Promoting Your Product

- Survey shows the most effective promotional strategies:
  - Word-of-mouth; from friends or family
  - Roadside signage
- Advertising moves a higher product volume in direct markets than price cutting
- Rule of thumb: 3% of gross sales spent on advertising
- Advertising to your target audience to make the most of your advertising dollars
Choose A Direct Marketing Channel

1. Roadside stand or on-farm marketing
   - Most common system
   - Location is vital to your success

2. Farmers’ markets
   - Offsets disadvantage of production location
   - Increased levels of consumer traffic
   - Must predict sales in order to bring enough product
   - Increased competition

3. Pick-your-own (U-pick)
   - Least labor intensive for grower
   - Better for crops intended for home processing
   - Location is vital to your success

4. Community supported agriculture (CSA)
   - Also called subscription farming or grower contracting
   - Must have a wide variety available throughout the season
   - Good for produce with special attributes, e.g. organic, gourmet, ethnic
   - Can work with other growers to offer customers a wider variety than you can produce

5. Restaurant sales
   - Exceptional quality necessary
   - Need small quantities of products
   - Delivery logistics
   - Growing in popularity

6. Retail sales
   - Some make purchases at the store level, others require higher-up decisions
   - Buy larger volumes of product
   - Prices must be competitive with an extensive market
Choose A Direct Marketing Channel

7. Institutional sales
   - Schools, nursing homes, hospitals, prisons, etc.
   - Usually a less-feasible option for direct marketing, but
     schools may be the best of the options
   - Usually buy from distributors
   - Main goal is minimizing costs

8. Internet marketing or mail orders
   - Market maker
   - May require shipping – is your product shippable?
   - A website is widely and easily accessible promotion
     for your product

References

   http://www.marketmaker.uiuc.edu/content/listing_files/stepstomarketingproduct.pdf
   (PowerPoint slides).
Sources of Additional Information


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USDA/RMA under Award Number 08IE08310225-C

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Marketing Your Products Directly

Today in the U.S., based in no small part on the productivity of the American farmer, consumers have access to a safe, abundant and relatively cheap food supply. In the presence of this stable production of food, producers are challenged by the decreasing margins in terms of prices they receive for their products. Relatively low prices that producers receive for their products force them to keep production costs under control in order to remain viable when using traditional marketing channels. More producers are exploring direct marketing strategies in an attempt to increase profitability. Marketing products directly to consumers provides opportunities for producers to capture higher margins in the marketplace.

Food Marketing Costs

The U.S. food distribution system efficiently markets food from the farm (production phase) to the table (consumption). This system is good at changing the location and form of various products through processing and transportation but operates on very thin margins for the purchases of raw commodities. According to a recent USDA study (ERS 2001), farmers receive on average 19 cents of every dollar spent on food. This amount varies by the type of product (meat, produce, grain, etc.) and on the degree of processing.

Statistics taken from the USDA publication “Food Marketing Costs at a Glance” reveal that U.S. consumers spent $661.1 billion on food in 2000, excluding seafood and imports. Expenditures for farm foods increased $211.3 billion from 1990 to 2000. The primary factor contributing to this increase was higher marketing costs. Over this time period, marketing costs increased by 57 percent and accounted for the largest part of the increase in consumer food expenditures. A large part of this increase is the result of value-added, further processing activities. Consumers have shown a willingness to pay a premium price for further processed or prepared (convenience) foods. Conversely, the farm value of food purchases increased by only 16 percent during this same period.

As the figure details inside, labor makes up the largest component of the food marketing bill. Labor represented 38% of the bill and accounted for $253 billion in expenditures in 2000. Other components contributing to this marketing bill in 2000 are packaging with costs of $53.3 billion (8%), energy costs of $23 billion (3.5%) and advertising costs of $26.1 billion (4%), respectively. The other components comprising the food marketing bill are transportation (4%), profits (4.5%), depreciation (3.5%), rent (4%), interest (2.5%), repairs (1.5%), business taxes (3.5%) and miscellaneous expenses (4%). The remaining 19% in the farm value segment of the graph represents the returns back to the farmers.
Farmers receive on average 19% of every dollar spent on food.

### Legal Considerations for Direct Marketing

As demonstrated in Figure 1 outlining differences in pick-your-own, roadside and farmer’s markets forms of direct marketing, all producers share some exposure to legal liability regardless of their chosen avenue of marketing. Those engaged in any form of direct marketing need to spend the time necessary to identify potential areas of legal liability in their operation. While this discussion can help the producer identify sources of legal liability, it cannot substitute for seeking local legal counsel to more fully discuss the liabilities the producer faces and what can be done to prevent legal problems associated with the operation.

Most states such as Arkansas have what are called recreational access liability limitation statutes. These statutes generally are designed to offer the private landowners some measure of limitations to their liability for allowing the public onto their land for the purpose of engaging in recreational pursuits. While useful in many instances, such statutes are of limited assistance in pick-your-own and farm stand operations, as one of the defining characteristics of the recreational access statute is that the liability protection may not apply if the landowner is engaged in business pursuits. Likewise, many insurance policies contain exclusions from coverage if individuals come onto the property pursuant to business activities.

### Insurance policy coverage and exclusions.

Pick-your-own operations are usually intended as business or income-generating pursuits so they would fall within the exclusions for business pursuits or within the exclusions from liability limitation in recreational access statutes. Therefore, a comprehensive insurance examination with your local insurance broker is in order.

A complete record of risk management activities should be maintained and updated on a regular basis. Some landowners also employ the use of signage and written releases signed by those entering the property. There is also no substitute for supervision and attention to the activities of those on the property. If employees are used, they must also be trained in all aspects of risk management on the operation.
**Figure 1. Direct Marketing Strategies for Agriculture Products.**

<table>
<thead>
<tr>
<th>Characteristic</th>
<th>Pick-Your-Own</th>
<th>Roadside Market</th>
<th>Farmer’s Market</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>INVESTMENT</strong></td>
<td>less capital investment: need containers, ladders, locational signs, parking, building or stand</td>
<td>need building or stand, parking, containers, signs, scales, coolers, etc.</td>
<td>very little capital investment: rent, parking or building space, containers, scales, bags, etc.</td>
</tr>
<tr>
<td><strong>GROWER LIABILITY</strong></td>
<td>high liability insurance: liable for accidents</td>
<td>liable for accidents: need liability insurance</td>
<td>need liability insurance unless covered by market</td>
</tr>
<tr>
<td><strong>OTHER COSTS</strong></td>
<td>need labor for field supervisors and check-out stand; field site transportation; advertising and promotion costs</td>
<td>need sales labor; advertising and promotion costs; some storage, packaging and handling costs; may need to purchase additional produce</td>
<td>need sales labor; stall or sales fees; display costs; transportation, storage, packaging and handling costs; no advertising and promotion costs</td>
</tr>
<tr>
<td><strong>PRICING</strong></td>
<td>large sales per customer; no transportation costs; no sales or broker fees</td>
<td>fairly large sales per customer; limited ability to sell large volumes; no transportation costs; no sales or broker fees</td>
<td>smaller sales per customer; direct competition from other growers</td>
</tr>
<tr>
<td><strong>QUALITY</strong></td>
<td>no grading; can sell whatever customers pick; freshness</td>
<td>can classify and sell more than one grade; can sell seconds; spoilage</td>
<td>highest quality needed</td>
</tr>
<tr>
<td><strong>BARRIERS TO ENTRY</strong></td>
<td>limited demand; limited crops; short season; location</td>
<td>limited demand; location; roadside access; marketing management zoning</td>
<td>municipal restrictions; conflicting goals of organizers; marketing management</td>
</tr>
<tr>
<td><strong>SPECIAL ADVANTAGES</strong></td>
<td>average value of purchase per customer may be higher than at other direct marketing outlets</td>
<td>can be expanded to meet needs of producer; can be tailored to customer’s tastes and preferences</td>
<td>potential for large number of customers; low overhead; advertising done by organization</td>
</tr>
<tr>
<td><strong>SPECIAL DISADVANTAGES</strong></td>
<td>affected by weather; damage to field, trees, plants; location may be critical</td>
<td>affected by weather; location may be critical</td>
<td>time consuming; must transport produce; do not have as much control over promotion</td>
</tr>
</tbody>
</table>

Source: “Characteristics of Direct Marketing Alternatives” by Deborah Young

The trend across most jurisdictions is to afford all those coming onto your property a duty of reasonable care. Regardless, all those entering onto your property for pick-your-own activities have always been afforded the highest standard of care, which requires the landowner to take all necessary precautions against their injury and to warn of all known or hidden dangers.

### Legal considerations when site is operated by third party.

If the roadside market is owned or operated by a third party, the producer should make inquiry whether the market owner has liability insurance for accidents that might occur on the property. Additionally, if the direct market producer is selling from a farmer’s market, different issues should be examined. Many farmer’s markets require their member producers to carry general liability insurance to cover illnesses or injuries that might occur attributable to product or activities on the market. The producer must normally keep insurance coverage up to date and provide proof of coverage to the market or market manager, usually on an annual basis. Farmer’s markets that take place on public property require different inquiry. Discussions between the farmers market board, the market manager and the public (usually municipal) government unit must take place, during which a careful examination of risks and responsibilities should occur.

The above discussion centers on risk of liability for physical injuries to those coming onto the property or into the market. There are other exposures that apply generally across all direct market locations. Specifically, all producers engaged in direct...
Direct Marketing Options for Small Farms

Reduce marketing and financial risks by choosing the best marketing options for your unique situation

By Monika Roth

Direct marketing is a common strategy for farmers marketing their products. It’s not a panacea. You need to carefully evaluate which strategies might work best for your operation, and make investments in your marketing. The key is to have enough customers and sales to cover your production, marketing, and staff costs. It doesn’t matter how many customers you have, you’ll need several customers per week to avoid financial risks. The demand for high quality, fresh produce is very volatile and can take many years. You need to develop your marketing skills.

OPTION 1: FARMERS MARKETS

Farmers markets are a good place to start getting to know your customers and vendors. You can use one to sell direct to consumers, or to get immediate feedback. Farmers markets also provide a good sales channel for small farms, especially in the case of PYO. Liability insurance is a must. Building loyal clientele is key, and can take many years. Your business plan must be based on realistic customer numbers and sales projections.

OPTION 2: ON-FARM SALES

Methods range from simple, self-serve stands to multi-department, year-round farm stores and may include pick-your-own or agritourism enterprises. The higher your overhead, the slimmer your margins will be. But if done right, you can attract more customers and boost your returns.

Self-serve stands are a good way to assess the potential draw from drive-by traffic. Strawberries, sweet corn, tomatoes, peaches, and pumpkins are crops that can stop traffic. Consumers learn about local farms primarily through word-of-mouth. Build a product line based on what customers want, and pay attention to quality. Sufficient traffic may enable your sales to warrant investment in facilities and staffing.

Pick-your-own (PYO) requires advertising and staffing. It can be very profitable, but can cost a lot to set up. For example, it rains every weekend during narrow harvest seasons. PYO can complement agritourism activities where it is one of several activities families can enjoy.

To be successful, you need to know how much your potential customers pay for your product and your field. The key is to have enough customers and sales to cover overhead and other marketing costs.

OPTION 3: COMMUNITY SUPPORTED AGRICULTURE (CSA)

CSA operations typically provide a weekly ‘share’ of pre-picked farm products to customers who pay for their shares at the beginning of the season – usually $300 to $600 per household. The up-front money reduces financial and marketing risks, since customers are sharing in production risks. Sometimes customers help pick, harvest and pack shares in return for a discount. Depending on the operation, customers pick up shares at the farm, a central distribution point, or pay extra for home delivery.

The big challenge is to have enough different crops each week so customers feel like they are getting their money’s worth. It’s important to never come up short, so CSA farmers often have additional outlets for surplus produce. Sometimes several farmers collaborate to offer a wider range of products including fruit, eggs, meat and more.

OPTION 4: RESTAURANT SALES

The farmers market rebrith of the ’80s drew the attention of top chefs (especially from higher-end restaurants) looking for fresh, local products to feature in their menus. Selling to restaurants is not easy. You need exceptional quality and to be willing to cultivate relationships with chefs. Restaurant sales need to be part of your overall strategy, not a way to dump surplus product.

Chefs are as hungry as farmers. You need to deliver on time and work around their schedule. Avoid melting! Find out what local chefs want, and grow a wide range of products for them for as long a season as possible. Most chefs will pay about 25% of retail for produce.

Drawbacks include the need for small quantities of some items. Watch that delivery cost and time don’t eat up profits, and be clear on payment terms. Once a relationship is solid, less face time is needed.

OPTION 5: SALES TO RETAILERS

More and more food retailers are interested in locally grown food, too. As with chefs, reliability is key. Contact retail farm market in your area. Be patient, do not grow all they sell. Most will offer prices only comparable to regional markets. Check out food cooperatives, independent groceries, and independent groceries, as well.

Everything else from convenience stores to supercenters is a channel. Each has unique purchasing requirements. Make sure your product is sellable at the store level, but most require approval from higher-ups. Initiate contact with store managers. For produce in bulk, it is usually sold to a buying consortium or to a “pick-your-own” service. It is common for retailers to buy seasonal produce. Very few handle local meats, cheese, eggs or other products.

Food retailers buy with the market and expect local prices. To be in line with the larger marketplace, understand buyer expectations and prices before agreeing to delivery. Don’t drop price too far or simply because they have a supply and price elsewhere. Many products have been left on the shelf, having to hustle product to other outlets.

The advantage of selling to food retailers is that you can move more volume to fewer buyers, reducing your marketing costs. But the disadvantage is that it is a fickle, price-driven market. Be sure to spread your risks.

OPTION 6: INSTITUTIONAL FOOD SERVICE SALES

Institutional markets are tantalizing, but usually a long-shot. Some schools, nursing homes, hospitals, prisons, etc. can purchase local products. But many are part of a buying consortium and have a single goal: keeping costs low. Meals are often pre-prepped or ready to serve, using few fresh items. Institutional food sales also come with institutional barriers, including federal food safety regulations.

A better strategy to tap institutional markets might be through the distributors who sell to them. By marketing to the middleman and reducing returns, you’ll need to make it work on high volume and low prices.

Some schools are interested in local purchasing to meet Federal regulations. This can often be an effective strategy.

OPTION 7: INTERNET AND MAIL ORDER

A final direct marketing strategy is mail order or Internet sales. If you develop unique, high-value products that are easy to ship, this strategy can complement your other direct marketing efforts. Current customers who love your product can order more and help you market your products through word of mouth. Package and shipping costs need to be considered but for products that are not too bulky, this can be a profitable strategy.

Monika Roth is an Agriculture and Marketing Specialist with Cornell Cooperative Extension’s South Central NY Agriculture Program based in Tompkins County.

13 Strategies to Reduce Direct Marketing Risks

1. Carefully evaluate your options before investing.
2. Grow, pack and deliver quality products.
4. Pick the right size market for the size of your operation.
5. Be intentional about your marketing. Have a written plan.
6. Dedicate yourself to being professional in meeting buying needs.
7. Communicate with customers and exceed their expectations.
8. Be prepared to conform to market place standards.
9. Sell through several complementary marketing channels.
10. Track marketing costs by channel. Know costs and returns for each.
11. If sales aren’t covering costs, change your strategy.
12. Don’t stick with unreliable buyers.
13. Carry adequate product and general liability insurance.

Resource Spotlight: Direct Marketing Books

Contact your local Cooperative Extension office to find out what your state offers in the way of farm business management and marketing advice. Here are some useful publications:


Lesson 1.3: Farmers Markets

Estimated time: One hour.

Overview

Lesson 1.3 will introduce farmers markets as a direct marketing option. Participants will learn who benefits from farmers markets and about the farmers market nutrition program. At end of the lesson is expected that participants will be able to determine if this is a viable marketing alternative to sell their products.

Objectives

1. Learn the steps to follow to sell products in the farmers market
2. Learn the advantages and disadvantages of selling a farmers’ markets
3. Learn strategies to reduce marketing risk at the farmers’ market

Assessment

Participants will be encouraged to actively participate by asking questions and sharing their personal experiences. Participants will take notes on provided handouts and will suggest topics to be addressed in more detail in future presentations.

Equipment, Supplies, and Materials

1. Laptop with Microsoft Office and Projector
2. Power Point presentation Lesson 1.3
3. Handouts for Lesson 1.3 (Farmers Markets) with space for notes
4. Paper and marker to write participants comments
References

# Classroom Procedures

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
</table>
| Slide 1: Welcome          | • If the group is not too large, participants can be asked to introduce themselves and comment on what attracted them to this specific workshop.  
|                           | • Facilitator welcomes the participants and outlines the program and process of the workshop. |
| Slides 2 – 3: Introduction | • Overview of the topic and the objectives of the presentation.         |
| Slides 4 – 8: Farmers’ Market Stats | • Give some statistics about farmers markets and their importance as a direct marketing option to sell farm products  
<p>|                           | • Emphasize that this is a good setting to sell organic products       |
| Slides 9 : Farmers’ Market Popularity | • Explain why farmers markets are becoming popular across the country  |
| Slides 10 : Farmers’ Market Participation | • Ask participants what factors attract people to farmers markets and link them to their popularity |
| Slides 11 : Farmers’ Market Opportunities | • Ask participants what opportunities they see for selling their products at farmers markets |</p>
<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
</table>
| Slides 12 – 15: Farmers Markets as a Direct Marketing Option                         | • Ask participants which steps they believe they should take before becoming a member of a farmers’ market  
• List the ten steps to follow before making the decision of selling at farmers markets  
• Emphasize that producers must like to interact with people |
| Slides 16 – 18: Who Benefits from Farmers Markets?                                   | • Ask participants who they believe benefits from farmers markets  
• List who benefits from farmers markets and explain why |
| Slides 19 – 24: Advantages and disadvantages of Selling a Farmers’ Markets           | • Divide the group in sub-groups (according to the numbers of participants)  
• Ask participants what are the advantages or disadvantages of selling at the farmers markets  
• Ask each group for one advantage and one disadvantage. Write both in a board |
| Slides 25 – 26: Reducing Direct Marketing Risks                                      | • List what strategies producers can use to reduce marketing risk at the farmers’ market |
| Slides 27 – 30: Farmers Market Nutrition Program                                      | • Explain the farmers market nutrition program and its importance as a marketing tool  
• Focus on the ability of some producers to sell organic products through this program |
| Slide 31: More information                                                          | • Inform producers of the associations and institutions that regulate and help to establish farmers markets across the country |
Classroom Procedures Continued

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
<tbody>
<tr>
<td>Summarize presentation</td>
<td>Quick review about:</td>
</tr>
<tr>
<td></td>
<td>- Why farmers markets are a good setting to sell products</td>
</tr>
<tr>
<td></td>
<td>- Main advantages of selling products at the farmers market</td>
</tr>
<tr>
<td></td>
<td>- Main disadvantages of selling products at the farmers market</td>
</tr>
<tr>
<td></td>
<td>- Review the strategies to reduce marketing risk at the farmers market</td>
</tr>
<tr>
<td>Questions?</td>
<td>Answer any specific questions and encourage participants to obtain more information using the links provided in slide 31</td>
</tr>
</tbody>
</table>

Sources of Additional Information

4. Farmers Markets Information [http://us.peeplo.com/search/?q=farmers%20market&type=web&from=adg2](http://us.peeplo.com/search/?q=farmers%20market&type=web&from=adg2)
8. Manage Your Risk [www.manageyourrisk.net](http://www.manageyourrisk.net)
11. To find farmers markets in your state, visit the USDA-AMS website: [www.ams.usda.gov/farmersmarkets/map.htm](http://www.ams.usda.gov/farmersmarkets/map.htm)
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Farmers Markets

Lesson 1.3

Overview

- Introduce farmers markets as a direct marketing option
- Learn who benefits from farmers markets
- Learn about the farmers market nutrition program
- Becoming a member of a farmers’ market

Objectives

1. Learn the steps to follow to sell products in the farmers market
2. Learn the advantages and disadvantages of selling a farmers’ markets
3. Learn strategies to reduce marketing risk at the farmers’ market
Farmers’ Market Stats

- A USDA farmers market study conducted by the Agricultural Marketing Service in 2000 (AMS, 2006) showed that:
  - Farmers markets are an important source of revenue to producers.
  - Farmers markets are self-sustaining (82%).
  - The income generated by farmers markets is sufficient to pay for all costs associated with the operation of the market.

Farmers’ Market Stats

- The study reported that 19,000 farmers sold their produce only at farmers markets.
- 58 percent of markets participate in Women, Infant, and Children (WIC) coupon program, food stamps, local and/or State nutrition programs.
- 25 percent of markets participate in aiding food recovery organizations in the distribution of food and food products to needy families.

Farmers’ Market Stats

- Shaffer and Cox (2005) estimated total sales at farmers markets to be $1 billion for year 2005.
- Same authors indicated that an average sales at individual farmers markets in 2005 totaled about $245,000 or $7,108 per vendor.
- 25 % of vendors surveyed relied on farmers markets as their only source of farm-based income.
Farmers’ Market Stats

- Farmers markets are a form of direct marketing.
- Producers that sell their fruit and vegetables directly to consumers experiment a positive affects in their profits.
- Farmers markets continues to be an important sales outlet for agricultural producers nationwide (AMS, 2009).

Farmers’ Market Stats

- According AMS (2009) approximately 4,700 farmers markets are operating in the United States.

Farmers’ Market Popularity

- Farmers markets have become very popular, mostly due to the growing consumer interest in obtaining fresh products directly from the farm.
- These markets are gaining recognition because they allow consumers to have access to:
  - locally grown food and
  - farm fresh produce
Farmers Markets Participation

- Participation by producers at farmers’ markets depends on several factors, including:
  - a market's popularity,
  - location, and
  - management.
- Customer participation depends primarily on a market's location, since most customers tend to shop at markets close to where they live.

Farmers’ Market Opportunities

- Farmers markets provide two main opportunities to farmers:
  - develop a personal relationship with their customers, and
  - cultivate consumer loyalty
- Additionally, direct marketing of farm products through farmers markets is an important sales outlet for agricultural producers.

Farmers Markets as a Direct Marketing Option

- According to Roth (2007) farmers markets are a good place to develop marketing skills. Before using this direct marketing alternative producers should:
  1. Start by visiting markets in their area
  2. Inventory what is available and note what does not sell out by the end of the day
  3. Differentiate their product
Farmers Markets as a Direct Marketing Option

4. Study their customers by answering the following questions:
   - How many customers are there?
   - What is their ethnicity?
   - Are they young or old?
   - Families or single buyers?
   - Affluent or bargain shoppers?

5. Ask shoppers and sellers what they like and do not like about the market.

Farmers Markets as a Direct Marketing Option

6. Get a copy of the market rules.

7. Enjoy interacting with people.

8. Be willing to invest the time it takes to pick, pack, transport, set-up and sell.

9. Maximize potential returns by growing a wide variety of vegetables or fruits.

10. Consider travel costs and time spent at market as well as growing, harvesting and marketing costs.
Who Benefits from Farmers Markets?

According to AMS (2006) there are many parties that benefit from farmers markets:

- **Small farm operators**: Producers with less than $250,000 in annual receipts (94 percent of all farms) who work and manage their own operations.
- **Farmers**: Farmers have direct access to markets to supplement farm income.

Who Benefits from Farmers Markets?

- **Consumers**: Consumers have access to locally grown, farm-fresh produce and the opportunity to personally interact with the farmer who grows the produce.
- **The community**: Many urban communities where fresh, nutritious foods are scarce gain easy access to food.

Who Benefits from Farmers Markets?

- Farmers markets help to promote (AMS, 2006):
  - nutrition education,
  - wholesome eating habits,
  - better food preparation, and
  - boosting the community’s economy.
Advantages of Selling a Farmers’ Markets

1. It provides a higher price because producers sell their products as a retailer.
2. Price fluctuations are usually reduced or eliminated.
3. Selling directly to consumers reduces the need for packing, which is a substantial cost reduction for producers.

Advantages of Selling a Farmers’ Markets (cont.)

4. Since growers provide all of the steps from producer to the consumer this adds value to their products.
5. As a direct marketing alternative farmers’ markets are appealing in that each grower can specialize in production and not be as involved with marketing activities as the other direct marketing alternatives.

Advantages of Selling a Farmers’ Markets (cont.)

6. A farmers’ market emulates many of the characteristics of a competitive market with numerous buyers and sellers gathered at a central location.
7. Producers are charged only a membership fee for the entire season.
8. Producers can plug into a well established thriving farmers’ market.
Advantages of Selling a Farmers' Markets (cont.)

9. Promotion expenses of farmers' markets are spread over all producers so that per unit advertising costs are generally low.

10. Producers can justify one-on-one why their product is so great.

Disadvantages of Selling a Farmers' Markets

- There are a few disadvantages of selling in farmers markets

1. Probably the biggest one is that producers take all the production and price risks.

2. One-on-one personal skills are required since many customers may want to know how a product was grown.

3. Farmers markets alone may not produce enough sales to generate enough income.

Disadvantages of Selling a Farmers' Markets (cont.)

4. It may take going to several markets a week to generate enough income over the season to make a living.

5. Producer must enjoy interacting with people.

6. Producer must be willing to invest the time it takes to pick, pack, transport, set-up and sell.

7. Producers are charged a membership fee.
Reducing Direct Marketing Risks

- As any other direct marketing alternative there are marketing risks that the producer needs to reduce when selling his/her products at the farmers’ market.
- These are a few strategies to reduce it:
  1. Carefully evaluate options before investing.
  2. Grow, pack and deliver quality products.
  3. Make realistic customer and sales projections.
  4. Have a written marketing plan.

Reducing Direct Marketing Risks (cont)

- Be professional in meeting buyers’ needs.
- Communicate with customers and exceed their expectations.
- Be prepared to conform to market place standards.
- Sell through several complementary marketing channels.

Farmers Market Nutrition Program

- The Farmers Market Nutrition Program (FMNP) is associated with the Special Supplemental Nutrition Program for Women, Infants and Children (WIC).
- This program provides supplemental foods, health care referrals and nutrition education at no cost to low-income pregnant, breastfeeding and non-breastfeeding postpartum women, and to infants and children up to 5 years of age, who are found to be at nutritional risk (AMS, 2007).
According to AMS (2007) the FMNP was established by Congress in July 1992, to:

- Provide fresh, nutritious, unprepared and locally grown fruits and vegetables to WIC participants and
- Expand the awareness, use of and sales at farmers’ markets.

Eligible WIC participants are issued FMNP coupons. These coupons are used to buy fresh, unprepared locally grown, fruits, vegetables, and herbs from farmers at farmers’ markets that have been approved by the State agency to accept FMNP coupons.

During fiscal year 2004, over 2.5 million WIC participants received benefits.

The FMNP is currently authorized in certain areas of 45 States.

According to AMS (2007) 14,050 farmers, 2,548 farmers’ markets, and 1,583 roadside stands were authorized to accept FMNP coupons during fiscal year 2004.

FMNP coupons redeemed for fiscal year 2004 resulted in over $26.9 million in revenue to farmers.
References


References


Sources of Additional Information

Farmers Markets Alliance http://www.seattlefarmersmarkets.org/

Farmers Market Coalition http://www.farmersmarketcoalition.org/


Farmers Market Information http://usa.peapito.com/search/?q=farmers%20market&type=web&from=adg2

How to start a farmers market http://www.gms.usda.gov/AMSv1.0/getfile?dDocName=STELDEV3021296&acct=stddf2

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Sources of Additional Information

http://www.ams.usda.gov/AMSv1.0/getfile?dDocName=STELDEV3002983&acct=wdmgeninfo

Local Harvest http://www.localharvest.org/
Manage Your Risk www.managemyrisk.net
North America Farmers’ Direct Marketing Association http://www.nafdma.com/Public/Welcome/
Resources for Farmers Markets http://www.farmersmarketsusa.org/

Sources of Additional Information

To find farmers markets in your state, visit the USDA-AMS website:
www.ams.usda.gov/farmersmarkets/map.htm
Understanding Farmers’ Market Rules
http://www.ams.usda.gov/AMSv1.0/getfile?dDocName=STELPRDC5060432&acct=wdmgeninfo

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Lesson 1.4: Value Added and Niche Marketing

Estimated time: One hour.

Overview

Lesson 1.4 will help participants to understand the importance of adding value to their fruits and vegetables produce. Participants will learn that there are many ways to add value to fruits and vegetables products and the difference between marketing and selling. Also, participants will learn the distinction between a strategy to capture value and a strategy to create value. At end of the lesson is expected that participants will be able to identify adding value strategies to implement in their own operations as well as niche markets for their products.

Objectives

1. Understand what value added is
2. List ways to add value to fruits and vegetables products
3. Understand current and future fruit and vegetable market trends
4. Recognize the difference between capturing value and creating value
5. Become familiar with the different alternatives to market fruit and vegetables
6. Understand what a niche market is

Assessment

Participants will be encouraged to actively participate by asking questions and sharing their personal experiences. Participants will take notes on provided handouts and will suggest new topics to be addressed in future presentations.

Equipment, Supplies, and Materials

1. Power Point presentation Lesson 1.4
2. Handouts for Lesson 1.4 (Fruit and Vegetable Marketing) with space for notes
3. Paper and marker to write participants comments
References


Classroom Procedures

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
<tbody>
<tr>
<td>Slide 1: Welcome</td>
<td>• Facilitator welcomes the participants and outlines the program and process of the workshop</td>
</tr>
<tr>
<td>Slides 2 – 3: Introduction</td>
<td>• Overview of the topic and the objectives of the presentation</td>
</tr>
<tr>
<td>Slides 4 – 6: Value Added</td>
<td>• Define what value added is</td>
</tr>
<tr>
<td></td>
<td>• Give some examples</td>
</tr>
<tr>
<td>Slides 7 – 8: Future Trends</td>
<td>• List future trends that support the development of value added agriculture</td>
</tr>
</tbody>
</table>
# Classroom Procedures Continued

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
</table>
| Slides 9 – 11: Direct Marketing | • Ask how producers can direct market their products  
• Explain the difference between marketing and selling |
| Slides 12 – 15: Capturing and Creating Value | • Introduce the concept of capturing value; Give examples related to fruits and vegetables  
• Introduce the concept of creating value; Give examples related to fruits and vegetables |
| Slides 16 – 19: Risk | • Introduce the concept of risk (i.e., production and marketing) incurred when adding value to fruits and vegetables  
• Give some examples of both |
| Slides 20 – 30: Alternatives to Market Fruits and Vegetables | • Explain each of the alternatives to market fruits and vegetables  
• Give some examples of how add value to fruits and vegetables for each alternative |
| Slides 31 – 36: Motivations for developing value added products - Activity | • The facilitator can divide the group in sub-groups (according to the numbers of participants)  
• The facilitator should ask participants their motivations for developing value-added products and ask participants for some potential examples  
• Write the top-five or top-ten motivations (at discretion of the facilitator)  
• Compare answers with the study conducted in California |
### Classroom Procedures Continued

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
</table>
| Slides 37 – 38: Niche Marketing   | • Define what a niche market is  
• Give some examples  
• Ask participants for potential niche markets they have identified for their products |
| Summarize presentation            | Quick review about:                                                                                                                        |
|                                   | • What add value is  
• How to add value to fruits and vegetables (hopefully using examples given by participants)  
• Review the concept of risk  
• List the alternatives to market fruits and vegetables  
• What is a nice market |
| Questions?                        | Answer any specific questions and encourage participants to obtain more information using their respective Cooperative Extension Service |

### Sources of Additional Information

1. Alternative Marketing and Business Practices  
2. Center for Rural Affairs – Niche Marketing  
   [http://www.cfra.org/node/236](http://www.cfra.org/node/236)
3. Manage Your Risk  
   [www.managemyrisk.net](http://www.managemyrisk.net)
4. Value Added and Niche Marketing  
   [http://agecon.uwyo.edu/RiskMgt/marketrisk/MARKETValueAdded.htm](http://agecon.uwyo.edu/RiskMgt/marketrisk/MARKETValueAdded.htm)
5. Value Added Fruit Products  
   [http://newfarm.osu.edu/management/value.html#Specialty](http://newfarm.osu.edu/management/value.html#Specialty)
6. VISTA Niche market or an expanding industry? Organic fruit and vegetable production in Canada  
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Value Added and Niche Marketing

Lesson 1.4

Overview

- Help participants to understand the importance of adding value to their fruit and vegetables produce.
- Learn the difference between marketing and selling.
- Learn the distinction between a strategy to capture value and a strategy to create value.
- Be able to identify adding value strategies to implement in your own operations and potential niche markets for your products.

Objectives

1. Understand what value added is
2. List ways to add value to fruits and vegetables products
3. Understand current and future fruit and vegetable market trends
4. Recognize the difference between capturing value and creating value
5. Become familiar with the different alternatives to market fruit and vegetables
6. Understand what a niche market is
The trend of reduced gross agricultural sales for producers has created an interest in value-added enterprises for agriculture.

Producers need to identify agricultural value-added opportunities to increase their profits through further processing.

Producers can add value to their fruits and vegetables by performing activities usually completed by others. In other words, adding value to those products with processing.

According to Born and Bachmann (2006) the value of fruits and vegetables products can be increased in endless ways by:
- packaging,
- processing,
- distributing,
- cooking,
- combining,
- labeling etc.

The value-added goes back to producers not agribusiness processors.

The benefit comes from the value-added activity performed, not by increasing commodity prices.

According to Born and Bachmann (2006) value-added products can open new markets, create recognition for a farm, expand the market season, and make a positive contribution to the community.
Future Trends

- According to Ellerman et al. the future trends that support the development of value-added agriculture are:
  - U.S. fruit and vegetable farming must adopt a model to cooperatively produce products with improved consumer-driven attributes.
  - The focus of the production sector is the manufacturing of goods with value-added, consumer-driven attributes.
  - Food safety and quality control will become driving forces in the food sector.

Future Trends

- Food supply chains will rely on vertical integration and coordination techniques of production, marketing, and/or processing to optimally deliver products with attributes that meet specific user needs.
- In most cases, technology for value-added processing is available.
- The development of organic and functional foods (i.e., substances that may be considered food and provide medical or health benefits) industries based on agricultural products is starting to develop at a rapid rate bringing numerous opportunities for value-added fruit and vegetables products.

Direct Marketing

- Many producers are finding that if they sell their products directly to consumers, it positively affects their profits.
- It does not require substantial capital investments or additional business development.
- It fits into the urban-development trends now occurring in the United States and a consumer-demand trend for healthy food products.
Direct Marketing

- There is growing consumer interest in locally-grown food with information available about where the food came from and how it was produced.
- There are many ways to add value to fruits and vegetables products. Most people think of some form of commodity processing into a more valuable consumer item as the most logical way to add value to commodities.
- This is a long-term approach. It requires the willingness and ability to take on risk, as well as adequate capital, management skills, and personal skills.

Direct Marketing

- Direct marketing does require a change in focus by producers. They have to focus production around their market rather than produce a commodity.
- The underlying concept is that there is a difference between marketing and selling.
- It is possible to add value to products by direct marketing when producers assume the marketing functions traditionally done by others. By doing this, producers become price makers in their market, not price takers.

Capturing Value and Creating Value

- Parcell et al. make the distinction between a strategy to capture value and a strategy to create value.
- Each strategy offers specific opportunities and risks that influence the success or failure of the value-added venture.
Capturing Value

- Capturing value occurs through changes in distribution of value in the food production chain.
- These changes are generally efforts to "capture" more of the consumer dollar.
- Direct marketing, vertical integration, producer alliances and cooperative efforts are often directed toward capturing more of the end-use value of farm production.
- Example: Producers who package or market their berry or tomatoes production directly to consumers.

Marketing directly to the consumer can be done on a small or large scale and in a variety of ways. Options for the producer who enjoys direct contact with consumers include:

- selling at farmers' markets
- selling through community supported agriculture systems
- sales directly to restaurants and local institutions, and
- mail orders and internet sales.

Creating Value

- Creating value occurs with actual or perceived value to a customer for a superior product or service.
- New products, enhanced product characteristics, services, brand names or unique customer experiences may create additional value for farm products.
- Examples:
  - Marketing unique or branded products (Florida's Natural)
  - Combining family activities (pumpkin patches, animal petting, etc.) or recreation associated with direct on-farm product marketing to consumers.
Production Risk

- Production risk from value-added production is often directly related to whether the value is captured or created.
- Production skills and risks are often lower with captured value-added activities because the production processes are generally well-known.
- Example: While producers packaging their products for direct sale to consumers may lack some of the necessary marketing and packaging skills, they usually understand the factors affecting production of their product.

Production Risk

- Creating added value may involve entirely new production practices or require new skills to produce unique goods or services, resulting in considerable added production risk.
- Example: Providing recreational activities increases safety and liability concerns (processing risks) along with activity design and people skills needed to provide enjoyable activities for customers.

Marketing Risk

- Marketing risk may also be influenced by whether value is captured or created.
- Capturing added value is often highly competitive. Integrating into a value chain often requires supplying a substantial volume of production at a competitive cost to the next step in the chain to capture the market position.
- Example: Producers marketing directly to consumers must compete with many other producers as well as supermarkets and other food suppliers.
Marketing Risk

- If created product demand is established, stable and potentially higher prices with limited direct competition may result.
- Example: Each farm creating an activity experience has a unique location and geographic features that usually cannot be duplicated exactly by competition. However, new marketing skills in addition to the new production skills for the product or services are needed.

Alternatives to Market Products

- Direct marketing of fruits and vegetables can describe the market channels that are available to producers. According to Ellerman et al. the alternatives are:
  - Wholesale Market Channel
  - Direct Sales to Restaurants and Retailers
  - Farmers' Markets
  - Roadside Markets
  - Pick-Your-Own
  - Agricultural Entertainment

Wholesale Market Channel

- There are many steps in that market channel, including:
  - picking, cleaning, packing
  - transporting, wholesaling
  - shipping from wholesale to a retail outlet
  - retail sales
Wholesale Market Channel

- The price retailers charge for products are at least two to three times higher than what is paid to the producer.
- Producers can market large quantities of product through this alternative, but their profit margin is very small.
- Because of fluctuating wholesale prices, at times producers sell their products below break-even prices.

Direct Sales to Restaurants and Retailers

- Selling directly to restaurants or retailers eliminates at least two steps in the market channel, which adds to the value the producer receives for the products.
- A producer often also supplies transportation, which can be looked at as value-added service.
- The price received is usually more stable, thus reducing price uncertainty.

Farmers' Markets

- This direct-marketing alternative reduces the need for packing, which is a substantial cost reduction for producers.
- It provides a higher price because producers sell their products as a retailer.
- Price fluctuations are usually reduced or eliminated.
Farmers' Markets

- For this marketing alternative, growers provide all of the steps from producer to the consumer, which adds value to their products.
- Selling through farmers' markets is flexible and is a good alternative for producers getting started in a suitable agricultural alternative or as an outlet for excess production.

Roadside Markets

- This alternative eliminates the need for transportation because products are usually sold on the farm where they are produced.
- Growers provide all of the steps from producer to retailer, which increases the price and reduces price fluctuations and price uncertainty.
- Roadside markets also give producers opportunities to further act as retailers by buying products wholesale and selling them retail.

Pick-Your-Own

- Consumers drive out to the farm, pick the products themselves, and transport those products back to their home.
- The price received at a pick-your-own operation is often very close to the price consumers would pay for those products at a retail level.
Pick-Your-Own

- Consumers are willing to pay that price because of the freshness of the products and the on-farm experience that goes with it.
- Costs for the producer are significantly reduced.
- The value added by this alternative is highest of all the marketing alternatives.

Agricultural Entertainment

- Agricultural entertainment has become one of the most profitable ways to add value to a product and/or farm.
- A few of the opportunities farmers are utilizing to add value to their products and generate income on their farm are:
  - corn mazes,
  - pumpkin patches,
  - school tours, petting zoos,
  - festivals, catered parties etc

- With this market alternative, farmers sell their products but they can also charge admission to consumers who want to participate in the on-farm activities.
Farmers' motivations for developing value-added products

- Ohmart (2003) conducted a case study to look at the value-added enterprises of five small independent farmers in Northern California. Interviews revealed that value-added products significantly enhance farmers' businesses:
  - by affording them a steady income throughout the year and
  - by knowing they have developed a high quality, distinctive and unique product that garners loyal customers

Farmers' motivations for developing value-added products

- In this case study, farmers cited three major reasons for expanding their farming business to include value-added products:
  1. to use excess produce,
  2. to supplement their regular farming income,
  3. to provide an outlet for their creative talents.

Value-added products eliminate waste, use excess produce

- Value-added products is an excellent solution to the waste problem.

- Less than perfect fresh fruit is not valued in today's competitive and cosmetic market. Value-added products provide an excellent use for this extra, less-than-premium-quality produce.
Value-added products add profit and stabilize farm income

- Off-season months present a problem to farmers, especially small farmers who rely on direct marketing.
- By putting their excess produce to good use, they can supplement their regular farm income in the slow season.
- Sometimes lower prices are not due to reduced quality, but to market fluctuations. Value-added products can help smooth out these dips.

The value-added portion of the direct marketing business plays a critical role in the farm's year round income especially during the off-peak winter season.

Value-added products allow control over pricing.

Developing value-added products also gives farmers more control over pricing and sales outlets.

Value-added products afford an outlet for creativity

- According to Ohmart (2003) several farmers emphasized that developing their value-added business affords them a creative outlet.
- The immediate feedback producers get from customers reinforces their motivation to create new products because they can see first-hand when people love a product and want more.
Niche Marketing

- Rainey (2005) defined niche marketing as marketing a product or service in a small portion of a market that is not being readily served by the main stream product or service providers.
- A niche market is the subset of the market on which a specific product is focusing on.
- The market niche defines the specific product features aimed at satisfying specific market needs, as well as the price range, production quality and the demographics that is intended to impact.

Niche Marketing

- According to Rafei and Mullis argue that consumers today are more interested in locally grown produce and in the nutritional value of the foods they eat.
- As the population of Hispanic, Asian, and Middle Eastern natives in the United States continues to grow, more people are looking for fruits and vegetables that are important to their culture and traditions.
- Many of those fruits and vegetables may not be available in a typical American grocery store.

References


References


Sources of Additional Information


Center for Rural Affairs – Niche Marketing http://www.cfra.org/node/236

Value Added and Niche Marketing http://agecon.uwyo.edu/RiskMgt/markettax/MARKETValueAdded.htm

Value Added Fruit Products http://newfarm.osu.edu/management/value.html#Specialty

VISTA Niche market or an expanding industry? Organic fruit and vegetable production in Canada http://dsp-psd.tpsgc.gc.ca/Collection/flatshare21-004-X201-000X200000.pdf

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Lesson 1.5: Establishing a Vendor Agreement with Walmart

Estimated time: One hour.

Overview

Interested producers will learn about the steps involved in establishing a vendor agreement with a Walmart Supercenter or a Walmart Neighborhood Market. This vendor agreement is a requirement for anyone wishing to sell product to Walmart. The steps will be explained successively. Sources of help, particularly from state agricultural specialists, will be highlighted.

Objectives

1) Introduce the seven steps involved in establishing a vendor agreement
2) Consider how to “tell your story” through your product
3) Understand the importance of developing a relationship with your Walmart representative
4) Review the 4 C’s of credit
5) Learn how to establish a credit rating through Dun and Bradstreet

Assessment

Participants will view the presentation on the vendor agreement and DUNS credit rating processes and interact throughout by responding to questions asked by the instructor and by being given the opportunity to offer their own questions and comments. They will follow along with the examples outlined in the presentation to learn the basic steps of the agreement process and how to fill complete the DUNS application and read a credit report.

Equipment, Supplies, and Materials

1. Power Point presentation Lesson 1.5
2. Notes pages Lesson 1.5
3. Handouts: Dun and Bradstreet Credit example
## References

1. Dun and Bradstreet Credit Bureau [www.dnb.com](http://www.dnb.com)
2. Personal communications with Walmart Home Office.

## Classroom Procedures

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lead discussion to assess previous knowledge.</td>
<td>• Is anyone aware of Walmart’s efforts to purchase local products?</td>
</tr>
</tbody>
</table>
| Slide 2-4: Introduction | • Discuss new and emerging markets for agricultural products.  
• Discuss Walmart’s objective  
• Briefly state the objectives of the presentation |
| Slides 5: Vendor agreement introduction. Take time for basic questions at the end of the slide | • Participants need to understand that Walmart requires anyone who wants to sell to a Supercenter or to a neighborhood market to have a vendor agreement  
• It is very important to stress that the existence of a vendor agreement does not obligate a producer to sell product to Walmart. Nor does it obligate Walmart to purchase product from a producer.  
• This presentation provides basic information for the producer to determine whether or not beginning the vendor agreement process is right for his or her business. Is there a unique story to tell about this product? |
| Slide 8: Step Two: Supplier Questionnaire | • The Vendor agreement process includes the completion of a number of questionnaires.  
• Filling out the questionnaires as completely and accurately as possible will help move the questionnaire through the system in a more timely manner than one that is incomplete or inaccurate. |
## Classroom Procedures Continued

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
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</tr>
</thead>
</table>
| Slides 9-10: Step Three: Credit Rating. Inform producers that this step will be reviewed in greater detail later in the presentation | • Walmart requires every vendor to have a Dun and Bradstreet Credit rating.  
• The first step in getting that rating is to apply for and receive a unique DUNS number for the company.  
• The application for the DUNS number can be made on line or over the phone. |
| Slides 11-12: Step Four: Product Liability Insurance                                  | • Product liability insurance is required by Walmart. It provides a level of safety for both Walmart and the producer.  
• Walmart requires different levels of liability insurance depending on the product. According to a recent contract, that value generally is $2M but can be as high as $5M.  
• Producers will need to check with Walmart for latest liability insurance requirements.  
• Liability insurance is costly. Producers will need to find appropriate vendors of such insurance in their own states. Lists may be available from their banker, from Farm Bureau or the Cooperative Extension Service. |
| Slide 13: Step Five: Food Safety Questionnaire                                        | • Walmart’s questionnaire asks (among other things) questions about a producer’s food safety procedures that are already in place. |
| Slide 14: Step Six: Food Safety Audit                                                | • Walmart has their own list of approved food safety auditors in each state. All vendors must obtain an audit from one of those on the list. A food safety audit through another party is generally not acceptable.  
• Audits are only good for one year, they must be renewed annually.  
• Audits must be done at harvest and packaging. Therefore producers should begin this vendor agreement process at least one season before they wish to sell to Walmart. |
### Classroom Procedures Continued

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
<tbody>
<tr>
<td>Slide 15: Step Seven: Sign Vendor Agreement</td>
<td>- Walmart personnel will work with the producer through this step.</td>
</tr>
<tr>
<td></td>
<td>- It is important that the producer work to establish a good relationship with his or her Walmart contact.</td>
</tr>
<tr>
<td>Slides 16-19: Important Features and Summary</td>
<td>- Working with Walmart may offer a profitable marketing strategy for the producer. However the producer must understand all risks of entering into any new market.</td>
</tr>
<tr>
<td>Slides 20-24: Four C’s of Credit</td>
<td>- These slides are meant to provide a very brief overview of the Four C’s of credit. More information can be found in other lessons throughout this guide.</td>
</tr>
<tr>
<td>Slides 25-33: The DUNS application process</td>
<td>- Walk the producer through the online process of completing an application</td>
</tr>
<tr>
<td></td>
<td>- The application has four brief steps that all businesses must complete.</td>
</tr>
<tr>
<td>Slides 34-36: Four Levels of Application</td>
<td>- Dun and Bradstreet offers four different levels of application.</td>
</tr>
<tr>
<td></td>
<td>- The free option provides a DUNS number to a business within thirty days. According to D&amp;B representatives, this option is generally suited for those who need a government credit rating to apply for federal grants.</td>
</tr>
<tr>
<td></td>
<td>- A business can select the $49 option that provides this same level of service in 5 business days.</td>
</tr>
<tr>
<td></td>
<td>- The Basic service currently costs $149 and offers the creation of a business file that gives the producer access to his or her report.</td>
</tr>
<tr>
<td></td>
<td>- The basic plus option offers the above and also the opportunity to provide six credit references that allows you to establish your credit history quicker and (hopefully) improve the predictability of your credit score.</td>
</tr>
<tr>
<td></td>
<td>- This lesson does not recommend any particular option. Producers should talk to both Walmart and Dun and Bradstreet to determine the option that is best for his or her business.</td>
</tr>
</tbody>
</table>
Teaching Procedures

<table>
<thead>
<tr>
<th>Handouts: Example of a Dun and Bradstreet Credit Rating</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Review with the participants the example credit rating created for a fictitious company in California.</td>
</tr>
<tr>
<td>• Point out the credit score and how to compare himself to others.</td>
</tr>
<tr>
<td>• Example the factors that influenced the score.</td>
</tr>
<tr>
<td>• Challenge producers to identify ways this company could improve its credit score.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Slides 37-38: Interactive Cooperative Extension Service Locator Map</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Displays how a producer can find his closest cooperative extension service office. Washington County, AR is used as an example.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Wrap Up</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Address any remaining questions</td>
</tr>
<tr>
<td>• Provide contact information</td>
</tr>
</tbody>
</table>

Sources of Additional Information

1. Dun and Bradstreet Credit Bureau
   For an application and more information regarding this process, visit the D&B website at http://www.dnb.com/US/duns_update/.

2. Food Liability Insurance Information

3. Link to Cooperative Extension System Nationwide

Contact Information

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Division of Agriculture
479-575-2279
jhpopp@uark.edu
Case Study Handout

Participants will receive copy of the Dun and Bradstreet Credit Scoring Report downloaded from http://support.dialog.com/searchaids/dialog/pdf/dnbcsr.pdf. This handout describes the key feature of the report as well as offers a sample report for a fictitious company.
Establishing a Vendor Agreement with Walmart

Lesson 1.5

Overview

Thanks to increased demand by consumers for fresh, local foods, agricultural producers have access to new marketing options.

These options include marketing to institutions (schools, restaurants, hospitals) and selling directly to food retailers.

Walmart states, “By supporting locally grown programs, it gives Walmart customers the opportunity to support local farmers and their local economies, provide high quality and low-priced fruits and vegetables. Walmart is committed to purchasing more agricultural products from small local growers and reducing its environmental footprint by decreasing greenhouse gas emissions, conserve fuel and reduce the number of food miles between farm to fork.”

This lesson is intended to provide basic information to those nationwide who want to explore establishing vendor status with Walmart Super Centers and Neighborhood Markets.
Objectives

1) Introduce the seven steps involved in establishing a vendor agreement
2) Consider how to “tell your story” through your product
3) Understand the importance of developing a relationship with your Walmart representative
4) Review the 4 C’s of credit
5) Learn how to establish a credit rating through Dun and Bradstreet
6) Learn how to find their closest cooperative extension service office

What is a Vendor Agreement?

- A vendor agreement provides the opportunity for a producer to sell products to Walmart.
- An agreement does not create an obligation for Walmart to purchase goods.
- In order to sell to Walmart, you must first establish a vendor agreement.
- There are seven steps to establish a vendor agreement.

Step 1: Contact Local Store Manager

- Producers must first contact the manager of their local Super Center or Neighborhood Market.
- A face to face will be set among the producer, the store manager and a Market Grocery Manager (MGM).
  - The MGM is similar to a district manager who oversees a group of stores in a given area.
Step 1: Contact Local Store Manager

- During this meeting the producer offers information related to his product.
  - variety
  - quantity of product expected to be produced
  - length of production season
  - consumer demand for the product
- Ask yourself: why should Walmart want to sell my product?
- If the store manager and MGM are interested in the product, the producer moves to step two.

Step 2: The Supplier Questionnaire

- All potential vendors must complete a questionnaire.
- This questionnaire requests information related to the product, the time frame for product delivery and the name of the store(s) the producer wishes to supply.
- Once signed by all parties, the questionnaire is mailed to a Walmart office for processing.

Step 3: Request a Dun and Bradstreet Credit Rating

- Creditworthiness is an essential requirement for conducting business with Walmart. While the questionnaire is under review, the producer should acquire a Dun and Bradstreet (D&B) credit score.
- D&B is the largest credit bureau in the world. D&B uses a set of criteria (including loan repayment history, supplier payment history, lawsuits and judgments against a company as well as other factors) to determine a business’s credit rating.
Step 3: Request a Dun and Bradstreet Credit Rating

- To establish a credit rating, a producer must apply for a Data Universal Numbering System (DUNS) number from D&B.

- Depending on the service acquired, the process can take 30 to 60 days.

- Walmart will receive a copy of the score. If the score fits the criteria the producer is told he must obtain product liability insurance.

Step 4: Obtain Product Liability Insurance

- Product liability insurance can help protect businesses against claims related to the sale of food (and other items) to the public.

- Food product liability coverage is a type of insurance designed for food product manufacturers and processors. It is designed to help protect the food supplier (in this case the producer) in cases where the food product causes injury or other harm to the consumer.

- Insurance providers evaluate many factors related to the business in order to determine the insurance premiums.
  - These factors can include gross sales, coverage requested, type of product, type of market, prior claims against the business, among others.

- Availability of insurance as well as premiums for liability coverage vary widely from state to state.

- Contact insurance providers in your state for more information regarding coverage and premiums.
Step 5: The Food Safety Questionnaire

- This step begins with the completion of a food safety questionnaire.
- Questions include information about your operation, types of production, production facilities, and any existing food safety procedures, good manufacturing procedures, recall traceability procedures and pest management programs among other things.

---

Step 6: Obtain Third Party Food Safety Audit Certification

- Four important points:
  - Walmart requires the use of one of their approved certifiers. There are a limited number of Walmart approved certifiers in any state. Allow sufficient time for the audit.
  - This audit must be conducted during harvest and packing.
  - Third, an audit is good for one year (for example, August to August).
  - Walmart requires that the audit be conducted each year to maintain vendor status.

---

Step 7: Complete the Vendor Agreement

- During this step of the process the last set of documents are completed, corrected and finalized.
- If a producer is successful in securing an agreement, a paper vendor agreement is sent to the producer. Walmart’s Supplier Development will review and process the application.
- As a new Walmart vendor in some areas of the country, the producer will receive access to the Walmart Retail Link Database.

---
Important Features of this Agreement Process

- An agreement does not create an obligation for Walmart to purchase goods. This is the start up process where Walmart works with the vendor to identify the niche market, establish the vendor’s program and grow it where relevant.
- Walmart agreements run for one year. Both Walmart and the producer have the option to decline an agreement in following years.

Important Features of this Agreement Process

- Walmart policy is not to purchase more than 25% of a producer’s overall business (value of sales). In other words, Walmart could purchase 100% of a producer’s tomatoes, but only if those tomatoes make up 25% or less of the value of all of his agricultural sales.
- Pricing is negotiated before the start of the growing season; short of unforeseen circumstances, prices remain constant throughout that growing season.

Important Features of this Agreement Process

- The initial agreement process can take time.
  - Credit rating establishment
  - Food safety audit
- Producers may consider initiating this process the season before wishing to market to Walmart.
Final Thoughts

- Marketing directly to local retailers can provide profitable alternatives to marketing through other channels. However, they may also introduce new risks and costs.
- Before engaging in any new marketing option, producers should fully re-evaluate their marketing strategies and update their business plan.
- Contact your local cooperative extension service office (or in Arkansas, www.uaex.edu) for assistance.

Four C’s of Credit

- Character
- Capacity
- Capital
- Conditions

Character

- Character
  - size, location, number of years in business, business structure, number of employees, history of principals, appetite for sharing information about itself, media coverage, liens, judgments or pending law suits, stock performance, and comments from references.
Capacity

- Capacity
  - the cash flow
  - the structure of the company’s debt (secured or unsecured)
  - existence of line(s) of credit, particularly if not used
  - existence of any defaults

Capital

- Capital
  - existence of financial resources that allows business to repay creditors assesses whether a company has the financial resources
  - looks closely at balance sheet information including working capital, net worth and cash flow
  - very important part of the credit report

Conditions

- Conditions
  - external factors surrounding the business under consideration
  - market fluctuations, industry growth rate, political/legislative factors, and currency rates
Establishing a D.U.N.S Number

- The D-U-N-S number is a unique nine-digit identifier for a business.
- This number is established through Dun and Bradstreet.
- Application can be made one of two ways:
  - On line
  - On the phone

On-Line Application Process

- Search first for existing rating.
- If none exists, complete the four step application on line or by phone.
- Choose the level of service appropriate for your business.
Four Levels of Application

- **Free in 30 Days**
  - mainly for those needing a government rating (applying for federal grants) provides number only.

- **$49* in Five Days**
  - also mainly for those needing a government rating provides number only.

---

Four Levels of Application

- **Basic Coverage - $149***
  - receive a DUNS number in 24 hours
  - creation of basic D&B file in 5 business days that helps establish your company’s credibility
  - access to your company’s file to understand how business partners are making decisions on your company

---

Four Levels of Application

- **Basic Plus - $499***
  - ability to submit up to 6 credit references in the first month (30 days) of your service to D&B for verification of your payment history to start establishing your company's D&B PAYDEX score and potentially improve the predictiveness of your other D&B scores and ratings

- Visit Dun and Bradstreet on line or by phone to determine the level of service appropriate for your business.

---

*As of November 2009*
Sources of Additional Information

- Dun and Bradstreet Credit Bureau
  - For an application and more information regarding this process, visit the D&B website at: [http://www.dnb.com/US/duns_update/](http://www.dnb.com/US/duns_update/)

- Food Liability Insurance Information

- Link to Cooperative Extension System Nationwide
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![Walmart](walmart.png)

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Dun & Bradstreet
Credit Scoring Report®

See also: D&B BBR, D&B BIR, D&B CR, D&B PAR, and D&B SER

In fast moving markets, a credit application held in review can become a customer lost to the competition. But a quick decision that’s wrong can hurt your bottom line. The D&B Commercial Credit Scoring Report predicts the likelihood of a company paying in a delinquent manner (90+ days past terms) during the next 12 months based on the information in D&B’s file.

Applications

Using this report, you can make faster credit decisions. The score helps you decide quickly whether to accept or reject accounts, adjust terms or credit limits, or conduct a more extensive review based on the report D&B provides. You can also learn how the company’s relative ranking among other businesses in the D&B database. It’s the perfect tool to help you manage a high volume of small to medium dollar accounts, so you can accelerate your credit decision process.

Key Features

The report offers effective tools to evaluate a business, including:

Company Overview: Our unique D&B D-U-N-S Number links key information on any company in D&B files. This summary provides a company’s name, address, net worth, size and date of current management’s control, as well as other valuable information.

D&B Commercial Credit Score Findings: We have included a number of ways you can evaluate risk:

- The 1-100 Credit Score Percentile-shows you where the company ranks among businesses in the D&B information base.
- The Credit Score Class-separates businesses into five classifications.
- The 101-670 Credit Score-predicts the likelihood of an account paying in a delinquent manner (90+ days past terms) during the next 12 months based on information in D&B’s file.

Commercial Credit Analysis: Highlights significant information that has had an impact on the score can include slow payment(s), overall financial strength and net worth, age of the business, and the presence of suit(s), lien(s), and/or judgment(s) in D&B files.

D&B PAYDEX® Score: Gives you an instant overview of how a firm pays its bills as reported to D&B. An industry D&B PAYDEX is also provided, when available, so that you can compare the company to other companies in its industry.

Credit: Average high credit and highest credit granted (as reported to D&B) put your risk in size perspective.

Special Events: Identifies major changes or significant activities D&B recently learned of. This section can note situations such as fire or a burglary that may adversely affect a company, or situations like expansion plans, which may indicate an opportunity.

Sample Credit Scoring Report (CSR)
The sample report below represents the type of information available to you. Not all reports will contain all of these sections or all of this information.

Do not confuse with other Gorman Companies, this is a fictitious company used by D&B for demonstration purposes.

COPYRIGHT 2001 DUN & BRADSTREET INC. - PROVIDED UNDER CONTRACT FOR THE EXCLUSIVE USE OF SUBSCRIBER 000-00002.

ATTN.: JOE SMITH

DUN & BRADSTREET COMMERCIAL CREDIT SCORING REPORT

DUNS: 00-007-7743 DATE PRINTED: OCT 01 2001
GORMAN MANUFACTURING BUSINESS SUMMARY
AND BRANCH(ES) OR DIVISION(S)

CONTROL: 1990
492 KOLLER STREET START: 1984
SAN FRANCISCO, CA EMPLOYS: 16
TEL: 415 000-0001 NET WORTH: $(450,000)
CEO: Leslie Gorman, President SIC: 27 52
LOB: COMMERCIAL PRINTING

COMMERCIAL CREDIT SCORE

The Commercial Credit Score predicts the likelihood of a firm paying in a delinquent manner (90 + Days Past Terms) during the next 12 months, based on the information in Dun & Bradstreet’s file. The score was calculated using statistically valid models derived from D&B’s extensive data files.

DECISIONMAKER (TM) RECOMMENDATION
CREDIT GUIDELINE:
APPROVE UP TO $5,000

CREDIT SCORE CLASS (0 - 5): 4 - SIGNIFICANT RISK
CREDIT SCORE PERCENTILE: 15
(Highest Risk: 1; Lowest Risk: 100)

The Credit Score Percentile above means this firm scores the same as or better than 15 percent of the businesses currently available in D&B’s Information Base.

COMMERCIAL CREDIT SCORE: 410
(Highest Risk: 101; Lowest Risk: 660)

INCIDENCE OF DELINQUENT PAYMENT AMONG
Companies with Scores 401-440: 19.8%
All Firms in D&B’s Files: 16.6%

AVERAGE HIGH CREDIT: $ 3,360
HIGHEST CREDIT: $ 42,000

# TRADE EXPERIENCES: 5
PAYDEX SCORE/INDEX - FIRM: 67 - 18 Days Beyond Terms
PAYDEX SCORE/INDEX - INDUSTRY: 77 - 5 Days Beyond Terms

Your DecisionMaker (TM) Recommendation is based on the criteria selected by your company.

COMMERCIAL CREDIT ANALYSIS

The Credit Score is based on the following are prioritized factors in addition to other information in D&B’s files.

- 18% of trade experiences indicate slow payment(s) are present.
- Payment information indicates negative payment comment(s).
- Payment experiences exist for this firm which are greater than 60 days past due.
- Evidence of open suit(s), lien(s), and judgment(s) in D&B database.
- D&B files indicate a negative net worth of $(450,000).

INDICATIONS OF SLOWNESS CAN BE THE RESULT OF DISPUTES OVER MERCHANDISE, SKIPPED INVOICES, ETC.

THE PUBLIC RECORD ITEMS REPORTED MAY HAVE BEEN PAID, TERMINATED, VACATED, OR RELEASED PRIOR TO THE DATE THIS DATA IS TRANSMITTED.

=================================================================

SPECIAL EVENTS

The following Special Events are present on this case and may not be reflected in the above score.

01/01/96 According to published subject experienced a fire at their main warehouse facility on Koller Street.

=================================================================

For additional information on this company, you may order other D&B products or Investigative Services.

END OF DUN & BRADSTREET COMMERCIAL CREDIT SCORING REPORT
(c) 2002 Dun & Bradstreet, Inc.

To Order Special Reports

REPORT S1/CSR/1-2 OR REPORT DN=XX-XXX-XXX/CSR
(Where the X series represents the DUN’s number)

For More Information

Contact D&B Customer Support Center at 1-800-234-3867 for further information or for help in your search strategies. Or call Dialog Customer Support at 1-800-334-2564 or in the U.K. call +44-61-455-5119.
Lesson 1.6: Marketing to Restaurants and Retailers

Estimated time: One hour.

Overview

Many restaurants and grocers or other types of food retailers have an interest in carrying local products for myriad reasons. Many of these direct marketing channels are pressured by consumer demand to carry local products. This lesson provides an introduction to entering this popular direct marketing venue and how to keep your customers happy, returning, and recommending you to other foodservice establishments.

Objectives

1. Be able to identify attributes of your operation that differentiate you from traditional suppliers and exploit these attributes.
2. Identify your obstacles to supplying restaurants or retailers.
3. Be able to identify attributes of potential customers to increase your attractiveness as a supplier.
4. Learn how to approach restaurants or retailers and maintain long term relationships.

Assessment

There is no homework or in class examples. The handout “Selling Directly to Restaurants and Retailers” will be explored in class.

Equipment, Supplies, and Materials

1. Power Point presentation Lesson 1.6
2. Handout “Selling Directly to Restaurants and Retailers”
References


Classroom Procedures

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
</table>
| Slides 2-3: Introduction | • Go over overview and objectives.  
| | • Lead discussion to assess who is already in venue and who are potential suppliers.  
| | • Assess knowledge of subject |
| Slide 4: Considerations before entering restaurants and retailers | • Do not want producers to enter if they are not interested in the customer relationships required or do not have the time or supply to meet demand.  
| | • Not everyone is a good candidate for supplying restaurants or retailers. |
## Classroom Procedures Continued

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
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</table>
| **Slide 6: Risk management** | • One bad experience with your product is enough to lose that customer because there are alternative sources  
• Most purchases are spot market – you and the customer usually don’t have a long-term contract except in special circumstances.  
• Carefully choose your customers – you make the initial contact usually.  
• Do not expose yourself to potential losses from unscrupulous customers. |
| **Slide 7: Distribution and delivery** | • Times that are convenient for both parties are paramount to having a good experience.  
• Restaurants tend to need smaller, more frequent deliveries than grocers or retailers.  
• Many issues and hidden costs involved with delivery that must be taken into account in both time management issues and price of the products.  
• Inconvenient distribution or inability to deliver is frequently cited as a drawback to sourcing local produce. |
| **Slide 9: Pricing competitively** | • Base price on your costs, competitors’ prices, and your product’s value and differentiating characteristics  
• Although most times local products command a premium, passing on savings to your customers can build a good reputation.  
• Undercutting other producers also makes you look unscrupulous to other local producers. |
### Classroom Procedures Continued

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
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</thead>
<tbody>
<tr>
<td><strong>Slide 10: Pricing competitively</strong></td>
<td>• Explore ways to offer low cost options to your customers without sacrificing quality or safety.</td>
</tr>
<tr>
<td></td>
<td>• Seconds are only marketable if they are still safe to eat and taste like your top quality products.</td>
</tr>
<tr>
<td></td>
<td>• “Value” is not easily measured in dollars. Use good judgment to price based on product value – undervaluing may falsely imply inferior quality, but overvaluing will quickly drive away customers.</td>
</tr>
<tr>
<td><strong>Slide 11-12: Pricing based on customer attributes</strong></td>
<td>• Be able to identify your customer based on the type of establishment</td>
</tr>
<tr>
<td></td>
<td>• Be able to identify your customer based on their buying criteria – quality or price based.</td>
</tr>
<tr>
<td></td>
<td>• Once you identify customer attributes, you can offer more relevant products at attractive prices tailored for that customer.</td>
</tr>
<tr>
<td><strong>Slide 13: Arm yourself with information</strong></td>
<td>• You must convince your potential customer that buying from you – a local producer – is a smart and profitable move for their business.</td>
</tr>
<tr>
<td></td>
<td>• What do their customers want?</td>
</tr>
<tr>
<td><strong>Slide 14: Chain retailers or restaurants</strong></td>
<td>• Some chain businesses have local buying programs or the franchise owner has a say in what products the business carries.</td>
</tr>
<tr>
<td></td>
<td>• Chains may have local or regional managers for your area who can circumvent traditional national distributors due to the demand for local foods.</td>
</tr>
<tr>
<td><strong>Slide 15: Contacting the potential customer</strong></td>
<td>• It is easier for you to seek out customers than waiting for a business to contact you.</td>
</tr>
<tr>
<td></td>
<td>• Marketmaker is making it increasingly easy for restaurants or retailers to find suppliers of local foods.</td>
</tr>
<tr>
<td><strong>Slide 16: Hours for appointments</strong></td>
<td>• Some restaurants are only open for dinner or may close between lunch and dinner. Many take deliveries only when they are not busy – before lunch or in between lunch and dinner.</td>
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</tbody>
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### Classroom Procedures Continued

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<td>Slide 16: Hours for appointments</td>
<td>- Some restaurants are only open for dinner or may close between lunch and dinner. Many take deliveries only when they are not busy – before lunch or in between lunch and dinner.</td>
</tr>
</tbody>
</table>
| Slide 17: Marketing your product | - Make sure you are prepared to share the story and philosophy of your operation so the contact can relate to you on a personal level – this intimate quality can differentiate your products from the traditional distributor.  
- On the other hand, always conduct business in a professional manner.  
- Some contact persons may be reluctant to buy new products or change their buying habits, so you must find persuasive arguments: customer demand, inability to get products anywhere else, etc. (from “Why buy local” slide 17).  
- Recipes and serving suggestions are key to supplying a new product.  
- Tasting your products and knowing you will be a reliable and punctual supplier is paramount to your success. |
| Slides 18-20: Maintaining long-term relationships | - Keep your customers happy in the long run by offering products they specially request.  
- Contracts could be used if you are growing a specific quantity of product for an existing customer. Make sure you do business with reliable customers.  
- A good reputation can promote your business to other potential customers in all types of direct marketing venues.  
- Do not cooperate with other producers to supply your customers whom you do not trust: some may try to move into your customer base, undercut you, or be unreliable sources. |
Sources of Additional Information

1. Selling Directly to Restaurants and Retailers.


   http://www.uky.edu/Ag/NewCrops/marketing/restaurants.pdf

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Marketing to Restaurants and Retailers

Lesson 1.6

Overview

- Many restaurants and grocers or other types of food retailers have an interest in carrying local products for myriad reasons.
- Many of these direct marketing channels are pressured by consumer demand to carry local products.
- This lesson provides an introduction to entering this popular direct marketing venue and how to keep your customers happy, returning, and recommending you to other foodservice establishments.

Objectives

1. Be able to identify attributes of your operation that differentiate you from traditional suppliers and exploit these attributes.
2. Identify your obstacles to supplying restaurants or retailers.
3. Be able to identify attributes of potential customers to increase your attractiveness as a supplier.
4. Learn how to approach restaurants or retailers and maintain long term relationships.
Consider Your Qualities and Needs

- Is selling your products to restaurants or retailers going to be profitable for your operation?
- How many locations can you service?
- Do you enjoy working directly with your customers and have the time and desire to provide adequate service?
- Will you be able to deliver your products?
- What price do you require to cover labor and production costs?
- Is there a demand for local products through restaurants or retailers in your area?

Attributes of An Attractive Supplier

- Honesty and integrity
- Good customer relations – ordering, product follow-ups
- Product quality, consistency, quantity, and safety
- Product variety and specialty products
- Competitive pricing
- Uncomplicated business transactions and payment systems
- Accessible communications
- Reliable and punctual distribution and/or delivery system
- Most attractive products are produce and meat

Risk Management

- Do not deliver an inferior or poor quality product
  - Your customers are paying for high quality
  - Quality is the most important attribute to expand customer base
  - You have competition
  - Usually not a contract, except in long term orders from restaurants or for a period at a retailer
- Is the customer a reliable business associate?
  - Some pay upon delivery, monthly, or weekly
  - Reduce your risk of default accounts or late payment
  - Be wary of extending credit, especially to new businesses.
Transportation Logistics

- Be **reliable** and **punctual** in distribution
- Create a regular schedule and system for delivery or pick up
- Some locations may require orders every couple of days, but others only weekly
- Inform your customer with plenty of notice if you can not fill their order
- Keep complete detailed records of quantities, dates, and what was delivered for both parties’ benefit
- Many restaurants and retailers prefer delivery; some require it

Issues With Delivery

- Before agreeing to delivery, ask yourself:
  - Can you deliver products punctually and economically?
  - How far do you live away from customer?
  - How many deliveries can you make in one trip while conforming to the customer’s schedule?
- Customer pick up results in lower prices for the customer
  - Cost of transportation
  - Cost of your time
- You can offer pick up at the local farmers’ market to save both parties a special trip

Pricing Your Products Competitively

- Must recoup production, labor, and delivery costs
- Must be competitive with alternative suppliers’ prices
  - Local producers can sometimes command a premium above market wholesale – 5 to 25% higher
  - Local producers may also be able to produce and deliver at a lower cost than market, so these savings are passed on to customers
- Do not undercut other producers severely – this practice will result in a decrease in profit or even a loss due to fixed production costs
Pricing Your Products Competitively

- You can offer products at lower prices by offering farm pick-up instead of delivery
  - Will not include the cost of transportation or your time
  - Pick up may be less attractive if your operation is far away from your customers
- Price produce "seconds" with cosmetic defects at a lower point and offer them to your customers as ingredients since they aren’t as aesthetically pleasing
- "Value" of your product can increase price: differentiating characteristics are in the eye of the customer, so identify your product's characteristics and market them

Pricing Based on Customer Attributes

- Retailers
  - May require larger quantities per delivery
  - May expect a volume discount (lower price per unit)
  - Accustomed to market price fluctuations
- Restaurants
  - May require smaller quantities more frequently
  - Will pay a higher price per unit
  - A spot market – usually no contract buying

Pricing Based on Customer Attributes

- Price sensitive buyers
  - May have no interest in your product if a lower cost option exists
  - May have no interest in specialty products
  - May not value differentiating characteristics monetarily
- Quality sensitive buyers
  - May require special packaging or labeling
  - May have no interest in your low price if your product does not meet their specifications
  - May place a monetary premium on the "value" of your product
Why Buy Local?

- Local foods tend to be fresher and of better quality
- Can procure specialty products not usually available
- Customer demand for local products – especially at fine dining restaurants or specialty grocers
- Accountability and product knowledge
- Food safety – buyers or chefs may view local foods as safer because they know where it was grown and exactly how it arrived in their store or kitchen
- According to a University of Nebraska – Lincoln survey, 73% agreed that purchasing local foods has been a profitable move for their foodservice establishment
- Supports local economy and keeps money within locale

Chains vs. Locally Owned

- Chain establishments
  - May prove to be more difficult markets for local producers to enter
  - May only be able to purchase through their distribution centers
  - Ask if they have a local purchasing program
  - Ask how many locations you would have to supply
- Locally owned establishments
  - More likely targets
  - Owners have autonomy
  - You have to supply one or very few locations

Contact Potential Customers

- Restaurants
  - Owner
  - Kitchen manager
  - Chef/ sous chef/ pastry chef
- Retailers
  - Owner
  - Manager
  - Produce/ deli manager
- It is important for you to make the initial contact: it is much easier for you to find restaurants than for them to find you.
Preparing For The Initial Approach

- Research the establishment:
  - Existing products
  - Target market
- Make an appointment ahead of time.
- The best hours to visit foodservice establishments may be different than other businesses:
  - At retailers, buyers or store managers usually work normal business hours.
  - At restaurants, owners/chefs are usually most available in the afternoon
- Prepare a price list ahead of time

The Initial Meeting

- Bring fresh samples of the products you have to offer to taste; recipe and pairing suggestions are helpful.
- Discuss your operation:
  - Make their relationship with you personal
  - Direct them to your website
  - Invite them to your farm
- Market your product:
  - Differentiating qualities and availability
  - Why is your product a profitable addition or substitution?
  - Shelf life, transportation logistics, packaging

Long Term Evolution of Relationship

- Long term relationships can be beneficial to your operation in the long run:
  - You have a guaranteed buyer for a certain quantity
  - You can grow specific quantities or a larger variety of products demanded by your existing customers
  - Orders before planting enable you to guarantee that you can meet all of your customer’s needs
  - You can offer a special product the customer is unable to procure easily at a reasonable price
- An existing relationship can help your business survive setbacks, such as weather or pest related crop failures
**Long Term Evolution of Relationship**

- Provide seasonal updates to entice existing customers to expand their demand to other products.
  - Seasonality may not be an issue for restaurants that have seasonal menus.
  - Customer may have to source products from non-local suppliers to meet off season demand.
- Word-of-mouth recommendations from existing customers can result in new business for your operation.
- Work with other producers to keep your customers happy: recommend suppliers of products you do not offer.

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**Long Term Evolution of Relationship**

- Offer existing customer samples of other products periodically to interest them in increasing their order size or variety.
- Discover your customer’s needs and preferences in order to offer relevant new products to them.
- Menu or sign mentions of your farm’s name may help you expand your customer base elsewhere – such as through the farmers’ market.

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**References**

Approaching foodservice establishments with locally grown products.  
[http://digitalcommons.unl.edu/cgi/viewcontent.cgi?article=1000&context=fpcreports](http://digitalcommons.unl.edu/cgi/viewcontent.cgi?article=1000&context=fpcreports)

Marketing fresh produce to restaurants.  
[http://www.uky.edu/Ag/NewCrops/marketing/restaurants.pdf](http://www.uky.edu/Ag/NewCrops/marketing/restaurants.pdf)

Selling directly to grocery stores and restaurants.  

Selling directly to restaurants and retailers.  
References

Selling strategies for local food producers.  

Selling to restaurants.  

The ABCs of marketing to restaurants.  
http://www.prideoftheprairie.org/potp-old/producefactsheet.pdf

Working with retail buyers.  

Sources of Additional Information

Bringing local food to local institutions.  

Arkansas farm to school programs.  
http://www.farmtoschool.org/AR/programs.htm

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In November, 2002, more than 50 growers, agricultural professionals, and others gathered in the beachside town of Ventura as part of the California Farm Conference, to discuss how to market directly to restaurants and retailers. During a half-day short course led by Kris Pustina, a successful and innovative restaurateur in Ventura, and Mark Mulcahy, well-known marketing consultant, participants discussed the key elements for creating a successful, entrepreneurial relationship with local restaurants and retailers. The group also compiled a list of people, organizations and resources for future information and assistance. This leaflet summarizes the results of the group discussion in a question/answer format. Key contacts are listed at the end.
In a small group discussion format, all participants developed answers to the following critical questions about strategies for direct marketing:

**Whom should I talk to when I am ready to make my first contact with a restaurant or retailer?**

Communication and first contact is extremely important!

- Suggestions for whom to contact first:
  - Restaurant or retail owner (person responsible for buying food and beverage)
  - Restaurant or retailer’s kitchen manager or assistant manager
  - Restaurant’s chef and/or sous chef
  - Restaurant’s pastry chef
  - Store’s produce manager (the person who might directly buy from you) Consider the size of the store—do they buy direct, or only from distributors?
  - Store’s deli manager (the person who prepares food and might need good produce)
  - Store’s other manager (if a large chain)

- Know the restaurant or business. What kind of food does it specialize in? Have you eaten there? Who are the key people involved? Who patronizes the business? How long has it been in business? What are its signature features? What are the menus and/or products like?

- Come with recipes and information about your farm, your produce, the ways you can use the produce. Be creative. Give people ideas, menus. If it’s a value-added product, such as a special sauce, give ideas about what it can be served with.

- Be sure you know the name of each person you contact and how to pronounce it. This will make a positive impression.

- If a person is not available at a particular time, leave a sample and tell him or her you will return. Leave a sample in any case—it’s always a good idea.

**What are the key points I want to address in my first contact with the restaurant or retailer?**

**Key points for restaurants:**

- **Taste and sample:** First, be sure you let them taste and sample the product. Nothing takes the place of the tasting. Let them hold it, touch it, give them a sensory experience. Talk about your farm or business while you eat together.

- **Story:** Be sure that you are ready with the “story” of your farm. Make it a story, if you haven’t already. People want to hear the real life context for your business. Make yourself and your farm real.
  - Where are you from? What’s the history of your farm?
  - Who else lives on the farm? What kinds of animals, if any, live there? Bring pictures. If you have a web site, be sure to direct them to it.
  - Invite them to visit your farm or ranch.
  - Tell them about your growing season.
  - Explain specifically how your product is better, even if the timing is not what they are used to.
  - Let them know about the shelf life of your product.
**Farm practices:** Talk about how you grow your produce. Be specific. Buyers want to know—is it organic? Is it certified? Exactly what do you do in terms of your practices and what is your philosophy that accompanies those practices? For some buyers, certification is less important than knowing the details of your practice. If they know you grow organic, even though you may not be certified, they might be willing to buy from you. *It all depends on the relationship you establish!*

**Logistics:** Find out their schedule and logistics. Ask them:

- What is your ordering cycle?
- What consumer groups do you cater to?
- What are your receiving hours (very important)? Which days of the week do you receive? What are your invoice procedures?
- What are your quality standards? Standards for organic?
- How do you need the product boxed, labeled, signed (signage)?

**Delivery:** Convince them of your ability to deliver. Then, be sure that your delivery schedule is reliable and consistent. Businesses need to be able to rely on regular, predictable orders (even though on their end they might need to be flexible). Be compulsive about being on time.

**Discuss your needs, too:** Discuss your scheduling needs. Make up a price list, so you can be clear on the minimum you need.

**Trust:** Build trust over time by maintaining the relationship. Be interested in the restaurant or retailer and their business. How are they doing? What are their interests in terms of their business? Keep to your agreements. Try to negotiate business details so that it’s easy and workable for both of you.

**Flavor:** Flavor is important! Be sure you maintain a good product! Give taste tests to demonstrate how good your produce tastes. If it needs to be prepared into a soup, for example, make some and bring it in.

**Projections:** Be able to give restaurants or businesses accurate (as much as possible) projections about the availability of your product, at least one to two weeks ahead.

**Contact Information:** Provide the restaurant with good contact information. Give your cell phone number if they might need to get in touch with you at odd times or while you are making delivery rounds.

**Be flexible:** Be flexible about scheduling and providing produce. If you can provide more at the last minute, the restaurateur will love you!

**Key points for retail contacts:**

- **Give samples:** Taste tests work wonders! They help a produce or deli manager make a decision in your favor. Ask if they will allow a tasting table for customers.
- **Be reliable:** Be very reliable on product quality. The store has to depend on you and your consistency.
- **Create easy and clear invoice procedures:** Make it clear for the user and for yourself. Keep it as simple as possible.
- **Keep clients current on your production:** Keep store managers and other clients up-to-date on your seasonality and availability, or on anything happening at your farm that might influence your product or delivery schedule.
- **Ask questions:** Show an interest in the retailer’s business—how it’s going, what kinds of goals they have, what their mission is.
- **Help them out:** Massage their egos (without going overboard). Give compliments. Make the relationship positive.
- **Show up regularly:** Consistency and reliability go a long way in building trust.
- **Do a monthly newsletter:** Farms with CSAs do this with their CSA customers. Do the same for retail or restaurant customers. It will keep them involved and connected to your farming operation. You want them to feel as though they belong and are invested!
Do call backs to check on quality satisfaction: This is important not only from the point of view of quality, but of business relationships. It will let the buyer know that you are committed to high quality and serious about keeping up the arrangement.

Write your own mission statement. You might want to use it sometime, and it’s a good exercise for clarifying your essential goals.

Commitment, commitment, commitment for both your product and your service!

What “homework” should I do before my first meeting with restaurateurs or retailers?

- What information should I have at my fingertips about my operation?
- What information should I know about the restaurant or retailer?

Homework about your own business
- Write up a history of your farm or be prepared to share it in some way. Don’t just wing it; think about it and plan something out. Write down notes or an outline to carry with you on a visit to the business.
- Figure out the price you need for your products—a range if necessary.
- Know your product and why it’s good or special.
- Be clear (for yourself as well as for them) about how much you can supply and when.
- Prepare a résumé and/or testimonials about your product. A list of quotes from fans is good! This can be verbal or written.

Homework about their business
- Look on the Web. See if the business is on it. If so, find out as much as you can beforehand.
- Look at the Zagat Guide on restaurants (www.zagat.com). How is the business categorized? How is it rated?
- Check out its menus and clientele to see if your product fits with what they do.
- Find out their price requirements, if not beforehand, then in your first contact.
- Find out if they use “seconds”—that is produce that is not the top quality in terms of appearance, but which is good nevertheless. They might use vegetables in soups for example, or in a number of dishes where the appearance of the produce is not a factor. This can be very important in supply.

What do I need to do to maintain a good relationship with my buyer?

Maintaining positive relationships
- Strive for consistency.
- Be reliable on product quality.
- Keep the buyer current on your production practices.
- Ask questions—show an interest in their business.
- Help them out (massage their egos); start with a compliment.
- Keep the relationship friendly and personal. Consider giving gifts periodically, especially if they are related to your farm.
- Show that you are interested.
- Show up regularly.
- Do a monthly newsletter.
- Do call backs to check on quality satisfaction level.
Where can I go for more assistance on this topic?

Contacts, information and assistance:

- Your peers
- Mid-sized distributors
- Agriculture Commissioner’s Department in your county
- Albert’s Organics (http://www.albertsorganics.com)
- California Certified Organic Farmers CCOF (http://www.ccof.org)
- Chef’s Collaborative (http://www.chefscollaborative.org)
- Culinary Institute Of America (http://www.ciachef.edu)
- Farmers Union (http://www.nfu.org)
- Food Marketing Institute (http://www.fmi.org)
- Food Brokers/Distributors (blue book)

- Localharvest.com
- Produce Marketing Association (http://www.pma.com)
- Raw Food movement (http://healing.about.com/library/uc_rawfood_0205.htm)
- SLOW Food movement (http://www.slowfood.com)
- Specialty Produce (http://www.specialtyproduce.com)
- University of California Cooperative Extension or your local county extension office (http://ucanr.org/ce.cfm)
- UC Sustainable Agriculture Research and Education Program (SAREP) (http://www.sarep.ucdavis.edu)
- UC Small Farm Center (http://www.sfc.ucdavis.edu)
- Vance Publishing ‘PACKER’ (http://www.thepacker.com)
- Zagat Survey: America’s Top Restaurants (categorized by year) (http://www.zagat.com)

Mark Mulcahy, Organic Options
PO Box 1886, Glen Ellen, CA 95442
707 939 8355 / 707 939 1613
markmulcahy2earthlink.net / http://www.fieldtoplate.com

Funding for this pamphlet provided by the Western Region USDA Sustainable Agriculture Research and Education (SARE) program. http://wsare.usu.edu

Lesson 1.7: MarketMaker Basics

Estimated time: One hour.

Overview

Interested growers and business owners will learn about MarketMaker including its general history, how it came to Arkansas and how it can be used to market their products and services. The registration process will be covered in detail and businesses will be able to complete registration and fully utilize all of MarketMaker’s features. Emphasis will be placed on understanding the benefits of differentiating products and services through filling in the application completely and by entering in additional information that helps ‘tell the story’ of the products and services being marketed. Participants will also learn how to maintain accounts.

Objectives

1. Discover the online marketing resource MarketMaker
2. Learn the history of MarketMaker and how it can be used
3. Understand how to register a business on MarketMaker
4. Become familiar with the importance of filing out the application fully
5. Consider how to “tell your story” through your product
6. Learn how to maintain your business profile

Assessment

Participants will view the presentation on MarketMaker and interact throughout with questions and comments. They will follow along with the example outlined in the presentation to learn how to fill out the registration materials required to use MarketMaker. Participants should be encouraged to view the case studies to learn some of its useful features.

Equipment, Supplies, and Materials

1. Power Point presentation Lesson 1.7
2. Notes pages Lesson 1.7
3. Arkansas MarketMaker General Flyer
4. Arkansas MarketMaker Registration Flyer
5. Handouts: Three MarketMaker Case Studies
References


Classroom Procedures

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
</table>
| Lead discussion to assess previous knowledge. | • Have you heard of MarketMaker?  
• Has anyone registered for or used the service? |
| Slide 2-3: Introduction | • Go through the overview to give participants and idea of what will be covered  
• Briefly state the objectives |
| Slides 4-6: MarketMaker Intro: present these slides pausing to answer questions throughout the presentation | • Give a good overview of MarketMaker  
• MarketMaker is a national network of State websites connecting farmers and processors with food retailers, consumers and food supply chain actors.  
• Currently 14 states with active sites  
• MarketMaker is useful for consumers and businesses  
• Customized Market Profile - users can build a personal ‘trade area’ with target census tracts, summing up queries and demographic data to map and print;  
• Consumption Pattern Data - a new feature allows users to map the highest concentrations of consumer by product;  
• Buyers and Sellers Forum - businesses can make weekly posts of available or needed food products, paving the way for potential business relationships. |
Classroom Procedures Continued

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
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<tbody>
<tr>
<td>Slides 7-10: Arkansas MarketMaker</td>
<td>• MarketMaker was brought to Arkansas by the University of Arkansas Division of Agriculture and the Walton College of Business Applied Sustainability Center</td>
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<tr>
<td></td>
<td>• It is Free for Users</td>
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<td>• Designed to connect all parts of the food supply chain including farmers, processors, buyers, sellers and consumers</td>
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<td>• The objective of Arkansas MarketMaker is to promote the products and businesses of agricultural producers in Arkansas</td>
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<td></td>
<td>• Present slides 9 and 10 and note that these are screen shots of how the national and Arkansas sites appear online</td>
</tr>
<tr>
<td>Slides 11-25: Instructions and Step-by Step example of How to register a business on MarketMaker. Allow for specific questions about the site.</td>
<td>• Slide 11 - This example illustrates how a producer would navigate the Arkansas MarketMaker registration pages</td>
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<td>• Slide 12 - Screen shot of the main Arkansas registration page. Instruct users to click the “Register Your Business” button</td>
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<td>• Slide 13 - Business Profile - on this page you will select your business type</td>
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<td></td>
<td>• Slide 14 - The farmer in the example selects “Producer/Farmers”. The following screens will be different for each of the business types listed here, but the process is the same regardless. Just different types of information gathered from the different types of businesses.</td>
</tr>
<tr>
<td></td>
<td>• Slide 15 - There will be several tabs available for the producer to check off the products that he grows. The tabs are grouped into general categories (meat, dairy, vegetables, etc.)</td>
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<td></td>
<td>• Slide 16 - There are many options for product attributes all of which are searchable by consumers. When registering, you should take the time to fill in as many product attributes as possible that help distinguish your products.</td>
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<td></td>
<td>• Slides 17-19 - the example continues with the business profile. Again, emphasize the importance of a complete application that lists all of the product attributes.</td>
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### Classroom Procedures Continued

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<thead>
<tr>
<th>Slides 11-25: Step-by Step example (cont.)</th>
<th>Content</th>
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<tr>
<td>• Slide 20 - This slide emphasizes the point that consumers will be using this information. Distinguish your products by filling in important product attributes. MarketMaker offers a great level of detail so take full advantage of it.</td>
<td></td>
</tr>
<tr>
<td>• Slides 21-23 - Our farmer wants to fill out his form completely so he edits his business profile. He lists information about the unique characteristics of his farm and its history. He also checks the Agritourism box and continues with filling in this information.</td>
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<tr>
<td>• Slide 24 - Users need an accurate address for the business so that users can fully utilize the GIS mapping feature</td>
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<thead>
<tr>
<th>Slides 26-27: Product Differentiation</th>
<th>Content</th>
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<tbody>
<tr>
<td>• The slides emphasize the importance of filling out the registration materials completely to aid in product differentiation.</td>
<td></td>
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<tr>
<td>• What types of information could the farmer add to help differentiate his products from competitors’?</td>
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<tr>
<td>• Can you think of other characteristics other than Grown Locally that could help make this business stand out?</td>
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<tr>
<td>• Examples: Good Agricultural Practices (GAPs), Certified Organic, No MSG, Kosher, GMO Free, Wild Harvest</td>
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<thead>
<tr>
<th>Slides 28-29: Registration Complete and Changing Information</th>
<th>Content</th>
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<tr>
<td>• Users can login and edit all of their information after registration is complete</td>
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<tr>
<td>• If you are a member of any grower associations you may have already been registered with MarketMaker</td>
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<tr>
<td>• If so, you can simply request account access from the main registration page to get a login id and password to access and edit your account</td>
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Classroom Procedures Continued

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</table>
| Slides 30-33: How Customers Use MarketMaker | • Fill out the registration and distinguish your products because consumers search MarketMaker and can generate results with a high level of detail  
• Customers can select basic information such as business and product types plus attributes such as locally grown and use a GIS mapping feature to locate businesses  
• Example: if you sell organic blackberries but have failed to check the attribute but the consumer searches with this criterion, your business would not be shown in the results.  
• Example: if you list a PO box or a non-911 address, the GIS mapping feature will not display your business correctly and some customers may have trouble locating it. |
| Handouts: Three MarketMaker Case Studies | • Suggest that participants read the printed materials and case studies and look for more information on the listed websites.  
• The presentation is only intended as an introduction to MarketMaker; the additional reading materials and links are a good start for participants interested in learning more. |

Sources of Additional Information

2. Arkansas MarketMaker Promotional Video. [http://www.uaex.edu/marketmaker/MMPromo.htm](http://www.uaex.edu/marketmaker/MMPromo.htm)
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Case Studies

The case studies are based on those found on the MarketMaker website, adapted with graphics removed and web addresses shown instead of links. For the web-based versions of these case studies, please visit the case studies section of the Arkansas MarketMaker website or visit: http://www.marketmaker.uiuc.edu/casestudies.php.
Case Study 1: Finding a New Market for Cattle

Larry O'Malley is a cattle producer who would like to sell a branded beef product to high-end consumers. Larry thinks the best potential customers would be households where income is in excess of $100,000.

Larry wants to use MarketMaker to learn two things:

1) Where are the highest concentrations of high-income households?
2) What are the names of the grocery stores that serve those high-end neighborhoods and where are they located?

Step by step directions to select household data and to id stores

1) Where are the highest concentrations of high-income households?

- From the Search page (http://www.marketmaker.uiuc.edu/search.php) select Find a Market.
- In the Find a Market area above the map, select Income as the Market Type.
- In drop box beside Income choose Household income $100,000 and over. In Search By, Larry will choose State/ County and then select the County he wants from the Search Location drop down box. Click Map It.
- A map of the county area will show the census data requested. The legend indicates the number of households in each census tract.
- Larry wants to focus on the census tracts with the highest concentration of high-income households. He will Zoom In around the areas where these households are located by drawing a box around that area. (Hold down the left mouse button and draw a box.)
- Using the Census Info button to the left of the map (click on it to activate), Larry can click on a specific census tract within the map to collect census data. Data appears in a separate window.
2) What are the names of the grocery stores that serve those high-end neighborhoods and where are they located?

- Larry chooses an area for a target market of grocery stores with high-end consumers. To search for grocers, Larry clicks on the Find Business tab located above the map. For Business Type, he selects Food Retailers. For Line of Business, he selects Grocery Store. He then clicks on Map It! (The speed of the grocery store mapping will depend on the number of grocery stores in the chosen area.)

- Once the grocery stores appear on the map, Larry will notice yellow dots and red dots. Yellow dots represent businesses included in the first 10 results listed below the map. Red dots are for other businesses in the search results but not currently in the results list. Putting the cursor over the yellow dot causes a small window to appear that tells the business name. Click on it for more information.

- Below the map, is the results table. Larry can click on the numbers below the results to move through the list. Within the same area, Larry can find out more about the specific store by clicking on View Details which provides information about a business that includes the name, address, telephone number, website address, sales volume, number of employees, business type and industry classification.

- Within the search results, Larry can click on Zoom to Location and MarketMaker will map only the individual record. If he wants additional information on a particular grocery store, Larry can click on Detail within that individual record.

- Larry has decided to contact a small grocer to market his beef. Even though there are larger ones in the same area, Larry realizes he cannot supply them with the amount of product they need and he will not have as much control on the price of his product.

Adapted from a MarketMaker Case Study:
http://www.marketmaker.uiuc.edu/singlecasestudy.php?recordID=24
Case Study 2: Increasing Manufacturing Output

Ingrid Parker has been making wine jelly in her home for years but has decided that selling the product to gift shops and gourmet food stores could become a profitable venture. Ingrid would need to sell more jars than she can reasonably produce out of her home. She is interested in locating a company to can the jelly and place her labels on the jars. Ingrid uses MarketMaker to locate manufacturers that will do contract canning of jellies, sometimes called co-packers.

Ingrid wants to use MarketMaker to:

Locate all the manufacturers that will do contract canning of jellies, sometimes called co-packers

Step by step directions to identify jelly co-packers

- From the **Find a Business** area of the Search page, click the drop down arrow beside **Business Type**.

- In the drop box, select **Processor**.

- In the **Line of Business** drop box, select **Fruit and Vegetables**.

- If Ingrid had a particular location she was targeting, she could search by City or County. Since Ingrid does not have a specific location in mind, she will select **Statewide** as her search area. Click on **Search**.

- The search results will appear. Ingrid can click on the **MapIt** icon in the Action column of a particular business and MarketMaker will map out the location of the business. If she wants additional information on a particular business, she can click on the **Details** icon of that individual record. The details include contact information, location, web address, and detailed product information, if available. Ingrid also has an option of clicking on **Map All** to view the entire results list in map view.

- Ingrid decides to use the **Map All** button located above the search results. By mapping all of the results, she can see where the businesses are located all at once. The advantage of this is that she can determine a location that best suits her without searching through all of the results.
Once the businesses are all mapped, Ingrid will notice yellow dots and red dots. Yellow dots represent businesses included in the first 10 results listed below the map. Red dots are for other businesses in the search results but not currently in the results list. Putting the cursor over the yellow dot causes a small window to appear that tells the business name. Click on it for more information about the business.

Below the map is the results table. Ingrid can click on the numbers below the results to move through the list. Within the same area, Ingrid can find out more about the specific business by clicking on View Details which provides information about a business including the name, address, telephone number, website address, sales volume, number of employees, business type and industry classification.

Within the search results, Ingrid can click on Zoom to Location and MarketMaker will map only the individual record.

Ingrid can also zoom in closer to some of the businesses located on the state map. After selecting the Zoom In icon located to the left of the map, she can draw a box around the area she wants to focus in on by holding down the left mouse button and drawing a box around that area. The major roads, U.S. highways and interstates become more visible the closer she zooms in to the business.

Once the map refreshes, Ingrid will click on Refresh Data! located above the map to update the results table below the map.

Adapted from a MarketMaker Case Study:
http://www.marketmaker.uiuc.edu/singlecasestudy.php?recordID=25
Case Study 3: Chef Wants Organic Produce

David Peronne is a chef in a French restaurant where dining is white tablecloth upscale. Chef Peronne prides himself in only the freshest ingredients. Lately his customer's have also been requesting organically grown entrees. Chef Peronne uses MarketMaker to locate farmers who can direct market and deliver fresh organic eggs and vegetables to his restaurant.

David wants to use MarketMaker to:

Locate farmers who can direct market and deliver fresh organic eggs and vegetables.

*Step by step directions to identify organic vegetable and egg producers*

- From the **Find a Business** area of the Search page, click the drop down arrow beside **Business Type**. David selects **Producers/Farmers**. Next he selects **Vegetables** for the **Producer Type**.

- Since David is looking for fresh organic vegetables, he will select **certified organic** in the **Product Attribute** drop down menu, and **fresh** from the **Product Form** drop down menu. He will select **Statewide** for the search area and then click on **Search**.

- The search results will appear. David can click on the **Map It or Details** icon in the Action column of a particular business to get information about them. **Map It** will map out the location of the business. **Details** brings up additional information on a particular business. The details include contact information, location, web address, and detailed product information, if available. David also has an option of clicking on **Map All** to view all results in map view.

- David is also looking for fresh organic eggs. He can select **Meat** from the **Producer Type** dropdown menu. David selects **Eggs** from the **Product Type** dropdown menu, **certified organic** from the **Product Attributes** dropdown menu, and **fresh** from the **Product Form** dropdown menu.

- The search results will appear. David can do the same steps mentioned above to learn more about the businesses listed in the results.

- David can now research and contact producers to purchasing product for his up-scale restaurant.

Adapted from a MarketMaker Case Study: [http://www.marketmaker.uiuc.edu/singlecasestudy.php?recordID=26](http://www.marketmaker.uiuc.edu/singlecasestudy.php?recordID=26)
MarketMaker Basics

Lesson 1.7

Overview

- Business owners will learn about MarketMaker and how it came to Arkansas
- The registration process will be covered in detail and businesses will be able to complete registration
- Fully utilizing all of MarketMaker’s features to help differentiate products and services will be explored
- Maintaining and changing account information is discussed

Objectives

1) Discover the online marketing resource MarketMaker
2) Learn the history of MarketMaker and how it can be used
3) Understand how to register a business on MarketMaker
4) Become familiar with the importance of filing out the application fully
5) Consider how to “tell your story” through your product
6) Learn how to maintain your business profile
What is MarketMaker?

- Free interactive mapping system that locates businesses and markets of agricultural products in Indiana
- Directory of State and Regional Food Producers and Buyers
- Began in 2004 in Illinois
- Electronically connect food producing farmers with economically viable new markets
- Currently one of most extensive databases of searchable food related data in the country

Why MarketMaker?

- Food system procures on price not value added
- Product flows through the system anonymously
- Niche markets go unmet because of lack of economies in distribution and high cost of market intelligence

  - From Farm to Plate - building an information network that helps farmers access markets and helps consumers find locally grown products

Why MarketMaker?

- Identify potential markets by demographic characteristics
- Access Demographic profiles of the markets you are targeting
- Locate other producers, processors, wholesalers, food retailers, restaurants, and farmers markets within Arkansas
- Users can conduct detailed searches based on a wide range of production practices, processing/packaging systems, and numerous product attributes
Arkansas MarketMaker

- MarketMaker is now available to Arkansas' farmers, businesses, and consumers
- Interactive web resource aimed at promoting the products and businesses of agricultural producers
- Free to use
- Designed to connect food producers, distributors, buyers, and sellers to their specific consumer markets

Arkansas MarketMaker

- University of Arkansas Division of Agriculture
- The Walton College of Business Applied Sustainability Center

National MarketMaker

...
Example: Producers/Farmers

This example goes through a step-by-step of how to register a business on the MarketMaker website.

- On Farm Sales and Pick Your Own business
- Grows apples, blueberries, and blackberries
- Also presses and bottles apple cider and sells homemade jellies and jams

Register Your Business

- Select the option “Register Your Business” on the right side of the screen to start the process
Register Your Business

Select a Business Type

- Select the type of business from the drop down menu
- Example:
  - Our farmer selects "Producer/Farmers"

Business Profile

- Tabs for a range of products grouped by type (meat, dairy, vegetables, etc.)
- Our farmer selects the "Fruit and Nuts" tab and checks boxes next to:
  - Apples
  - Blackberries
  - Blueberries
Business Profile

☐ Our farmer scrolls down to fill out
  ■ Product Attributes
  ■ Product Forms
  ■ Method of Sales

☐ Our farmer checks the boxes next to:
  □ No Artificial Color
  □ Locally Grown
  □ No Preservatives

Business Profile

☐ Product Forms
  ☐ Our farmer checks the boxes next to:
    □ Bottled
    □ Canned
    □ Cider
    □ Jams Jellies
    □ Unpasteurized

Business Profile

☐ Method of Sales
  ☐ Our farmer checks the boxes next to:
    □ On Farm Sales
    □ Pick Your Own
**Business Profile**

- Days/Hours of Operation
- Our farmer lists hours of operation for two time periods based on the seasonal nature
  - April 1 – Oct 31
  - Nov 1 – March 31

**Keep in Mind**

- Customers can conduct searches for products by a number of criteria
  - Take advantage of the detailed information on production practices, processing/packaging systems, and different product attributes
  - Fill out completely the enterprises and marketing channel characteristics
  - Differentiate the products and service offerings to potential customers
  - Highlight the unique attributes and specialties allowing for enhanced niche marketing efforts

**Business Profile - Expanded**

- Additional description of your business
- Our farmer fills in information about the history of the farm
- Our farmer also checks the button next to "yes" for Agritourism
Agritourism

☐ Under “Attraction” our farmer checks
  ☑ Pick Your Own
  ☑ Enters “Old Fashioned Cider Pressing”
  ☑ Our farmers notes that Motorcoaches are welcome
  ☑ No reservations

Agritourism

☐ Our farmer checks
  ☑ Handicapped Accessible
  ☑ Months of Operation
  ☑ Makes a note of the months for U-Pick and Cider Press operation
  ☑ Then clicks “Continue”

General Business Information

☐ Our farmer fills in his business information
  ☑ It is important to fill in the address in its correct 911 format so the GIS mapping feature will work accurately
  ☑ Clicks “Continue”
Business Preview

- Summary of all the entered information
- Our farmer checks all information for accuracy before submitting

Product Differentiation

- For small and mid sized producers, it is of particular importance to differentiate their products
- Tell the story of the product in the marketing
- Don’t compete on price alone
- Example: Grown Locally

More info: www.arkansasgrown.org

Product Differentiation

- Some consumers are willing to pay more for locally grown products as well as for other attributes
- Consumers need to become more familiar with your products and services

More info: www.arkansasgrown.org
Completed Registration

- Our farmer has differentiated his products and services
  - With the additional information regarding the history of the farm and the agritourism activities, our farmer has given customers a great deal of information
  - Our farmer told the story of his products and the additional information combined with the detailed product attributes listed may lead to more customers

Updating/Changing Information

- Once registration is complete, users can login and change their profile
- Do not be surprised if your business is already listed
  - Some grower associations list members
  - Purchased business database secured by the MarketMaker network
  - From the Arkansas MarketMaker registration page, click the “Request Account Access” button and fill out the information to gain access to your account

How do customers use MarketMaker?

- Consumers will be able to search many different criteria
  - Business Type – restaurant, farmer, retailer, etc.
  - Line of Business (if applicable) – fruits, vegetables, dairy, meats, beverages, bakery products, etc.
  - Product Type – apples, catfish, woven baskets, etc.
  - Product Attributes – locally grown, organic, etc.
How do customers use MarketMaker?

- Consumers will be able to search many different criteria
  - **Product Form** – bottled, smoked, pickled, etc.
  - **Method of Sale** – farmers market, u-pick, etc.
  - **Location** – state, county, city, multi-state, zip code
  - **Mapping** – all results can be mapped

Results of search are shown on a map and in a list.
Detailed information is as easy as the push of a button.

*Example from Mississippi MarketMaker*

Full information for all registered businesses is available.
Customers can even enter their zip code and then print out directions to your business.

*Example from Mississippi MarketMaker*
Summary

- Arkansas MarketMaker
- The registration process needs to be completed with as much detail as possible
- Differentiate your products and services
- Fully utilizing all of MarketMaker’s features to market your products and your story
- Your profile can be self maintained by use of your username and password
  - Customers want a high level of detail – so provide it for them!

References

University of Arkansas Division of Agriculture. MarketMaker registration website. Available online: http://www.uaex.edu/marketmaker/Registration.pdf


Arkansas Grown Program. Arkansas Department of Agriculture. Available online: http://www.arkansagrown.org

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of any information disclosed in this document.
Arkansas MarketMaker Registration

MarketMaker is an online marketing resource available to Arkansas’ farmers, businesses, and consumers. The interactive web resource aimed at promoting the products and businesses of agricultural producers is free to use. It is designed to connect food producers, distributors, buyers, and sellers to their specific consumer markets.

The registration process is straightforward and uses a menu-driven system. To start the process simply click on the registration link (www.uaex.edu/marketmaker/register). Once you click on the link, users will have three options to choose from: 1) Members Area, 2) Register Your Business, and 3) Request Account Access.
Members Area
The member area is for users who have already registered and received a membership account. The registration process is secure and users can be confident that the system will protect the privacy of their account information. User supplied information will not be shared with third parties (outside of the University of Arkansas and the University of Illinois) and will only be used to promote MarketMaker educational activities and correspond. When you initially register you will select a username and password, which is used to sign-in on subsequent visits.

Register Your Business
If you are new to the site, click on this link to develop your business profile. The following link will display when registering your business initially.

![Business Profile](image)

(NOTE: Consumers can not register on the site; you must represent a business to register.)

The first step is to select your business profile from a drop down menu. The registration process is mostly menu-driven with drop-down menus. There are seven different types of businesses that can register to the site:

- Eating and Drinking Places
- Wholesalers
- Food Retailer
- Producers/farmers
- Farmers’ Markets
- Winery

Once you have selected your business type, simple click on the tabs and highlight your product and service listings. The site has different tabs detailing types of production agriculture, numerous processing/packaging systems, and different product attributes. As you register, users will notice a selection of enterprises and marketing channel characteristics. The site allows users...
to conduct searches for products by these criteria in addition to defining the region for the search. Therefore, users should pay specific attention to the numerous ways they can differentiate their products and service offerings to potential customers. Users can highlight the various unique attributes and specialties that their operations provide allowing for enhanced niche marketing efforts. Also, the site contains a section for growers to highlight any agritourism activities on their operation. While registering, users should think what would my target customer want to know about my operation.

In addition to the menu system requests, there are some general information requests. When registering, make note of the “required” information. You must supply an active email account and a street address (required for the GIS mapping feature). Below is a preview of the general information requested.

Once you have successfully registered, the site will allow you to “preview” your business profile. The preview shows the user how their information will be displayed on the site for queries. Users will again have the option of editing their profile to make any needed changes before “submitting”.

Section 1 - 161
Request Account Access

If you are already included in our business database and want to edit or change your information but do not yet have a username/password click this link. A business may already be in the database if you were a part of a grower association or purchased business database secured by the MarketMaker network.

Once you click on this link, the page will ask you to complete and submit the form shown below to request a member account. Once registered you will receive a membership username and password. Then you can sign in as a member and edit and manage your business profile listing.

* required

*Business Name: ________________________________

*Contact Person: ________________________________

*Email Address: ________________________________

   Email address must be active. Username/password will be sent to this address.

*Primary Phone: ___________ xxx-xxx-xxxx

Once you have registered you can preview and edit your listing. Please note that the site will not be active until September 2009. Therefore, active searches of the database will not be allowed until the resource is launched. Again, the site is free to use for businesses and consumers. If you have questions, feel free to email us at marketmaker@uaex.edu or call 501-671-2347.
What’s MarketMaker?
MarketMaker is a national network of State websites connecting farmers and processors with food retailers, consumers and food supply chain actors. (http://national.marketmaker.uiuc.edu/). The network has one of the most extensive collections of searchable food industry related data in the U.S. with 350,000+ farmer and food business profiles.

There are currently 14 states with active sites, and several other states exploring options to partner with this dynamic effort. Partner states become part of the emerging national network aimed at developing a web-based resource to aid in the development of a value-added food supply chain.

Each State’s site allows users to query, map and locate data. Each site is open and accessible on a no-fee basis.

Arkansas MarketMaker Soon Online!
At Extension, we are gathering data on farmers' markets, food processors, wholesalers, and wineries to create the farmer/producer database for the entire state. Our Illinois partners purchased private data for all retail food businesses.

- Currently Arkansas Cooperative Extension Service faculty are collecting and organizing agribusiness information through August 2009.
- Arkansas MarketMaker site is set to go live by the middle of September in 2009: (http://www.uaex.edu/marketmaker).
- Every farmer or business listed on Arkansas MarketMaker can edit, update, and manage their own online profiles via a secure password.
- If you have questions about this resource, email us at: marketmaker@uaex.edu or call 501-671-2347.

MarketMaker Features
- Customized Market Profile - users can build a personal ‘trade area’ with target census tracts, summing up queries and demographic data to map and print;
- Consumption Pattern Data: a new feature allows users to map the highest concentrations of consumer by product;
- Buyers and Sellers Forum: businesses can make weekly ‘posts’ of available or needed food products, paving the way for potential business relationships.

Make Sure You’re Registered!
Every Arkansas producer should want to be listed on this site by registering through the website. The Producer Registration Form is available on University of Arkansas Cooperative Extension Service’s website (www.uaex.edu/marketmaker).

Every Arkansas producer that is interested in direct marketing should join now to become a part of this growing and dynamic database!
Lesson 1.8: Organic Marketing

Estimated time: One hour.

Overview

This lesson is designed to address specific concerns and interests of organic producers in direct marketing venues. First, you will learn about the NOP and where to find more information on USDA’s guidelines and regulations for organic producers. Then, you will learn about marketing issues organic producers face – customer demographics and education; choosing and pricing products.

Objectives

1. Become familiar with the National Organic Program (NOP).
2. Learn basic organic regulations and where to find more information about regulations.
3. Become familiar with marketing techniques and considerations for organic producers in direct markets.

Assessment

Although there are no homework assignments or in-class examples, further reading documents and handouts provide more information for students who are interested in learning more about the subject.

Equipment, Supplies, and Materials

1. Power Point presentation Lesson 1.9
2. Handout “Certification”
3. Handout “Organic Labeling and Marketing Information”
References


Classroom Procedures

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
<tbody>
<tr>
<td>Slides 3-4: Discussion of overview and objectives.</td>
<td>- Lead discussion to assess students’ previous knowledge of the subject.</td>
</tr>
<tr>
<td></td>
<td>- Who is certified organic?</td>
</tr>
<tr>
<td></td>
<td>- Who is thinking of converting?</td>
</tr>
<tr>
<td></td>
<td>- What special issues have you faced with marketing organic produce?</td>
</tr>
<tr>
<td></td>
<td>- Go over objectives.</td>
</tr>
</tbody>
</table>
### Classroom Procedures Continued

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
</table>
| Slide 6: More information on the e-CFR                   | • Link to the entire document in sources.  
• Important to be familiar with all aspects of the NOP in order to be compliant and have good customer relations (answering questions). |
| Slide 7: $5,000 exemption                                 | • Emphasize that even these smallest organic producers must follow all relevant regulations to their operation.  
• All other producers must be third-party organic certified  
• Exemption is based on prohibitive certification costs for very small operations |
| Handout “Certification”                                  | • Addresses issues such as who must be certified, how to get certified, the certification process, and compliance.                                                                                    |
| Slide 8: Labeling standards                              | • Note the minute but important differences in labeling for certified vs. not certified operations  
• Mislabeling can result in a $11,000 fine and disbarment from the NOP for five years.                                                   |
| Handout “Organic Labeling and Marketing Information”     | • Discusses the difference between “100% organic,” “organic,” and “made with…”  
• States what other information must be on the label and outlines penalties for misuse.                                            |
| Handout “Organic Standards for All Organic Operations”   | • Summarizes the highlights of the e-CFR on the NOP in plain English.  
• Go through handout and ask if anyone has questions.                                                                               |
| Slide 11: Free advertising through good customer relations| • What does “organic” entail?  
• How are these products different than conventional?  
• Why are they more expensive?  
• Why should I buy organic products?  
• Customer relations are free and the most effective form of advertising and reputation building in direct markets.  
• Customers’ interest can be based on both real and perceived benefits. Organic products are neither safer nor healthier than conventional products. |
## Classroom Procedures Continued

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
</table>
| Slide 12: Reasons for marketing organic | - Room for new suppliers and extended production in the organic segment  
- Fresh produce accounts for the largest segment of consumption |
| Slide 13: Consumer demographics | - Studies disagree on who is the target market for organic products.  
- Good news for Arkansas producers: the south is a quickly growing market for organic products  
- Most popular items are not necessarily the ones with the highest or the lowest margins. |
| Slide 14: Farmers’ market information | - Data is scarce when regarding specifically organic operations or outlets – price, consumers, demand  
- No specific information on other direct marketing venues found.  
- This data can help organic producers decide if their local farmers’ market is a good option |
| Slide 15: Pricing organic products | - Can be difficult – are you a price maker or a price taker?  
- Premium may be attractive, but note the work, investment, and possibility for price decline in the future  
- Be able to give and educated and reasonable answer when customers ask why organic products are more expensive. |
| Slide 16: Pricing organic products | - When supply covers the shortage due to excess demand, the attractive price premium may be severely decreased or may disappear altogether.  
- Use all resources available to determine prices to capture consumer surplus |
| Slide 17: Conclusion | - Go over bullets.  
- Ask for questions. |
Sources of Additional Information


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Organic Marketing

Lesson 1.8

Overview

- This lesson is designed to address specific concerns and interests of organic producers in direct marketing venues
- Learn about the NOP and where to find more information on USDA’s guidelines and regulations for organic producers
- Then you will learn about marketing issues organic producers face – customer demographics and education; choosing and pricing products

Objectives

1. Become familiar with the National Organic Program (NOP), its regulations, and where to find more information
2. Become familiar with marketing issues and special topics pertaining to marketing organic products in direct markets
NOP Title 7 Part 205 Code: Decoded

- The e-CFR (electronic code of federal regulations) is the legal document that codifies USDA’s NOP and includes
  - Who must be certified (subpart B)
  - Production and handling requirements (subpart C)
  - Labels, labeling, and market information (subpart D)
  - Certification (subpart E)
  - Certifying agent accreditation (subpart F)
  - National list of allowed and prohibited substances (subpart G)
  - Compliance (subpart G)

$5,000 Exemption

- If you intend to sell, label, or represent your products as “100% organic,” “organic,” or “made with organic (specific ingredients)” you must follow NOP guidelines.
- If your annual gross agricultural income from organic sales is less than or equal to $5,000
  - You do not have to be certified but must follow relevant NOP production guidelines (subpart C) and labeling requirements of §205.310.
  - You must keep records for at least 3 years to prove that products were organically produced and handled and verify quantities produced.

Exempt Operations Labeling Caveats

- You may not display the USDA seal or the seal of any certifying agent on your product
- You may not represent your product as certified organic to a buyer
- You may identify the product as an organic ingredient in a multiingredient product only when it is produced by the exempt operation
- You may not use nonorganic ingredients when organic ingredients are available
- You may not use nonorganic and organic forms of the same ingredient
Marketing Organic in Direct Venues

- Marketing organic products is not fundamentally different than conventional products
  - Deliver a consistently high quality product
  - Price products where your willingness to accept the price intersects the customer's willingness to pay the price
- Customer relations are especially important to organic producers in direct markets

Education is Advertising

- Good customer relations are free and can combat negative perceptions of organic products or their prices
- Consumers' interest based on a variety of reasons
  - Sustainable development
  - Environmental pollution and protection
  - Human and animal health concerns
  - Product taste, quality and safety
  - Support for local farmers
- Certified growers can use signs displaying their certification or USDA organic labels on their produce

Reasons to Market Organic Products

- Direct marketing of organic products has traditionally been more common than of conventional products
- Organic operations tend to be smaller and therefore well suited for direct marketing venues
- The organic industry is no longer a "niche" market and has been continuously growing in both supply and demand since the 90s
- Fresh produce is about 39% of the organic market (OTA, 2006)
- Organic chicken and dairy products are fast growing sectors
The Organic Consumer

- Studies disagree on whether or not income is a factor
- Studies also disagree on the demographic of the organic consumer.
- The southern U.S. is one of the fastest growing markets
- Most popular items: tomatoes, carrots, peaches, squash, leafy vegetables, apples, potatoes, and bananas

High Demand Farmers’ Markets

- Demand for organic products was strong in 87% of markets polled
  - Markets close to urban areas, universities, some religious centers, or holistic health care facilities
  - Some rural markets (most convenient access to fresh, organic foods)
- Organic producers stand out because of high quality, customer relations, and a wide variety of specialty products

Organic Price Premiums

- Organic products have higher production costs, especially labor
- Demand for products is growing faster than supply
- Yield may be less than when grown with conventional practices
- Premiums vary widely in range:
  - <10% for oranges and mesclun
  - 78 to >100% for potatoes, broccoli, and carrots
Organic Price Premiums

- Almost all producers receive a premium for organic products except in situations of exceptionally low demand, high supply or especially high conventional product prices.
- Increased supply (lower prices) in the future may result in more consumers choosing organic over conventional products.
- Price your product based on:
  - Market reports for conventional and/or organic products
  - Your competitors' prices

Conclusion

- Know the organic standards
  - Follow legal requirements
  - Answer your potential consumers' questions
- Capitalize on market potential in your area
  - Demographics
  - Location and venue

Conclusion

- Choose your products wisely
  - Variety
  - Quality
  - Demand
- Price products where you are willing to accept and customers are willing to pay
References


Sources of Additional Information


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Certification

The U.S. Department of Agriculture (USDA) accredits State, private, and foreign organizations or persons to become "certifying agents." Certifying agents certify that organic production and handling practices meet the national standards.

Who needs to be certified?

Operations or portions of operations that produce or handle agricultural products that are intended to be sold, labeled, or represented as "100 percent organic," "organic," or "made with organic ingredients" or food group(s).

Who does NOT need to be certified?

Producers and handling (processing) operations that sell less than $5,000 a year in organic agricultural products. Although exempt from certification, these producers and handlers must abide by the national standards for organic products and may label their products as organic.

Handlers, including final retailers, that:

- Do not process or repackage products;
- Only handle products with less than 70 percent organic ingredients;
- Process or prepare, on the premises of the establishment, raw and ready-to-eat food labeled organic;
- Choose to use the word organic only on the information panel; and
- Handle products that are packaged or otherwise enclosed in a container prior to being received by the operation and remain in the same package.

How do farmers and handlers become certified?

An applicant must submit specific information to an accredited certifying agent.

Information must include:

- The type of operation to be certified;
- A history of substances applied to land for the previous 3 years;
- The organic products being grown, raised, or processed;
- The organic system plan (OSP) – a plan describing practices and substances used in production. The OSP also must describe monitoring practices to be performed to verify that the plan is effectively implemented, a record-keeping system, and practices to prevent commingling of organic and nonorganic products and to prevent contact of products with prohibited substances.

Applicants for certification must keep accurate post-certification records for 5 years concerning the production, harvesting, and handling of agricultural products that are to be sold as organic.

These records must document that the operation is in compliance with the regulations and verify the information provided to the certifying agent. Access to these records must be provided to authorized representatives of USDA, including the certifying agent.
Inspection and certification process

Certifying agents review applications for certification eligibility. A qualified inspector conducts an on-site inspection of the applicant's operation. Inspections are scheduled when the inspector can observe the practices used to produce or handle organic products and talk to someone knowledgeable about the operation.

The certifying agent reviews the information submitted by the applicant and the inspector's report. If this information demonstrates that the applicant is complying with the relevant standards and requirements, the certifying agent grants certification and issues a certificate. Certification remains in effect until terminated, either voluntarily or through the enforcement process.

Annual inspections are conducted of each certified operation, and updates of information are provided annually to the certifying agent in advance of conducting these inspections. Certifying agents must be notified by a producer or handler immediately of any changes affecting an operation's compliance with the regulations, such as application of a prohibited pesticide to a field.

Compliance review and enforcement measures

The regulations permit USDA or the certifying agent to conduct unannounced inspections at any time to adequately enforce the regulations. Certifying agents and USDA may also conduct pre- or postharvest testing if there is reason to believe that an agricultural input or product has come into contact with a prohibited substance or been produced using an excluded method.

October 2002
Updated April 2008
Organic Labeling and Marketing Information

The Organic Foods Production Act (OFPA) and the National Organic Program (NOP) assure consumers that the organic agricultural products they purchase are produced, processed, and certified to consistent national organic standards. The labeling requirements of the NOP apply to raw, fresh products and processed products that contain organic agricultural ingredients. Agricultural products that are sold, labeled, or represented as organic must be produced and processed in accordance with the NOP standards.

Except for operations whose gross income from organic sales totals $5,000 or less, farm and processing operations that grow and process organic agricultural products must be certified by USDA-accredited certifying agents.

Labeling requirements are based on the percentage of organic ingredients in a product.

Agicultural products labeled “100 percent organic” and “organic”

Products labeled as “100 percent organic” must contain (excluding water and salt) only organically produced ingredients and processing aids.

Products labeled “organic” must consist of at least 95 percent organically produced ingredients (excluding water and salt). Any remaining product ingredients must consist of nonagricultural substances approved on the National List including specific non-organically produced agricultural products that are not commercially available in organic form.

Products meeting the requirements for “100 percent organic” and “organic” may display these terms and the percentage of organic content on their principal display panel.

The USDA seal and the seal or mark of involved certifying agents may appear on product packages and in advertisements.

Agricultural products labeled “100 percent organic” and “organic” cannot be produced using excluded methods, sewage sludge, or ionizing radiation.

Processed products labeled “made with organic ingredients”

Processed products that contain at least 70 percent organic ingredients can use the phrase “made with organic ingredients” and list up to three of the organic ingredients or food groups on the principal display panel. For example, soup made with at least 70 percent organic ingredients and only organic vegetables may be labeled either “soup made with organic peas, potatoes, and carrots,” or “soup made with organic vegetables.”

Processed products labeled “made with organic ingredients” cannot be produced using excluded methods, sewage sludge, or ionizing radiation. The percentage of organic content and the certifying agent seal or mark may be used on the principal display panel. However, the USDA seal cannot be used anywhere on the package.
Processed products that contain less than 70 percent organic ingredients

These products cannot use the term organic anywhere on the principal display panel. However, they may identify the specific ingredients that are organically produced on the ingredients statement on the information panel.

Other labeling provisions

Any product labeled as organic must identify each organically produced ingredient in the ingredient statement on the information panel.

The name of the certifying agent of the final product must be displayed on the information panel. The address of the certifying agent of the final product may be displayed on the information panel.

There are no restrictions on use of other truthful labeling claims such as “no drugs or growth hormones used,” “free range,” or “sustainably harvested.”

Penalties for misuse of labels

A civil penalty of up to $11,000 can be levied on any person who knowingly sells or labels as organic a product that is not produced and handled in accordance with the National Organic Program’s regulations.

October 2002
Updated April 2008
Organic Standards for All Organic Operations

Highlights of the USDA's National Organic Program Regulations

By Ann H. Baier
NCAT Agriculture Specialist
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This collection of excerpts from the USDA's National Organic Program provides the reader with key standards relevant to all certified organic operations. This publication should be used as needed with excerpts for crop production, livestock production or handling.

Highlights of the USDA's National Organic Program Regulations include key standards for:
1) All certified organic operations
2) Crop production
3) Livestock production
4) Handling (including processing)

Use this publication for all certified organic operations, in combination with one or more of publications two, three or four as relevant to organic crop production, livestock production or handling.

Introduction

This publication provides easy reference to the standards relevant to all organic operations. These excerpts from the USDA's National Organic Program Final Rule contain the general requirements for an organic system plan, recordkeeping, product labeling and preventing commingling and contamination.

This is not a complete collection of organic standards. It must be used in conjunction with standards for crops production, livestock production or handling of agricultural products, as applicable.

This set of excerpts is not a substitute for reading the entire set of standards, which can be found online at www.ams.usda.gov/NOP. This set of excerpts should also not be used for verifying points of compliance for organic production and handling activities with an accredited organic certifier. For a list of these, go to the List of Accredited Certifying Agents on the National Organic Program Web site, www.ams.usda.gov.

Using this guide:
This is a collection of verbatim excerpts from key parts of the National Organic Program's Final Rule. Organic regulations are found under the USDA's Agricultural Marketing Service 7 CFR Part 205. CFR stands for Code of Federal Regulations.

Part 205 of the regulations, found under Title 7: Agriculture, is the National Organic Program.

The Organic Foods Production Act was enacted under the 1990 Farm Bill. The Act, as it is referred to in the text, authorized creation of the USDA National Organic Program to set national standards for the production, handling and processing of organically grown agricultural products. The National Organic Program oversees mandatory certification of organic production. Producers who meet National Organic Program standards may label their products as “USDA Certified Organic.” The subparts reference organizational levels in each excerpt.

The following sections of the National Organic Program are excerpted:

- Recordkeeping and organic system plan
  - § 205.103 Recordkeeping by certified operations
  - § 205.201 Organic production and handling system plan
- The National List of Allowed and Prohibited Substances
• § 205.600 Evaluation criteria for allowed and prohibited substances, methods and ingredients
• Labels, labeling and market information
  o § 205.300 Use of the term “organic”
  o § 205.301 Product composition
• § 205.2 Selected defined terms

For complete information about labeling requirements, see sections 205.302-3.11 included in ATTRA’s Organic Handling Standards Highlights.

**Excerpts**

**Recordkeeping and organizing systems**

1) § 205.103 Recordkeeping by certified operations

a) A certified operation must maintain records concerning the production, harvesting and handling of agricultural products that are or that are intended to be sold, labeled or represented as “100 percent organic,” “organic” or “made with organic (specified ingredients or food groups).”

i) Such records must:

1) Adapt to the particular business that the certified operation is conducting;

2) Fully disclose all activities and transactions of the certified operation in sufficient detail that is readily understood and audited;

3) Be maintained for at least 5 years beyond their creation; and

4) Demonstrate compliance with the Act and the regulations in this part.

ii) A certified operation must make records available for inspection and copying by authorized representatives of the secretary, the applicable state program’s governing official and the certifying agent during normal business hours.

2) § 205.201 Organic production and handling system plan

a) A producer or handler of a production or handling operation, except as exempt or excluded under § 205.101, intending to sell, label or represent agricultural products as “100 percent organic,” “organic” or “made with organic (specified ingredients or food groups)” must develop an organic production or handling system plan that is agreed to by the producer or handler and an accredited certifying agent. An organic system plan must meet the requirements set forth in this section for organic production or handling.”

i) An organic production or handling system plan must include:

1) A description of practices and procedures to be performed and maintained, and the frequency with which they will be performed;

2) A list of each substance to be used as a production or handling input, indicating its composition, source, location(s) where it will be used and documentation of commercial availability, as applicable;

3) A description of the monitoring practices and procedures to be performed and maintained, including the frequency with which they will be performed, to verify that the plan is effectively implemented;

4) A description of the recordkeeping system implemented to comply with the requirements established in § 205.103;

5) A description of the management practices and physical
barriers established to prevent commingling of organic and non-organic products on a split operation and to prevent contact of organic production and handling operations and products with prohibited substances; and

6) Additional information deemed necessary by the certifying agent to evaluate compliance with the regulations.

b) A producer may substitute a plan prepared to meet the requirements of another federal, state or local government regulatory program for the organic system plan, provided that the submitted plan meets all the requirements of this subpart.

The National List of Allowed and Prohibited Substances

1) § 205.600 Evaluation criteria for allowed and prohibited substances, methods and ingredients

a) The following criteria will be utilized in the evaluation of substances or ingredients for the organic production and handling sections of the National List:

i) Synthetic and non-synthetic substances considered for inclusion in or deletion from the National List will be evaluated using the criteria specified in the Act (7 U.S.C. 6517 and 6518).

ii) In addition to the criteria set forth in the Act, any synthetic substance used as a processing aid or adjuvant will be evaluated against the following criteria:

1) The substance cannot be produced from a natural source and there are no organic substitutes;

2) The substance’s manufacture, use and disposal do not have adverse effects on the environment and are done in a manner compatible with organic handling;

3) The nutritional quality of the food is maintained when the substance is used and the substance itself or its breakdown products do not have an adverse effect on human health as defined by applicable federal regulations;

4) The substance’s primary use is not as a preservative or to re-create or improve flavors, colors, textures or nutritive value lost during processing, except where the replacement of nutrients is required by law;

5) The substance is listed as generally recognized as safe by the Food and Drug Administration (FDA) when used in accordance with the FDA’s good manufacturing practices and contains no residues of heavy metals or other contaminants in excess of tolerances set by the FDA; and

6) The substance is essential for the handling of organically produced agricultural products.

iii) Non-synthetics used in organic processing will be evaluated using the criteria specified in the Act (7 U.S.C. 6517 and 6518).

Editor’s note: The National List of Allowed and Prohibited Substances is subject to change as a result of legal actions, petitions to add or remove materials or technical corrections. Please check the Web site www.ams.usda.gov/nop/NOP/standards/FullRegTextOnly.html for the most current update of § 205.601-606 for lists of materials allowed and prohibited for crop and livestock production or handling.
Labels, labeling and market information

1) § 205.300 Use of the term “organic”

a) The term “organic” may only be used on labels and in labeling of raw or processed agricultural products and ingredients that have been produced and handled in accordance with the regulations in this part. The term “organic” may not be used in a product name to modify a non-organic ingredient in the product.

b) Products for export or produced and certified to foreign organic standards or foreign contract buyer requirements may be labeled in accordance with the organic labeling requirements of the receiving country or contract buyer if the shipping containers and shipping documents meet the labeling requirements specified in § 205.307(c).

c) Products produced in a foreign country and exported for sale in the United States must be certified pursuant to subpart E of this part and labeled pursuant to this subpart D.

d) Livestock feeds produced in accordance with the requirements of this part must be labeled in accordance with the requirements of § 205.306.

2) § 205.301 Product composition

a) Products sold, labeled or represented as “100 percent organic”

i) A raw or processed agricultural product sold, labeled or represented as “100 percent organic” must contain (by weight or fluid volume, excluding water and salt) at least 100 percent organically produced ingredients. If labeled as organically produced, such product must be labeled pursuant to § 205.303.

b) Products sold, labeled or represented as “organic”

i) A raw or processed agricultural product sold, labeled or represented as “organic” must contain (by weight or fluid volume, excluding water and salt) at least 95 percent organically produced raw or processed agricultural products. Any remaining product ingredients must be organically produced unless not commercially available in organic form or must be nonagricultural substances or non-organically produced agricultural products produced consistent with the National List in subpart G of this part. If labeled as organically produced, such product must be labeled pursuant to § 205.303.

c) Products sold, labeled or represented as “made with organic (specified ingredients or food groups)”

i) Multi-ingredient agricultural product sold, labeled or represented as “made with organic (specified ingredients or food groups)” must contain (by weight or fluid volume, excluding water and salt) at least 70 percent organically produced ingredients that are produced and handled pursuant to requirements in subpart C of this part. No ingredients may be produced using prohibited practices specified in paragraphs one through three of § 205.301(f). Non-organic ingredients may be produced without regard to paragraphs four through seven of § 205.301(f). If labeled as containing organically produced ingredients or food groups, such product must be labeled pursuant to § 205.304.

d) Products with less than 70 percent organically produced ingredients
i) The organic ingredients in a multi-ingredient agricultural product containing less than 70 percent organically produced ingredients (by weight or fluid volume, excluding water and salt) must be produced and handled pursuant to requirements in subpart C of this part. The non-organic ingredients may be produced and handled without regard to the requirements of this part. Multi-ingredient agricultural product containing less than 70 percent organically produced ingredients may represent the organic nature of the product only as provided in §205.305.

e) Livestock feed

i) A raw or processed livestock feed product sold, labeled or represented as “100 percent organic” must contain (by weight or fluid volume, excluding water and salt) not less than 100 percent organically produced raw or processed agricultural product.

ii) A raw or processed livestock feed product sold, labeled or represented as “organic” must be produced in conformance with §205.237.

iii) All products labeled as “100 percent organic” or “organic” and all ingredients identified as "organic" in the ingredient statement of any product must not:

1) Be produced using excluded methods, pursuant to §201.105(e);

2) Be produced using sewage sludge, pursuant to §201.105(f);

3) Be processed using ionizing radiation, pursuant to §201.105(g);

4) Be processed using processing aids not approved on the National List in subpart G of this part, however products labeled as “100 percent organic,” if processed, must be processed using organically produced processing aids;

5) Contain sulfites, nitrates or nitrites added during the production or handling process. However, wine containing added sulfites may be labeled “made with organic grapes”;

6) Be produced using non-organic ingredients when organic ingredients are available; or

7) Include organic and non-organic forms of the same ingredient.

For complete information about labeling requirements, see sections 205.302-3.11 included in ATTRA’s Organic Handling Standards Highlights.

Selected defined terms

1) Audit trail

a) Documentation that is sufficient to determine the source, transfer of ownership and transportation of any agricultural product labeled as “100 percent organic,” the organic ingredients of any agricultural product labeled as “organic” or “made with organic (specified ingredients or food groups)” or the organic ingredients of any agricultural product containing less than 70 percent organic ingredients identified as “organic” in an ingredients statement.

2) Certified operation

a) A crop or livestock production, wild-crop harvesting or handling operation or portion of such operations, that is certified by an accredited certifying agent as utilizing a
3) Certifying agent
   a) Any entity accredited by the secretary as a certifying agent for the purpose of certifying a production or handling operation.

4) Claims
   a) Oral, written, implied or symbolic representations, statements, advertising or other forms of communication presented to the public or buyers of agricultural products that relate to the organic certification process or the terms “100 percent organic,” “organic” or “made with organic (specified ingredients or food groups),” or, in the case of agricultural products containing less than 70 percent organic ingredients, the term “organic” on the ingredients panel.

5) Excluded methods
   a) A variety of methods used to genetically modify organisms or influence their growth and development by means that are not possible under natural conditions or processes and are not considered compatible with organic production. Such methods include cell fusion, microencapsulation and macroencapsulation and recombinant DNA technology (including gene deletion, gene doubling, introducing a foreign gene and changing the positions of genes when achieved by recombinant DNA technology). Such methods do not include the use of traditional breeding, conjugation, fermentation, hybridization, in vitro fertilization or tissue culture.

6) Inspector
   a) Any person retained or used by a certifying agent to conduct inspections of certification applicants or certified production or handling operations.

7) Inspection
   a) The act of examining and evaluating the production or handling operation of an applicant for certification or certified operation to determine compliance with the Act and the regulations in this part.

8) Label
   a) A display of written, printed or graphic material on the immediate container of an agricultural product or any such material affixed to any agricultural product or affixed to a bulk container holding an agricultural product, except for package liners or a display of written, printed or graphic material which contains only information about the weight of the product.

9) Labeling
   a) All written, printed or graphic material accompanying an agricultural product at any time or written, printed or graphic material about the agricultural product displayed at retail stores.

10) Market information
    a) Any written, printed, audiovisual or graphic information, including advertising, pamphlets, flyers, catalogues, posters and signs, that are distributed, broadcast or made available outside of retail outlets and used to assist in the sale or promotion of a product.

11) National List of Allowed and Prohibited Substances (National List)
    a) A list of allowed and prohibited substances as provided for in the Act.

12) National Organic Program
    a) The program authorized by the Act for the purpose of implementing its provisions.
13) National Organic Standards Board
   a) A board established by the secretary under 7 U.S.C. 6518 to assist in the development of standards for substances to be used in organic production and to advise the secretary on any other aspects of the implementation of the National Organic Program.

14) Non-synthetic.
   a) A substance that is derived from mineral, plant or animal matter and does not undergo a synthetic process as defined in section 6502(21) of the Act (7 U.S.C. 6502(21)). For the purposes of this part, non-synthetic is used as a synonym for natural as the term is used in the Act.

15) Organic production
   a) A production system that is managed in accordance with the Act and regulations in this part to respond to site-specific conditions by integrating cultural, biological and mechanical practices that foster the cycling of resources, promote ecological balance and conserve biodiversity.

16) Organic system plan
   a) A plan of management of an organic production or handling operation that has been agreed to by the producer or handler and the certifying agent and includes written plans concerning all aspects of agricultural production or handling described in the Act and the regulations in subpart C of this part.

17) Person
   a) An individual, partnership, corporation, association, cooperative or other entity.

18) Practice standard
   a) The guidelines and requirements through which a production or handling operation implements a required component of its production or handling organic system plan. A practice standard includes a series of allowed and prohibited actions, materials and conditions to establish a minimum performance level for planning, conducting and maintaining a function, such as livestock health care or facility pest management, essential to an organic operation.

19) Prohibited substance
   a) A substance that is prohibited or not provided for in the Act or the regulations of this part for use in any aspect of organic production or handling.

20) Records
   a) Any information in written, visual or electronic form that documents the activities of a producer, handler or certifying agent to comply with the Act and regulations in this part.

21) Split operation
   a) An operation that produces or handles both organic and non-organic agricultural products.

22) Synthetic
   a) A substance that is formulated or manufactured by a chemical process or by a process that chemically changes a substance extracted from naturally occurring plant, animal or mineral sources. The term shall not apply to substances created by naturally occurring biological processes.
Organic Standards for All Organic Operations:
Highlights of the USDA’s National Organic Program Regulations

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Section 2 - Legal Considerations

Lesson 2.1  Contract Basics
Lesson 2.2  Contracting: UCC Article 2
Lesson 2.3  Common Sense Contracting
Lesson 2.4  Food Safety Laws and Regulations
Lesson 2.5  Farmers Markets and You-Pick: Legal Issues
Lesson 2.1: Contract Basics

*Estimated time: One hour.*

**Overview**

Lesson 2.1 is an introduction to the basic principles of contracts. This lesson will take you through the life of a contract, beginning with offer, acceptance and consideration. It will then cover the importance of written contracts and what happens when one party does not fulfill the contract. This lesson will provide you with a basic understanding of contracts and allow you to better analyze contracts for your business.

**Objectives**

1. Understand the formation of a contract and identify the offer, acceptance and consideration.
2. Understand the statute of frauds and the importance of having most contracts in writing.
3. Understand breach of contract and the remedies available.

**Assessment**

There is no homework, but participants will view the presentation on Contract Basics and interact throughout with questions and comments. Examples will be included in the presentation.

**Equipment, Supplies, and Materials**

1. Power Point presentation Lesson 2.1
2. Notes pages Lesson 2.1

**References**

# Classroom Procedures

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| **Slide 4: What is a Contract** | • Lead discussion of how a contract is different than a promise to do something. It requires more.  
• Important to note that contracts are enforceable by courts. This is why you should consider the terms carefully before entering a contract. |
| **Slide 5: Contracts** | • Ask for other examples of contracts participants may have entered into previously.  
• Contract law is often referred to as private law because the parties can set the rules of the relationship.  
• We have the right and the ability to negotiate contract terms with little restriction. However this means the parties are not protected from a bad deal. A court will still enforce contracts that represent a great bargain for one party and a sour deal for the other.  
• Restrictions on contracting are limited: cannot contract for anything illegal or against public policy; minors and incompetent people typically cannot enter contracts. |
| **Slide 6: Life of a Contract** | • We will go through each part of the life of a contract and examine what happens when the obligations of a party to the contract are not met. |
| **Slide 7: Offer** | • Offeror: the person making the offer  
• Offeree: the person to whom the offer is made  
• Advertisements are an expression of intent to sell or an invitation to bargain, not intent to enter into a contract.  
• If an offer is to be revoked, it must be before the offeree has accepted the offer. Usually the revocation must be in the same manner as the offer. If the offeree accepts the offer before it is revoked, then both parties are bound. |
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| Slide 9: Counter Offer      | • A request for more information is not considered a counter offer, but the addition or deletion of terms or changes to existing terms is a counter offer.  
• If the counter offer is rejected, the original offer cannot be accepted at that time. A new offer must be made (even if it is identical to the original offer, the “life” of the contract has started over) |
| Slide 10-12: Consideration | • Consideration is the promise part of the contract – it is either what one party promises to do or exchange in return for the promised action from the other party. |
| Slide 14: Written Contracts | • These are a few of the types of contracts that are required to be in writing by the statute of frauds                                  |
| Slide 16: Performance       | • Full performance is what we hope for and expect. This is usually the outcome, but if the obligations of the contract are not met, then the contract has been breached. |
| Slide 17: Breach of Contract| • The contract sets forth legally enforceable promises. These promises are enforced by the courts.  
• The court will carefully consider all of the facts, including whether there was proper offer, acceptance and consideration; whether the statute of frauds was met, if required; and what type of remedy is most appropriate. |
### Classroom Procedures Continued

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| **Slide 17: Remedies** | • Expectation damages: what the party expected to gain from the bargained exchange. Expectation damages are forward looking. Puts the party the position they would have been in if the contract had been fulfilled.  
• Reliance damages: compensates for the losses incurred in reasonable reliance on the contract that was breached. Reliance damages are backward looking. Puts the party in the position they would have been in if the contract had never been entered into.  
• Restitution: meant to prevent “unjust enrichment” by one party. Can require one party to return an unfair benefit they received as a result of the contract. This remedy is usually used when there has been partial performance of the contractual obligations by one party which results in the other party’s benefit. |
| **Slide 19: Remedies** | • Stipulated damages: usually a fixed sum of money or a formula for calculating the sum of money due if one of the parties breaches the contract in a certain way.  
• Specific performance: By court order, the breaching party will be required to uphold their end of the contract. This is only available in situations where money damages is considered an inadequate remedy. |
Source of Additional Information


Contact Information

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Legal Disclaimer

Contract laws often vary from state to state, and issues that arise are frequently fact-sensitive. This information is provided for educational purposes only and is not a substitute for professional legal advice.
Contract Basics

Lesson 2.1

Overview

- Introduction to the basic principles of contracts
- This lesson will take you through the life of a contract, beginning with offer, acceptance and consideration
- It will then cover the importance of written contracts and what happens when one party does not fulfill the contract
- This lesson will provide you with a basic understanding of contracts and allow you to better analyze contracts for your business

Objectives

1. Understand the formation of a contract and identify the offer, acceptance and consideration
2. Understand the statute of frauds and the importance of having most contracts in writing
3. Understand breach of contract and the remedies available
What is a Contract?

- A legally enforceable promise between 2 or more parties
- Involves legally enforceable commitments or promises to do or not do something

Contracts

- Contracts are everywhere!
  - Buy or Sell Goods
  - Loans
  - Leasing Property
  - Vendor Agreements
- Contracts are used to define relationships
  - Freedom to Contract
  - "Private" Law

Life of a Contract

- Consideration
- Acceptance
- Performance
- Other
Life of a Contract: Offer

- A contract begins with an offer
  - Communication by the offeror of an intent to enter a contract with the offeree with the stated terms
  - It is not an invitation to bargain or negotiate.
  - Advertisements are not offers.
  - Can be revoked before it has been accepted

Life of a Contract: Acceptance

- The next step is acceptance
  - Communication of assent or agreement by the offeree to the terms of the offer to the offeror
  - Acceptance must be made in the manner required by the offerer
    - May require performance of an act or merely communicating to the offeror
  - Offer can only be accepted by offeree
  - Must be accepted within a reasonable time

Life of a Contract: Counter Offer

- Acceptance v. Counter Offer
  - Offer must be accepted exactly as it is, without modifications
  - If the offer is changed, it is a counter offer
  - The original offer is "killed" and the counter offer is then in place
  - If counter offer is rejected, original offer cannot be accepted. The process must begin again.
Consideration is like the glue that holds the contract together and makes it enforceable. The bargained exchange of something of value. Consideration can take many forms:
- Money
- Physical Objects
- Services
- Promised Actions

Selling a Good:
- Adam offers to buy Bill's car for $5000 - Bill accepts Adam's offer
- Adam's consideration is the $5000
- Bill's consideration is the car

Consideration cannot be something that was required of the party already.
- For example: An agreement to pay a previous debt cannot be consideration for a new contract because payment of the prior debt was already required.
Certain contracts must be in writing and signed according to the **Statute of Frauds**.

The contract must also identify the parties and the essential terms and obligations of the agreement.

**Statute of Frauds**

- Obligations that take longer than 1 year to perform
- Real estate sales
- Goods over $500
- Surety – becoming responsible for another’s obligation or debt

Changes or additions should be in writing and signed also.

Even if not required, having contracts in writing is a good business practice.
Life of a Contract: Performance

- If the obligations contained in the contract are fulfilled by both parties, then full performance of the contract has occurred.
- If full performance has not occurred, then the contract may have been breached.

Life of a Contract: Breach of Contract

- "Breach of Contract" – the contract terms were not met by at least one party.
- Courts can step in to provide remedies if the contract is breached.

Life of a Contract: Remedies

- Money is usually the remedy used by the courts.
- The court may order one party to pay the other for:
  - Expectation Damages
  - Reliance Damages
  - Restitution
Life of a Contract: Remedies

- Stipulated Damages
  - Included in the contract when it is formed
  - Agreed on by both parties

- Specific Performance
  - The court may require one party to complete the contractual obligations

Sources of Additional Information

The National Agricultural Law Center
http://www.nationalaglawcenter.org/

- Reading Rooms
- Publications
- Bibliography

References


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of any information disclosed in this document.

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arise are frequently fact-sensitive. This information is
provided for educational purposes only and is not a
substitute for professional legal advice
Lesson 2.2: Contracting: UCC Article 2 – Sale of Goods

Estimated time: One hour.

Overview

Lesson 2.2 is an overview of the basic principles of UCC Article 2 on the sale of goods. This lesson will work through many of the provisions of Article 2 as they relate to contracting for the sale of goods, including definitions, contract terms between merchants, warranties and remedies for breach of contract.

Objectives

1. Understand what the UCC is and why it is important.
2. Understand contract formation and terms of the contract under UCC Article 2.
3. Understand how the UCC aids in contract formation and interpretation between merchants.

Assessment

There is no homework, but students can learn more on their own by reviewing the references listed below.

Equipment, Supplies, and Materials

1. PowerPoint presentation Lesson 2.2 Contracting: UCC Article 2
2. Notes pages Lesson 2.2

References

4. Lesson 2.1 Contract Basics
# Classroom Procedures

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
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</thead>
</table>
| Slides 4, 5 & 6: What is the UCC and what does it cover? | • Drafted by the National Conference of State Law Commissioners. Adopted in the 1950s by most states and has gone through several revisions.  
• It governs most business transactions, from the sale of goods to letters of credit to banking rules.  
• The UCC is divided into 11 different sections called “articles.” Each article addresses a different type of business transaction. |
| Slide 7: Article 2 The Sale of Goods | • Article 2 applies to the sale of goods. It will be the focus of the remainder of this lesson, although any or all of the sections of the UCC may apply to your business transactions. |
| Slides 8 & 9: Definitions | • Article 2 covers the sale of anything that can be considered a “good”.  
• Some transactions include both goods and information. For example, a car is a good even though it contains many computer systems and programs that provide information. However, an architect’s plans delivered on a computer disk would not be a good since the transaction was for the information on the disk.  
• Why does it matter if you are a “merchant”? Article 2 treats contracting between merchants differently than contracts between non-merchants (usually a consumer) and a merchant. This lesson will address contracts between merchants. |
| Slides 10 & 11: Contract Formation | • For more information on the basics of contracting, see Lesson 2.1 Contract Basics.  
• Article 2 was formed with those transactions that take place multiple times in mind.  
• It makes it easy to accept an offer by simply fulfilling the terms within the offer, or by communicating that you will fulfill the terms. |
### Classroom Procedures Continued

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
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</table>
| **Slides 12 & 13: Statute of Frauds** | - The idea behind the statute of frauds is that a contract is not enforceable unless there is evidence that a contract existed. The best evidence of that is a written contract containing the terms that both parties agreed to.  
- Article 2 has three exceptions to the statute of frauds. These are situations in which a contract does not have to be in writing to be enforceable. |
| **Slide 14: Terms of the Contract** | - The terms of a contract may be established in a number of ways. They can be included explicitly within the contract – these are express terms.  
- Often the terms of a contract are not clear, so the court will use the performance during the life of the contract – this is the course of performance of the parties.  
- If the parties have contracted often and for the same things, then they may develop a customary relationship. Terms of the contract can be implied from this as well. It is called course of dealing.  
- Within certain industries there are customs and expectations that may not be made clear in the contract. These terms can be implied from this usage of trade. |
### Slide 15: Gap Fillers

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<tr>
<th>Teaching Procedures</th>
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<tr>
<td>- Article 2 includes many “gap fillers” for terms not mentioned in the contract.</td>
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<tr>
<td>- <strong>Price</strong> – the parties may agree to set a price at a later time, have a 3rd party set the price, or simply leave the price out of the contract. As long as there was an intent to enter into a contract, the contract is still valid and the price set must be reasonable at the time of delivery. This means considering market value at the time the delivery is made.</td>
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<tr>
<td>- <strong>Delivery</strong> – If there is no express agreement as to delivery, Article 2 provides for the manner, place and time of delivery. Unless agreed otherwise, tender of the goods is required in a single delivery, and payment is due only upon receipt of the goods. The place of the delivery, if none is provided in the agreement, is the seller’s place of business – meaning the buyer will pick up the goods from the seller. If no time is mentioned in the contract, delivery must be made in a reasonable time.</td>
<td></td>
</tr>
<tr>
<td>- <strong>Payment</strong> – Unless there are other terms in the contract between the parties that specify otherwise, payment is generally due at the point of receipt to allow the buyer an opportunity to inspect the goods. Even when goods are considered “delivered” upon shipment by the seller, the buyer need not pay until the goods are received.</td>
<td></td>
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<tr>
<td>- There is no gap filler for quantity. The other gap fillers can be determined based on the market or the typical relationship in similar transactions, but there is no way to know what the parties were thinking when it comes to the quantity of goods. It must be specified in the contract.</td>
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## Classroom Procedures Continued

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<th>Teaching Procedures</th>
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</table>
| Slides 16: Express Warranties | - There are 2 types of warranties provided for in Article 2 – Express and Implied  
- Express Warranties arise from the seller’s affirmative actions and become part of the “basis of the bargain”.  
- **Promise or Affirmation of Fact Made by the Seller** – representations made to the buyer by the seller – distinguish from “puffing” or general statements that are an exaggeration of the attributes of the product. “This is the best one on the market.” – a certain amount of puffing can be expected from a salesperson, but it is not a warranty.  
- **Descriptions made by the Buyer or Seller**: Very similar to affirmations of fact. A description can also be made by the buyer. A buyer may request a product of a certain description and the seller may furnish that product.  
- **Sample or Model** – Samples or models used by the Seller in the course of bargaining can also create express warranties as to the standard of quality of work the seller guaranteed to meet. |
| Slide 17: Implied Warranties | - Implied warranties are certain assurances that are made in the sale of goods as a matter of law. They relate to the condition of the goods.  
- **Implied Warranty of Merchantability** - based on unstated, reasonable expectations of the buyer about the quality of the goods. It is meant to change the rule of “caveat emptor” or buyer beware. This warranty guarantees that goods from a merchant meet a certain minimum level of quality. A merchantable good is one that falls within the quality range normally associated with the good by those in the trade. This warranty does not apply to good sold by non-merchants, and it cannot be disclaimed unless expressly disclaimed by name. |
Classroom Procedures Continued

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<th>Teaching Procedures</th>
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</table>
| **Slide 17: Implied Warranties** | • **Warranty of Fitness for a Particular Purpose** – This warranty is implied when a buyer relies on the seller’s judgment or skill when buying goods for a “particular purpose.” It is based on the idea that a seller who knows a buyer’s needs and knows the buyer is relying on the seller to furnish suitable goods has a responsibility to furnish suitable goods. The seller does not have to be a merchant for this warranty to apply. The buyer must prove the seller knew of the use for which the goods were purchased. The buyer must also prove actual reliance on the seller’s assurances.  
• **Warranty of Title** – This is a warranty that the seller has title to, or owns, the goods and has the right to sell them and that the title the seller is passing to the buyer is a good title, free from security interests, liens and encumbrances (except for those the buyer is made aware of). |
| **Slides 18 & 19: Battle of the Forms** | • There are many cases where merchants are fighting over which terms apply. This is a general rule provided by Article 2, but under different circumstances the results may differ. However, most contracts are executed without a problem. These issues only arise when there has been a breach of the terms by one party. |
| **Slide 20: Performance & Breach** | • If both parties meet the terms of the contract, full performance has been made.  
• Goods that do not meet the terms of the contract are “nonconforming” goods. |
### Classroom Procedures Continued

<table>
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<th>Teaching Procedures</th>
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</table>
| Slide 21: Rejection & Cure | • The "perfect tender rule" means that the goods must meet the requirements of the contract and the other governing rules of Article 2, such as usage of trade, course of performance, implied warranties, etc.  
• The seller has the chance to “cure” the breach in 2 situations: if the time for performance has not expired the seller can substitute conforming goods within the contract time and if the time for performance has expired but the seller had reasonable grounds to believe the goods would have been accepted the seller has a reasonable amount of time to cure. In this second situation, the circumstances are usually such that the seller was unaware of the nonconformity, or had no way to know of the nonconformity.  
• The seller must notify the buyer of its intent to cure the situation in a timely manner. |
| Slide 22: Revocation of Acceptance | • This is a rare situation. If you are the buyer, the goods should always be inspected before acceptance to avoid the complications of revoking the acceptance. |
| Slide 23: Anticipatory Repudiation | • Anticipatory repudiation is also called “anticipatory breach.”  
• Sometimes the parties do not wait until the time of performance or delivery to indicate they will not perform their contractual obligation.  
• For more information on contract remedies, see Lesson 2.1: Contract Basic |
Source of Additional Information


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Lesson 2.2

Overview

- This lesson covers the basic principles of UCC Article 2 on the sale of goods
- This lesson will work through many of the provisions of Article 2 as they relate to contracting for the sale of goods, including definitions, contract terms between merchants, warranties and remedies for breach of contract

Objectives

- Understand what the UCC is and why it is important
- Understand contract formation and terms of the contract under UCC Article 2
- Understand how the UCC aids in contract formation and interpretation between merchants
What is the UCC?

- Uniform Commercial Code
- Set of standardized state laws
- Adopted in all 50 states
- Designed to make doing business across state lines easier and more uniform
- Governs most common business transactions

What does the UCC cover?

- Article 1: General Provisions
- Article 2: Sales
- Article 2A: Leases
- Article 3: Negotiable Instruments
- Article 4: Bank Deposits & Collections
- Article 4A: Funds Transfers

What does the UCC cover?

- Article 5: Letters of Credit
- Article 6: Bulk Sales
- Article 7: Documents of Title
- Article 8: Investment Securities
- Article 9: Secured Transactions
Article 2. The Sale of Goods

- Definitions
- Formation of the Contract
- Terms of the Contract
- Performance and Breach of Contract

Article 2. Definitions

- Goods
  - All things that are moveable at the time of identification to a contract for sale
  - Includes specially manufactured goods, unborn young of animals, growing crops and other identified things attached to reality
  - Does not include information, the money in which the price is to be paid or investment securities

- Merchant
  - A person that deals in goods of the kind or holds himself out by occupation as having knowledge or skill peculiar to the practices or goods involved in the transaction

- Between Merchants
  - Any transaction where both parties are charged with the knowledge or skill of a merchant
Article 2. Contract Formation

- The basic requirements to form a contract under Art. 2 are the same as any contract:
  - Offer
  - Communication from offeror to offeree that includes the terms
  - Acceptance
  - Communication of assent to the terms by the offeree to the offeror
  - Consideration
  - Bargained exchange of something of value

- An offeree can accept the offer by either a return promise or by performance of the contract.
- Example:
  - When an order or other offer is made to buy goods, the offer can be accepted by:
    - 1. Promise to ship the goods, or
    - 2. Shipment of the goods

Statute of Frauds

- Contracts for the sale of goods over $500 must be in writing and signed to be enforceable:
  - Must also contain the quantity of goods
Exceptions to the Statute of Frauds

- Specially Manufactured Goods
  - If the seller has already taken steps in the production of goods that are not marketable in the ordinary course of business

- Admission that a contract exists
  - In a pleading, testimony, etc.

- Payment or Delivery has occurred
  - Acceptance of payment or of the goods is an objective indication that a contract existed

Terms of the Contract

- Express Terms
  - Whatever is expressly written into the contract

- Course of Performance
  - Repeated course of action during the life of the contract

- Course of Dealing
  - Repeated course of action during the relationship between the parties

- Usage of Trade
  - Regular practice or method of dealing that is expected within the industry

Terms of the Contract: Gap Fillers

- Price
  - Reasonable price at the time of delivery

- Delivery
  - Single delivery at the seller’s place of business

- Payment
  - Generally due at the point of receipt.

- No gap filler for quantity
Contract Terms: Warranties

- **Express Warranties**
  - Promise or affirmation of fact made by the Seller related to the characteristics and utility of the good
  - Descriptions of the goods
  - Sample or Model used in the course of bargaining

Contract Terms: Warranties

- **Implied Warranties**
  - Implied Warranty of Merchantability
    - Minimum quality standards
  - Warranty of Fitness for a Particular Purpose
    - Good is fit for a particular purpose that the seller knows about
  - Warranty of Title
    - Seller has the right to sell the goods

Battle of the Forms

- Business often have standard forms used in the course of business
- These forms may have differing terms as to warranties, remedies, or disclaimers
- The price, quantity and delivery terms may be the only parts that match up
- Which party’s terms make up the enforceable contract?
Battle of the Forms

- Between Merchants
  - Additional terms become part of the contract, UNLESS
    - The offer forbids alteration,
    - The new terms in the acceptance materially alter the agreement, or
    - One of the merchants objects to the terms added by the other merchant

Performance & Breach

- Failure to perform the terms of the contract is a breach of the contract.
  - If the seller delivers the goods according to the terms, and the buyer rejects them, the buyer has breached
  - If the goods do not meet the terms of the contract, the buyer can either accept or reject the goods.
  - Even if the buyer accepts the goods, the seller has breached the contract and the buyer can seek remedy.

Rejection and Cure

- Rejection
  - The buyer can reject nonconforming goods under the "perfect tender rule"
  - Rejection must be in good faith and in a timely manner
- Cure
  - The seller that deliver nonconforming goods has the right to cure the defect in some situations
Revocation of Acceptance

- After a buyer accepts the goods, it is difficult to return them.
- A buyer may only revoke acceptance if the nonconformity of the goods substantially impairs the value of the goods.
  - The original acceptance must have been based on a reasonable assumption that the nonconformity would be cured.
  - The buyer must not have known about the defects at the time of acceptance.

Anticipatory Repudiation

- Anticipatory Breach
- What can the other party do?
  - Stop its own performance under the contract
  - Wait for performance for a reasonable amount of time
  - Immediately resort to remedies for breach of contract

References


Sources of Additional Information

The National Agricultural Law Center
http://www.nationalaglawcenter.org/

- Reading Rooms
- Publications
- Bibliography

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Section 2-30
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Lesson 2.3: Common Sense Contracting

*Estimated time: One hour.*

**Overview**

Lesson 2.3 will review the legal impacts of signing a contract. You will learn questions to ask before entering a contract and some general rules to follow when contracting to sell your goods.

**Objectives**

1. Review basic points of law on contracting.
2. Understand legal implications of entering a contract.
3. Review key questions and considerations of entering a contract.

**Assessment**

There is no homework, but students can learn more on their own by reviewing the references and handouts listed below.

**Equipment, Supplies, and Materials**

1. PowerPoint presentation Lesson 2.3
2. Notes pages Lesson 2.3
3. Handout “Ten Questions to Ask and Answer Before Signing a Contract”

**References**

### Classroom Procedures

<table>
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<tr>
<th>Teaching Procedures</th>
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<tbody>
<tr>
<td>Slide 4: Common Sense</td>
<td>- This lesson will help you understand the impact of contracting, provide you with questions to answer before signing a contract and give you some guidance on how a contractual relationship works.</td>
</tr>
<tr>
<td>Contracting</td>
<td></td>
</tr>
<tr>
<td>Slide 5: What is a Contract</td>
<td>- It is important to understand that a contract is more than a promise – it is a legally enforceable promise.</td>
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<tr>
<td></td>
<td>- This means the court can step in and enforce the agreement.</td>
</tr>
<tr>
<td></td>
<td>- Do not enter a contract if you do not intend to follow through with the promises you are making.</td>
</tr>
<tr>
<td>Slide 6: Breach &amp; Remedies</td>
<td>- <strong>Specific performance</strong>: By court order, the breaching party will be required to uphold their end of the contract. This is only available in situations where money damages is considered an inadequate remedy.</td>
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<td></td>
<td>- <strong>Expectation damages</strong>: what the party expected to gain from the bargained exchange. Expectation damages are forward looking. Puts the party the position they would have been in if the contract had been fulfilled.</td>
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<tr>
<td></td>
<td>- <strong>Reliance damages</strong>: compensates for the losses incurred in reasonable reliance on the contract that was breached. Reliance damages are backward looking. Puts the party in the position they would have been in if the contract had never been entered into.</td>
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<td>- <strong>Stipulated damages</strong>: usually a fixed sum of money or a formula for calculating the sum of money due if one of the parties breaches the contract in a certain way</td>
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### Classroom Procedures Continued

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<tbody>
<tr>
<td>Slide 7: Who are the parties to the contract?</td>
<td>- These are important questions to answer. More questions and tips are available in the Handout: Ten Questions to Ask and Answer Before You Sign a Contract</td>
</tr>
</tbody>
</table>
| Slide 8: What are the requirements? | - **License**: Business licenses may be required at the local or state level depending on the type of business you operate. In some cases, farmers are exempt from the licensing requirements. However, even if you are a producer you should check with the proper offices to be sure you meet the business requirements. If you are a direct marketer, a license may still be required.  
- **Bonding**: Bonding, or surety bond, is an agreement by a third party promising to pay or have the work completed if a vendor does not fulfill his or her obligations under a contract. A bond is not an insurance policy. It does not cover loss due to personal injury or property damage; it only provides assurance that the work contracted is satisfactorily complete. Banking institutions, surety bond companies and even the Small Business Administration (SBA) offer bonding services.  
- **Insurance**: Liability insurance may be required if you are selling at a farmer’s market. |
| Slide 9: Ten Rules: Rule 1 | - This means there is no reason to assume a contract you are asked to sign is fair or balanced, or that it protects your interests. In fact it is probably safer to assume the opposite. This does not mean the party on the other side is evil, instead it just reflects the fact that most contracts are arms-length business transactions in which both sides try to maximize their advantage. |
## Classroom Procedures Continued

<table>
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<tr>
<td><strong>Slide 10: Ten Rules: Rule 2</strong></td>
<td>• Signing a contract creates a binding legal obligation. It is in your best interest to understand what you are agreeing to do and what the other party’s obligations are as well. Ask questions until you understand and are comfortable with the terms of the contract.</td>
</tr>
</tbody>
</table>
| **Slide 11: Ten Rules: Rule 3** | • Contracts usually offer an economic incentive. But don’t expect to take advantage of it until you have fulfilled your obligations under the contract – including quantity, quality and delivery terms.  
• If a contract to provide a local store with vegetables requires you to meet the quality standards of the buyer, you should not expect to be paid if what you deliver does not meet those standards. |
<p>| <strong>Slide 12: Ten Rules: Rule 4</strong> | • Every provision of a contract has some legal effect. Failure to meet any the terms is considered a breach of the contract. While the party on the other side of an agreement may excuse your failure to perform in one situation, such as not delivering the quantity you promised, this may not always be the case. In some situations, like a crop failure due to weather, the law may provide you with an excuse but in other situations where the failure to perform was due to your actions, the other party might choose to enforce the contract. If you believe you will not be able to perform a contract as agreed it is a good idea to notify the other side and alert them to your situation. Then you can attempt to negotiate a resolution. |
| <strong>Slide 13: Ten Rules: Rule 5</strong> | • Take precautions to limit the risk that you will not be paid. This can be done by learning more about their financial situation: by requesting financial guarantees, and by selling crops or livestock only to businesses which are covered by the public laws designed to insure farmers get paid. |</p>
<table>
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<tr>
<td>Slide 14: Ten Rules: Rule 6</td>
<td>• Even though many contracts are on printed forms, it does not mean they cannot be changed, if the parties agree to it. A good rule to keep in mind is that you will never have more bargaining power in a contract relation than just before you sign. The reverse is also true – once you have signed a contract, it will be difficult to alter it.</td>
</tr>
<tr>
<td>Slide 15: Ten Rules: Rule 7</td>
<td>• Just as the statute of frauds dictates that certain contracts must be in writing, the amendments should also be in writing. Have the other party sign or initial the written changes. Be sure the person you are dealing with has the proper authority to make changes to the contract, especially if they represent a larger business.</td>
</tr>
<tr>
<td>Slide 16: Ten Rules: Rule 8</td>
<td>• Just because you believe the written contract was amended by your discussions doesn’t make it true. In fact most written contracts include provisions that state that only the written terms are binding. It is also important to keep copies of any letters or other documents that might help show what was agreed.</td>
</tr>
<tr>
<td>Slide 17: Ten Rules: Rule 9</td>
<td>• This includes any records or documentation concerning the quantity you delivered and any payments made. It may also be helpful if you keep notes on any communications you have with the other party. If a dispute should arise about your performance, your records may help provide the answers needed to sort out the situation.</td>
</tr>
<tr>
<td>Slide 18: Ten Rules: Rule 10</td>
<td>• Communication between the parties can be important in resolving uncertainties and in preventing misunderstandings. Do not hesitate to ask questions if you don’t understand what is happening, such as why your payment is late. It may be that the other side is unaware of the situation.</td>
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Classroom Procedures Continued

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</table>
| **Slide 19: Getting Paid** | • There are several different approaches to answering the question “How do you make sure you get paid for what you sell?”  
  • **Cash on Delivery**: This maybe possible when the buyer knows the time of your delivery and the amount involved, or when stopping to get cash or write a check does not interrupt the buyer’s business.  
  • **Invoice**: allows the buyer to pay at a later date, which may be more convenient for them. Many businesses have a standard policy as to when a payment is made – as in 30 days after delivery, or once per month.  
  • **Expenses**: bookkeeping, mailing invoices reminding buyers that have not paid on time are expenses that must be incurred if payment is not made upon delivery. The biggest cost is the value of the money during the delay in payment, as you continue to incur costs.  
  • **Risks**: The biggest risk is that of not being paid at all. Selling to buyers on terms other than cash-on-delivery is a form of extending credit to buyers. |
| **Slide 20: PACA** | • In some limited situations state or federal law may provide legal protections to help insure you are paid.  
  • The Perishable Agricultural Commodities Act (PACA) is a federal law that protects growers who sell produce at wholesale.  
  • PACA creates a process for protecting producers who sell produce in interstate commerce. Under PACA certain buyers are required to obtain a license from USDA Agricultural Marketing Service (AMS). |
Source of Additional Information


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This lesson will review the legal impacts of signing a contract. You will learn questions to ask before entering a contract and some general rules to follow when contracting to sell your goods.

Objectives

1. Review basic points of law on contracting
2. Understand the legal implications of entering a contract
3. Review key questions and considerations of entering a contract
Common Sense Contracting

- Understand the impact of signing a contract
  - Legal consequences
- Questions to ask before signing
  - Know all that you can
- Rules to follow when contracting
  - Tips for success

What is a contract?

- A legal document that represents an agreement between 2 or more parties
- Involves legally enforceable commitments or promises to do or not do something

Breach & Remedies

- If one of the parties to the contract doesn't follow through
  - BREACH OF CONTRACT
- Many remedies available
  - Specific Performance to Monetary Damages
Who are the Parties to the Contract?

- Know who you are contracting with
  - Is it an individual or a business?
  - Are they in good financial standing?
  - Do they have a good reputation in the industry?

What requirements are there?

- Some businesses will ask that you meet certain requirements before they will contract with you.
  - License
    - Maybe required by local authorities
  - Bonding
    - Provides assurance that the contract will be met
  - Insurance
    - Liability insurance maybe required

Ten Rules of Contracting

- 1. The first rule of contracts is that the parties who wrote the contract took care of themselves first.
Ten Rules of Contracting

2. Read and understand (at least try to) any contract before signing.

3. Complying with the terms of a contract will be required before you are considered to have satisfied the agreement.

4. Never assume your failure to meet the terms of the agreement will be excused.
Ten Rules of Contracting

5. If the contract calls for you to be paid by another party, know their financial situation.

6. Remember that proposed contracts are always negotiable.

7. Make sure any changes to a contract are in writing.
Ten Rules of Contracting

8. Do not rely on oral communications to amend the terms of an agreement.

9. Keep good records of your performance under the contract.

10. Stay in touch with the other party to the contract.
Getting Paid

- Methods
  - Cash on Delivery
  - Invoice

- Considerations
  - Expenses
  - Risks

PACA

- Perishable Agricultural Commodities Act
  - Protects producers who sell in interstate commerce
  - Certain buyers must get a license
  - License holders must meet certain financial standards
  - License holders are subject to the authority of AMS in resolving disputes over payments
  - See www.ams.usda.gov for more info

Presentation References


Sources of Additional Information

The National Agricultural Law Center
http://www.nationalaglawcenter.org/

- Reading Rooms
- Publications
- Bibliography

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Contract laws often vary from state to state, and issues that arise are frequently fact-sensitive. This information is provided for educational purposes only and is not a substitute for professional legal advice.
Ten Questions to Ask and Answer Before You Sign a Contract*

1. Do you understand what you are agreeing to do, for example are you selling a specific quantity or a quality of produce or other goods?

2. What is the price you will be paid and how is it determined?

3. When will you be paid, or when is payment due if you are buying something?

4. Who will decide whether you have satisfied the terms of the contract?

5. What will happen if a dispute arises, will it go to court or does the contract include some form of alternative dispute resolution such as mediation or arbitration?

6. If there is a dispute where will it be heard and which state’s law will be used?

7. How long will the agreement run and how can it be terminated or extended?

8. Can the agreement be modified once it is signed?

9. Are you considered a merchant under the agreement and held to a higher commercial standard or will you be treated as a farmer?

10. Can the contract be assigned to another person or is it personal to you?

* Taken from The Legal Guide for Direct Farm Marketing, by Neil D. Hamilton (1999).
Lesson 2.4: Food Safety: Laws and Regulations

*Estimated time: One hour.*

**Overview**

Lesson 2.4 will walk you through food safety regulations at the federal, state and local levels. You will learn about different agencies and their responsibility for food safety, as well as several exemptions for farmers and small processors.

**Objectives**

1. Discuss what products are likely to be regulated and require licenses or inspect
2. Review the agencies that address food safety
3. Understand the process for licensing and inspection

**Assessment**

There is no homework, but participants will view the presentation on Food Safety and interact throughout with questions and comments.

**Equipment, Supplies, and Materials**

1. Power Point Lesson 2.4 Food Safety: Laws and Regulations
2. Notes pages Lesson 2.4
3. Handout: Questions to Ask State and Local Food Officials About Inspections and Licenses

**References**

## Classroom Procedures

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
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</table>
| Slide 4: Do the laws apply to me? | • If you sell raw products, then in most circumstances you have little to be concerned with when it comes to food processing and inspection.  
• Value added products have more regulations.  
• No matter what you produce and sell, you should contact the appropriate agency to ensure you are in compliance with any regulations or laws. |
| Slide 5: Value Added Products | • Value added products may help you to increase your sales and profits. However once you become involved in selling processed foods – even just lettuce that has been cut and mixed in a bag for ready to eat salads – your activities will probably fall under state and federal laws that regulate food safety.  
• These laws may limit what you can sell and to who. They include minimum standards for preparation and may even require licenses and inspections. |
| Slide 6: Food Safety Regulation | • Food safety is regulated at many different levels from the federal government down to the local city government.  
• Check with these officials if you have any questions about your products. |
| Slide 11: Food Safety Poultry | • For producers that meet these requirements, they are exempt from the regulations and inspection. It is still important to contact your state officials to learn if there are other requirements for raising poultry or to qualify for the exemption |
| Slide 12: Food Safety Poultry | • These are additional exemptions for small scale operations that process on the farm, or sell directly to households, restaurants, hotels, or small operations that process and distribute poultry.  
• The requirements under any of these exemptions are the same: must have fewer than 20,000 birds, birds must be healthy at slaughter, poultry can only be sold within the state and sanitary processes and procedures must be used.  
• These are federal exemptions. Be sure to check the laws in your state for other requirements. |
### Classroom Procedures Continued

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<th>Teaching Procedures</th>
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</table>
| **Slide 13: Food Safety Meat & Poultry** | • This exemption from inspection for custom processed meat and poultry allows producers to pre-sell animals or potions of the live animal – such as quarters or halves of beef - to other customers before they are processed.  
• There are important restrictions on this method of selling and processing meat and poultry. These vary from state to state. States may require the “owner” – the customer- to pay the processing charges. Some states require the meat to be sold using live weight prices rather than per pound for a cut of meet. Check with your state regulators to find out how the exemption is applied in your state. |
| **Slide 14: National Organic Program** | • The National Organic Program is a marketing program run by USDA. Under the program, producers may place the “USDA Organic” label on their products if certain requirements are met in the production. The program is designed to assure customers that products with the “USDA Organic” label are produced, processed and certified to meet the national organic standards. The labeling requirements apply to raw, fresh products and products that contain organic agri. ingredients.  
• Only certain substances are allowed to be used in the production and processing of certified organic foods. To become certified, a farm or processing facility must go through an application process that involves inspection to ensure they are meeting the requirements of the program. This is a different inspection process than what is required by state and federal agencies to ensure food safety. |
| **Slide 15: State Regulation** | • State laws vary greatly across the country. Many states have exemptions for the direct sale of food products by the farmer – this may or may not include sales made at a famers’ market.  
• The more processed a food product is, the greater the likelihood of state regulation. Contact officials in your state to learn about what specific exemptions exist. |
### Classroom Procedures Continued

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| Slide 16: State Regulation | • Within the state law, the best place to start is with the definitions. These are common definitions of a few terms that are relevant to value added processing.  
• Food establishments are required to have a license to operate. |
| Slide 17: State Regulation | • Home food establishments are a different kind of facility, so a different kind of license is required. It is also limited by the amount of goods sold.  
• Farmers’ markets that meet certain requirements will not need a license. Vendors that sell raw fruits and vegetables will not need a license in most areas, but vendors that sell processed foods will likely need a license. Additionally, vendors selling meat, poultry or eggs will need to follow specific food safety laws for those products. |
| Slide 18: How to get a license | • Although the law varies from state to state, these are the general steps necessary to obtain a license.  
• The application form is usually supplied by the agency and requires you to provide information and details required by the law.  
• If your application is approved, the state will collect a license fee. The amount of the fee varies by state and by the type and size of your business. As a general rule, though, the license fee is not a significant cost of doing business.  
• State laws usually provide that the appropriate agency can inspect your facility at any time, without warning during regular business hours  
• To maintain your license, you must reapply each year, pay the fee and you remain subject to inspection by the state. |
| Slide 20: Local Regulation | • Every farmers’ market will be different. Ask when you join what rules and requirement are in place for food safety. |
Source of Additional Information


Contact Information

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Lesson 2.4 will walk you through food safety regulations at the federal, state and local levels. You will learn about different agencies and their responsibility for food safety, as well as several exemptions for farmers and small processors.

Objectives

1. Discuss what products are likely to be regulated and require licenses or inspection
2. Review the agencies that address food safety
3. Understand the process for licensing and inspection
Do the laws apply to me?

- **Raw Products**
  - Fruit and produce which are not processed in any way
  - Not cooked, prepared, sliced, or transformed from their natural state

- **Value Added Products**
  - Food that has been "processed" in some way
  - Altered from its natural state

Value Added Products

- Jams and Jellies
- Bread and Pies
- Fresh Meat and Poultry
- Fruit Juices
- Cut Lettuce

Food Safety Regulation

- Regulated at several levels
  - Federal
    - USDA
    - FDA
  - State
    - State Health Departments
  - Local
    - City or County Inspectors
Food Safety

- Federal Regulation
  - FDA
  - USDA

- All processed foods, including meat that is sold directly to the consumer or from the wholesaler on
- Raw agricultural products, meat sold at the wholesale level, fresh fruits and vegetables and whole grains.
- Beef, pork, lamb, goats, poultry and eggs, milk and milk products.

Food Safety: Meat

- The USDA has food safety regulations that are separate from state regulations
- Some processing facilities are inspected only by the federal government or only by a state agency.
- Some states do not have a state meat inspection program, so facilities are inspected only by federal inspectors.

Livestock slaughtered and/or processed in a federally inspected facility can be sold in inter-state commerce
- Meaning across state lines, anywhere in the U.S.

Livestock slaughtered and/or processed in a state inspected facility can only be sold in intra-state commerce
- Meaning only in the state where it was processed.
Food Safety: Poultry

- Poultry inspection is handled by USDA
- Some states have inspectors as well
- There are several exemptions for small processors

Food Safety: Poultry

- Exemption
  - 1,000 birds or less
    - Birds must be raised and processed on your farm
    - You are limited to 1,000 birds or less
    - You cannot sell outside of your state
    - You cannot sell or market poultry products other than those from poultry raised on your own farm

Food Safety: Poultry

- Exemptions
  - 1,000 to 20,000 birds
  - For small scale operations that process on-farm or sell directly to consumers or process and distribute poultry
    - Must have 20,000 or fewer birds
    - Poultry must be sound and healthy before slaughter
    - Poultry may only be distributed within the state
    - Must be slaughtered and processed using sanitary standards, practices and procedures
### Food Safety: Meat & Poultry

- **Custom Processing**
  - Another option for the processing and sale of meat and poultry is custom processing by local processors.
  - The facility must meet state standards and are inspected by the state agency.
  - Animals are processed for personal consumption of the owners who deliver them to the facility.
  - Meat is not subject to inspection because it will not be sold.

### National Organic Program

- Different than food safety inspection.
- Administered by USDA.
- Organic certification.
  - List of approved substances to be used in production and processing.
  - Farms and processing facilities must be inspected.

### Food Safety: State Regulation

- State laws vary from state to state.
- There may be exemptions for the direct sale of food products by farmers.
- General rule:
  - The greater the potential hazard from the food or the more the food is processed from its original form, the more likely it is that the state law will require you to obtain a license or get inspection.
Food Safety: State Regulation

Definitions

Food
- Any raw, cooked, or processed edible substance, ice, beverage …for human consumption

Food Establishments
- Place used as a baker, confectionery, cannery, packinghouse, slaughterhouse where animals or poultry are killed or dressed for food, retail grocery
- Common exceptions: home food establishments & farmers’ markets

License is required

Food Safety: State Regulation

Home Food Establishment
- A business on the premises of a residence in which prepared food is created for sale or resale…with gross annual sales less than $20,000
- A special license may be required

Farmers’ Markets
- Raw fruits and vegetables – no license required
- Other laws apply to meat, poultry, eggs
- Licenses and inspection requirements

How to get a license?

Submit a written application

License Fee

Inspection

Reapplying
Food Safety: Local Regulation

- County or City Level Regulation
  - Many state laws are enforced at the county level, so you may be in contact with officials at your county offices
  - Many cities and metropolitan areas have established their own rules and regulations for food safety
  - Contact your city officials for licensing and other special requirements

Food Safety: Local Regulation

- Market Rules
  - Some farmers’ markets may have rules about food handling and storage
  - California
    - All food shall be stored at least 15 centimeters off the floor or ground
    - Food preparation is prohibited except for samples
    - Potentially hazardous food samples shall be maintained at or below 45 degrees Fahrenheit.
    - Utensils and cutting surfaces shall be smooth, non-absorbant and easily cleaned or disposed of

References


Sources of Additional Information

The National Agricultural Law Center
http://www.nationalaglawcenter.org/

- Reading Rooms
- Publications
- Bibliography

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Questions to Ask State and Local Food Officials About Inspections and Licenses*

1. Do I need a state license or permit to produce and sell the products in question?

2. Do the local health officials – such as the city or county inspectors – have their own set of rules for food processing and marketing?

3. If I am presently marketing “processed foods” which require a state or local license what is the procedure for obtaining a license and what is the penalty for failing to have one?

4. What types of home produces foods can I sell without having to be licensed or inspected?

5. What type of kitchen or food processing facility will require me to obtain a food processing license?

6. Does the state provide assistance to producers who want to develop food processing and manufacturing businesses?

* Taken from The Legal Guide for Direct Farm Marketing by Neil D. Hamilton (1999).
Lesson 2.5: Farmers’ Markets & You-Pick: Legal Issues

Estimated time: One hour.

Overview

Lesson 2.5 will examine many of the legal concerns and liability questions associated with farmers’ markets and you-pick operations. It will also address some insurance issues.

Objectives

1. Review legal considerations for participation in farmer’s markets
2. Review legal considerations for you-pick operations
3. Address insurance needs for different types of direct marketing

Assessment

There is no homework, but the handout provides more information for participants.

Equipment, Supplies, and Materials

1. Power Point presentation Lesson 2.5 Farmers’ Markets & You-Pick: Legal Issues
2. Handout “Twenty Questions to Ask About Your Farmers’ Market”

References

### Classroom Procedures

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
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</thead>
<tbody>
<tr>
<td>Slide 5: Questions to Consider</td>
<td>• It is important to consider what risks there are on your property. By considering these questions you can do a brief risk analysis of your property</td>
</tr>
</tbody>
</table>
| Slide 6: Legal Considerations for Farmers’ Markets | • The agreements are a contract between the vendor and the organization that runs the market. The agreements usually include several different clauses:  
  • Agreement to follow market rules: these include the rules on location of the market and times that you may sell among other things that apply to the general operation of the market.  
  • Restrictions on what can be sold: different markets allow different types of products to be sold. The most common restriction is the “producer only,” which means that you can only sell the goods that you raise. Sometimes this rule can be less stringent, allowing a percentage of the items you sell to be grown by another producer.  
  • Insurance: the market may require you to show proof of insurance up to a certain amount with the market listed as an insured policy  
  • Terms of the Membership: This will address admission to the market, suspension or termination of membership, conflict resolution and other issues that may arise if there is a dispute. |
| Slide 7: Legal Considerations for Farmers’ Markets | • There are several questions about potential liability for vendors at farmers’ markets. What happens if there is an injury? Who should have insurance to cover accidents? |
### Slide 10: Legal Considerations for You-Pick Operations
- The primary risk for You-Pick operations come from "premises liability" or the or the notion of having people on your land and how you as the landowner may be liable.
- Premise liability is based on Negligence. A person is negligent if they fail to exercise the care that a reasonably prudent person would exercise in like circumstances.
- If you uphold your duty of care – or your level of responsibility – then you are not negligent.

### Slide 11: Premise Liability Issues
- Traditionally, entrants upon land have been categorized into 3 different categories. A different level of responsibility exists for each category of entrant.
- Some states have done away with the categories, but the concept of owing a duty of care to those upon your land remains the same. If someone is on your property you have a certain level of responsibility to keep them safe.

### Slide 12: Trespasser
- **Trespasser:** On the property without permission. You owe trespassers a very low responsibility to keep them safe or prevent their injury.
- If you know about trespassers, and cause them harm, you will be liable even though they did not have permission to be on your land.

### Slide 13: Licensee
- **Licensee:** Present for a non-commercial, non-business purpose with the consent of the possessor of the property, such as a social guest at someone’s residence. You should warn licensees of hidden dangers where they do not know or are unlikely to know of the conditions or risks.
- For example, you should warn that the steps down into the basement are steep.
## Classroom Procedures Continued

<table>
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<tbody>
<tr>
<td>Slide 14: Invitee</td>
<td>- <strong>Invitee:</strong> Invited on the property to conduct business or for other benefits to the property owner, such as customers, employees, business visitors. You owe invitees a general duty to use ordinary care to keep the premises reasonably safe for their benefit. This means making sure your employees have safe equipment, facilities, proper training, etc.</td>
</tr>
</tbody>
</table>
| Slide 16: Legal Considerations for You-Pick Operations | - Unreasonable risk and willful, wanton or reckless conduct usually refer to purposely injuring a customer, or doing or not doing something that creates a risk that is unacceptable in the eyes of the law.  
- Arkansas, Massachusetts, Michigan, New Hampshire, New Jersey, Ohio and Pennsylvania are a few of the states with laws specifically addressing the liability of you-pick operations.  
- Kansas, Tennessee, Louisiana, North Carolina, Georgia and Virginia are a few of the states with liability protections for agritourism operations – which often include you-pick operations.  
- It is important to remember that these laws do not guarantee that you will not be held liable. They offer protection in specific circumstances only. It is important to be familiar with the laws in your state on these issues. |
| Slide 17: Insurance | - Insurance is a great risk management tool. There are several different types and you may have questions about what is covered |
### Classroom Procedures Continued

<table>
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<th>Teaching Procedures</th>
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</table>
| **Slide 18: Insurance** | - Your comprehensive farm liability policy may or may not cover your direct marketing activities. Comprehensive policies that do cover direct marketing usually only cover roadside stands.  
- Often there are exclusions for retail activities and other business pursuits. Selling at a farmers’ market and operating a you-pick operation – even on the property where you grow the product – may not be covered by a general policy like this. It is best to talk with your insurance agent about whether your activities are adequately covered under the policy that you have. |
| **Slide 19: Insurance** | - Some small growers have opted to increase their coverage under their homeowner’s insurance policy. Generally these types of policies are available where the sales are less than $5000 per year and the business is a secondary source of income. |
| **Slide 20: Insurance** | - Product liability refers to the situation where a person is hurt by the product – such as the produce making them ill.  
- Premise liability refers to the situation where a person is injured while on the farm premises.  
- General farm liability policy probably won’t cover product liability claims because it is not the type of injury that is connected to the use of the farm premises.  
- It is best to ask your insurance agent if you would have coverage for a product liability claim, and if not, you may want to inquire as to whether “products liability” insurance is available for the types of products you sell. |
Source of Additional Information


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Overview

Lesson 2.5 will examine many of the legal concerns and liability questions associated with farmers' markets and you-pick operations. It will also address some insurance issues.

Objectives

1. Review legal considerations for participation in farmer's markets
2. Review legal considerations for you-pick operations
3. Address insurance needs for different types of direct marketing
Farmers’ Markets & You-Pick Operations

- Questions of liability
  - What if someone is injured?
  - What is my risk of being held liable?
  - Whose insurance covers it?
  - Do you need additional insurance?

Questions to Consider

- What have you done to insure the safety of customers that come on the property?
- Are you aware of any hazardous conditions on your property or with your machinery which have not been corrected?
- Have you trained all employees in the safe operation of machinery or tools?
- Do you know if your current insurance policies cover your direct farm marketing operation?

Legal Considerations for Farmers Markets

- Vendors at farmers’ markets are often asked to sign an agreement when they join.
- These agreements usually include:
  - Market rules
  - Restrictions on what can be sold
  - Insurance requirements
  - Terms of the membership
Legal Considerations for Farmers Markets

- What if there is an accident?
- What if there is an injury to a shopper?
- What about injuries to vendors?
- What about insurance?

Farmers' markets take different approaches
- Some have their own insurance
- The most common way is the insurance provision in the market agreement
  - Requires the vendor to have insurance with the market listed as an insured party

Legal Considerations for You-Pick Operations

- Inviting people on your property to engage in harvesting activities increases your liability risk
  - Customers may be unfamiliar with the equipment
  - Ladders may fall or customers may fall from ladders
  - Customers may be injured from the rough terrain
Legal Considerations for You-Pick Operations

- Premises Liability
- Negligence
  - Failure to exercise the care that a reasonably prudent person would exercise in like circumstances
- Duty of Care
  - Your level of responsibility

Premise Liability Issues

- Your duty of care — or responsibility — depends on why the person is on your property
- 3 Categories of People on Your Property
  - Trespasser
  - Licensee
  - Invitee

Premise Liability Issues

- Trespasser
  - On your property without permission
  - Lowest duty of care
- The most important thing to remember about trespassers is not to take the law into your own hands.
Premise Liability Issues

- **Licensee**
  - On the property for their benefit rather than yours
  - Higher duty of care than trespasser, but less than invitee

  You must warn of hidden dangers where they do not know or unlikely to know of the conditions or risks.

Premise Liability Issues

- **Invitee**
  - On the property for your benefit
  - Highest duty of care

  Customers on your land to harvest fruits and vegetables will be considered invitees.

Premise Liability Issues

- The customers on your land for your you-pick operation will be invitees.

- You must take precautions to protect your customers and employees.

- You owe them the highest level of responsibility under the law.
Legal Considerations for You-Pick Operations

- Several states have enacted laws to protect you-pick operations
  - Under these laws the operator is protected as long as he did not create an "unreasonable risk" or engage in "willful, wanton or reckless conduct"
- Several states also have agritourism liability statutes that offer similar protections

Insurance

- A great risk management tool
- Different types of insurance
- What is covered with each one

Insurance

- Comprehensive Farm Liability Policy
  - Covers activities that are considered “farming”
  - “ownership, maintenance or use of premises for the production of crops or the raising or care of livestock”
  - Some definitions include “operation of roadside stands”
  - Some do not
    - “farming does not include retail activity”
    - “other business pursuits” are excluded
Insurance

- Homeowner’s policy with excess liability coverage
  - Farming “on the side” as a second job
  - Depending on the insurance company, you may be able to obtain coverage for “incidental farming liability”

- Products Liability
  - Products Liability v. Premise Liability
  - General farm liability policy probably won’t cover product liability claims

References

Shannon Mirus, Landowner Liability Issues, presentation (2008)
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Twenty Questions to Ask About Your Farmers’ Market*

1. Who is the sponsor of the farmers’ market? Is it a local government or a non-profit?
2. Who owns the land on which it is located and are they responsible in case of accidents or injuries to shoppers?
3. Who is in charge of how the farmers’ market and who has authority to make decisions about how it is run, such as deciding who gets to set up in which location?
4. Is the farmers’ market a “producers only” market, meaning only farmers who produce food may sell it, or are other vendors and wholesale peddlers allowed to participate?
5. Does the farmers’ market provide for “carrying rules” which allow one farmer to sell food raised by another farmer?
6. What types of rules or regulations apply to your market participation, for example can you provide samples to customers?
7. What penalties apply for violating market rules, are there fines or can you be expelled from the market for serious violations?
8. If you are forced to leave the market or are unable to continue to come, is any portion of the seasonal fee you paid refundable?
9. What happens if you just miss one market day, do you lose your location in the market?
10. What is the procedure to be followed if there is a dispute over a rule violation, is there a committee of vendors and customers who decide the matter or does the market manager?
11. Does the market have all the necessary local business permits or licenses or do you need to obtain business permits for each of the farmers’ markets in which you participate?
12. Is the farmers’ market approved for participation in the USDA’s Women Infants and Children (WIC) Farmers’ Market Nutrition Program (FMNP) and the food stamp program?
13. If you want to sell products such as meat, poultry, eggs and canned or processed food is this allowed by the market rules and what licenses will you need to obtain?
14. How does the market manager make sure all of the vendors are not selling the same thing, such as sweet corn, so that people don’t start lowering prices?
15. Does the market carry insurance in case of accidents?
16. What type of insurance does the market expect you to have and what proof of insurance must you provide?
17. Do the market rules require the farm owner actually attend the market or can you send your employees to do the selling?
18. Does the market require you to submit a plan before the market season begins listing what you intend to produce and the approximate amounts?
19. Can the market officials visit your farm and inspect your operation and records?
20. Do the market rules place limits on how you can label or describe your products?

* Taken from The Legal Guide for Direct Farm Marketing by Neil D. Hamilton (1999).
Section 3 - Business and Financial Risk

Lesson 3.1  Starting and Managing a Business
Lesson 3.2  Developing a Business Plan
Lesson 3.3  Financial Record Keeping
Lesson 3.4  The Balance Sheet
Lesson 3.5  The Income Statement
Lesson 3.6  Cash Flow Budgeting
Lesson 3.7  Labor Management Issues
Lesson 3.8  Food Safety for Producers in Direct Marketing Venues
Lesson 3.1: Starting and Managing Your Business

Estimated time: One hour.

Overview

Lesson 3.1 will give cover basic issues prospective business owners should consider before starting a business. The characteristics of a successful entrepreneur will be discussed emphasizing three key traits. Some points to consider and questions to ask before starting a business will be covered and participants will be encouraged to complete a questionnaire from the Small Business Administration to explore these questions further. The top ten “DOs” and “Don’ts” of starting a business will help prospective business owners understand some of the basic and key steps to a successful startup. Nine questions regarding getting the most out of your agribusiness will give agriculture focused attendees additional decision making tools.

Objectives

1. List the three characteristics of a successful entrepreneur
2. Consider where the interest in running a small business comes from
3. Complete the checklist for going into business
4. Cover the DOs and Don’ts of starting a business
5. Explore ways to get the most out of your agribusiness

Assessment

Participants will view the presentation on starting and managing a business and participate throughout with questions and answers. The presenter will engage the audience to keep their interest and attention focused on the materials. Participants will take notes on provided handouts and will complete the SBA handout “Checklist for Going into Business”.

Equipment, Supplies, and Materials

1. Power Point presentation Lesson 3.1
2. Notes pages Lesson 3.1
3. Additional reading materials
4. Handout - Checklist for Going into Business
5. Handout - Ten Frequently Asked Questions for Micro and Home-Based Business Start-Up
References


Classroom Procedures

<table>
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| Slides 2-3: Introduction - Start off with a brief Q&A about why the participants are in attendance and assess prior knowledge. | • What kind of business are you considering starting?  
• Does anyone already operate their own business?  
• Why are you here? What do you want to get out of this lesson?  
• Review the overview and objectives for the lesson  |
| Slides 4: Characteristics of a Successful Entrepreneur                              | • The entrepreneur has an enthusiastic vision, the driving force of an enterprise.  
• The entrepreneur promotes the vision with enthusiastic passion.  
• With persistence and determination, the entrepreneur develops strategies to change the vision into reality.  
• The entrepreneur takes the initial responsibility to cause a vision to become a success.  
• Entrepreneurs take prudent risks. They assess costs, market/customer needs and persuade others to join and help.  
• An entrepreneur is usually a positive thinker and a decision maker.  |
| Slide 5: Determination (Guts)                                                        | • You must have an entrepreneurial instinct - an overwhelming desire to have your own business  
• Be completely devoted to your goal  
• Devotion to your goal is much more likely if you have a love for your intended business.  |
## Classroom Procedures Continued

<table>
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</thead>
</table>
| **Slide 6: Brains** | • The entrepreneur's vision is usually supported by an interlocked collection of specific ideas not available to the marketplace.  
• Appropriate educational credentials are important, entrepreneurial "brains" means more than scholastic achievements.  
• The working knowledge about the business is important. |
| **Slide 7-8: Capital** | • You will need seed money  
• Sufficient cash to maintain a positive cash flow for at least the first year  
• Possibly you don't need starting capital to hire other people because you might start by doing everything yourself  
• "Do it yourself" start is a good way to learn everything about your business and also makes you better qualified to delegate work to others later on.  
• You can control your risk by placing a limit on how much you invest in your business. |
| **Slide 9: Small Business a Good Fit** | • Is the risk worth the reward?  
• Are you physically and mentally tough enough to run your own business?  
• Will this be a full-time or part-time endeavor?  
• Are you passionate about running your own business?  
• Do you have seed money and access to finances to run your business? |
### Classroom Procedures Continued

<table>
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<th>Teaching Procedures</th>
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<tbody>
<tr>
<td><strong>Part-Time:</strong></td>
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<tr>
<td>1. It enables the part-time entrepreneur to earn and save more money to be used as capital for their business</td>
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<tr>
<td>2. It allows the part-time entrepreneur to save enough money to serve as a financial cushion for themselves and their families when they decide to pursue the business full-time.</td>
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<tr>
<td>3. There is uncertainty if the business will work, hence it is prudent to start more slowly</td>
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<tr>
<td>4. Balances out the uncertainty of starting a business. Even if the business proved to be a failure, the entrepreneur can still have the security of a regular paycheck from their jobs</td>
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<tr>
<td><strong>Full-Time:</strong></td>
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</tr>
<tr>
<td>1. More overall opportunities for your full-time business. Given that your day job occupies much of your time, there will be lots of opportunities that you will be unable to pursue for the business you run part-time.</td>
<td></td>
</tr>
<tr>
<td>2. Growth of the business will be very faster. Because of missed opportunities, a part-time business is more likely to be slow-growing.</td>
<td></td>
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<tr>
<td>3. Ability to give 100% focus - you need to focus daily on how to improve your business, how to reach your target market, and how you can be better than your competitors.</td>
<td></td>
</tr>
<tr>
<td>4. Business may not lend itself to be done on a part-time basis. The type of business you will start will determine whether a full-time job mixed with a part time business is doable.</td>
<td></td>
</tr>
<tr>
<td>5. Competing priorities. When you have a full-time job and a part-time business, you will inevitably be faced with tasks that are equally important.</td>
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</tr>
<tr>
<td>6. Fitting business and family obligations into a 24-hour period could be challenging.</td>
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</tbody>
</table>
### Classroom Procedures Continued

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
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</table>
| **Slides 13-17: Starting a Successful Business**          | • These slides contain some bullets summarizing tips for starting a successful business  
                                                          • Study the market you want to start a business in and be patient  
                                                          • Select the business that is right for your  
                                                          • Define your goals thoroughly  
                                                          • Challenge yourself but be realistic  
                                                          • Will your business be in a growth market?  
                                                          • Who can I work with?  
                                                          • Get completely qualified  
                                                          • Seek out experts in your field |
| **Slide 18: Handout - Checklist for Going into Business.**| • Instruct the participants to begin on page 4 and stop on page 13  
                                                          • Go through the instructions on page 4 then allow 10 minutes for the participants to fill out the checklist  
                                                          • Pages 14-17 in the Finance section are crucial, but not enough time to fill this part out during the presentation  
                                                          • Encourage them to finish the finance portion at home - it may be too timely for the time allotted here. |
| **Slides 19-22: Top Ten Do’s and Don’ts**                 | • These slides are a simple list of top do’s and don’ts  
                                                          • Cover the Top Ten DOs  
                                                          • Take time to interact with the group and ask questions  
                                                          • Cover the Top Ten Don’ts |
| **Slides 23-31: 9 questions for managing an agribusiness**| • These concluding slides have some tips for managing your agribusiness  
                                                          • Go through each slide presenting the information and examples  
                                                          • Ask audience members if there is anyone present who owns and/or operates an agribusiness |
| **Handout - Ten Frequently Asked Questions for Micro and Home-Based Business Start-Up** | • Encourage participants to read the handout and visit the links for more information |
Sources of Additional Information

   http://www.sba.gov/services/training/onlinecourses/index.html
   http://app1.sba.gov/training/sbprimer/assessment.htm
   http://pubs.cas.psu.edu/freepubs/pdfs/ua371.pdf
   http://leeds-faculty.colorado.edu/moyes/bplan/
5. USDA National Agricultural Library, Rural Information Center. Small Farm Funding.  
   http://www.nal.usda.gov/ric/ricpubs/small_farm_funding.htm#FPA
   http://www.agmrc.org/business_development/starting_a_business/index.cfm

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Starting and Managing Your Business

Lesson 3.1

Overview

- Cover basic issues prospective business owners should consider before starting a business
- Three characteristics of a successful entrepreneur are key to starting a business and running it well
- There are several questions to ask yourself before starting a business
- Some key tips to consider before starting a business and the top ten “Do’s” and “Don’ts”
- There are basic questions to ask yourself to make sure you are getting the most out of your agribusiness

Objectives

1. List the three characteristics of a successful entrepreneur
2. Consider where the interest in running a small business comes from
3. Complete the checklist for going into business
4. Cover the Do’s and Don’ts of starting a business
5. Explore ways to get the most out of your agribusiness
A Successful Entrepreneur

An entrepreneur should have three characteristics:

1) Determination (Guts)
2) Brains
3) Capital

The most common serious mistake made in business is not picking the right one to begin with.

Determination

Before starting your own business you must:

- Have an overwhelming desire to have your own business
- Start a business in something that you love to do
- Have the dedication to be completely devoted to your business through good times and bad times
- Be happy in your intended business

"Find something you love to do and you’ll never have to work a day in your life." Harvey McKay

Brains

To become a successful entrepreneur, you should have a working knowledge about the business you plan to start before you start it.

- Common sense, combined with appropriate experience, is the necessary brainpower.
- Prudence, follow through and attention to detail are very important.
Capital

☐ In every business, you need your own money to maintain a positive cash flow for at least a year

☐ Many businesses can be started on a very small scale with a small investment

☐ Then, as the business grows and you gain experience, cash flow from your business can be used for growth

Capital

☐ In some cases, you do not need starting capital to hire other people because you might start by doing everything yourself

☐ The "do it yourself" start is a good way to learn everything about your business and also makes you better qualified to delegate work to others later on

☐ You can control your risk by placing a limit on how much you invest in your business

Is Small Business a Good Fit?

☐ You are putting some (not all, hopefully) of your net worth at risk

☐ You may run the risk of working long hours, taking away from other family or pleasurable activities

☐ There may be levels of stress you have not experienced as an employee
Advantages of starting in your off hours while still working at your current job:

- You avoid losing earnings including retirement, health and vacations
- You can avoid conflict of interest with your job by choosing a business that is appropriate for your off hours (i.e., real estate, e-commerce or family-run operations)

Disadvantages of starting in your off hours while still working at your current job:

- There is a temptation to spend time at your job working on your other business
- Competing with your employer, which is not right
- Any kind of conflict with your regular work can jeopardize your job and your other business
- Overwork can cause mental and physical exhaustion

Full-Time or Part-Time

Advantages of starting in your off hours while still working at your current job:

- You can operate a family business
- Your family can run the business while you are at work
- You can teach your kids the benefits of being in business
A Successful Business

- If you have not yet selected a business, take your time and wait for the business that is just right for you.
- Do not pursue businesses that may be too challenging.
- Try to identify a business that has long-term economic potential.
- Operate a business that will grow in today's and tomorrow's markets.
- Bet on a business you know.

Be careful of …

- Being impatient.
- Being over confident.
- Not analyzing your business carefully.
- Not considering the negative aspects of your business.
- Not understanding every aspect of the business before you open its doors.

Selecting your Business

If you have not yet decided on a business, answer the following questions:

- Can I do what I love to do?
- Will I fill an expanding need for which there is no close substitute?
- Can I specialize?
- Can I learn it and test it first?
Selecting your Business

If you have not yet decided on a business, answer the following questions:

☐ Can I handle the capital requirements?
☐ Can I learn the business by working for someone else first?
☐ Should I consider a partner who has complementary skills or who could help finance the business?

Get Completely Qualified

Before you proceed further in your business, get completely qualified:

☐ The best way to become qualified is to go to work for someone in the same business
☐ Attend all classes you can on the skills you need: for example, accounting, computing and selling
☐ Read all the “How To” books you can
☐ Do not be afraid to ask questions or seek help from the most successful people in your intended business

Handout

Check-List for Going into Business
☐ Complete Pages 4 – 13 of the checklist
  ▪ Self-Analysis
  ▪ Personal Skills and Experience
  ▪ Finding a Niche
  ▪ Is Your Idea Feasible?
  ▪ Market Analysis
  ▪ Planning Your Start-Up

Section 3-12
### Top Ten “Do's”

1. Begin saving money
2. Begin a study on what business would be best for you
3. Begin working part-time in the kind of business you would like to start
4. Learn from people already in your business
5. Learn basic accounting, how to use a computer and how to navigate the Internet
6. Objectively measure your skills and training against potential competition
7. Remember that your financial commitment includes living expenses
8. Make a “for” and “against” list describing the business you are in or considering
9. Prepare a written business plan for your intended business
10. Test market your product or service before starting or expanding

### Top Ten “DO NOTs”

1. Quit your job before your business is in place and running
2. Consider operating a business in a field you do not enjoy
3. Incur new financial obligations above basic necessities
4. Sign any legal business document without your lawyer’s approval
5. Risk all the family assets. Limit your liabilities to a predetermined amount

---

Section 3-13
Top Ten “DO NOTs”

6. Be in a hurry to select a business
7. Depend on your banker to provide start-up capital
8. Commit to a concept without proving it first on a small basis
9. Commit to a business in which you must have the lowest cost to survive
10. Pick a business that is too high a risk

1. Are you farming efficiently?
   - Can you maintain current farm size without additional income off-farm?
   - Are you adopting appropriate technologies?
   - Do you have skills and/or experience to run a farm?
   - Do you manage efficiently:
     - Do things in a timely manner
     - Minimize waste
     - Maintain equipment

2. Are your resources and management ability adequate for new expansion?
   - Can manage addition/new responsibilities?
   - Do lender and farmer understand current resources and management limitations?
3. Do you have realistic price and yield estimates?

- Need to be conservative to provide a safety cushion
  - For example, assuming a 35 bushel yield when 25 is county average, or 11 pig/litter when 8 is state average, or omitting additional start-up costs are unrealistic
  - First year may not yield normal production, cost can exceed returns

4. Do you have adequate repayment plans?

- Are payments due when cash is running short?
  - Do not understate rapid repayment plan (repayment closer to life of particular asset)
  - Budget family living expenses properly
  - Schedule first “regular” payment to occur in second year of operation as costs are high in first year

5. Do you have control over your living expenses?

- Keep lifestyle in line with income
  - Prioritize expenses: e.g., 4 X 4 pickup for pleasure vs. travel funds for livestock shows vs. vacation
  - Clear major business purchases with lender

Section 3-15
6. Are you making excessive farm improvements?

- A dollar of improvement does not always add a dollar of value
- Do not spend all your cash on fixed improvements
  - Have cash available for other needs

7. Do you have multiple sources of credit?

- Commercial banks
- FCS
- Land contract
- FSA
- John Deere credit
- GMAC credit
- Sears
- Dillards
- Master Card
- finance companies
- unsecured creditors

Confusion over security and repayment priorities

8. Is there a lack of communication between the lender and the borrower (two-way street)?

- How much money is needed, for what and when?
- Where are proceeds from sales to go and when?
- Surprises are bad news!
- List all assets and debts on balance sheet: what for, when, and how much
9. Do you have adequate records?

- Budget cash flow
  - You know where the money goes
- Evaluate budget plans periodically
  - Was the plan accurate
- Provide income and expense records
  - Important for credit and business assistance programs

References


Sources of Additional Information

U.S. Small Business Administration
http://www.sba.gov/services/training/onlinecourses/index.html

Arkansas District Office
2120 Riverfront Drive, Suite 250
Little Rock, AR 72202-1786
Phone: (501) 324-7379
Fax: (501) 324-7394

Starting your Small Business
http://www.sba.gov/training/sbprimer/assessment.htm

Getting Assistance for your Project
http://www.uark.edu/ua/migrisk/
Sources of Additional Information


Rural Information Center- Small Farm Funding. http://www.nal.usda.gov/ric/ricpubs/small_farm_funding.htm#FPA


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Check-List for Going into Business

Management and Planning Series

U. S. Small Business Administration
April 2009

Helping Small Business Start, Grow and Succeed
Check-List for Going into Business

Management and Planning Series
MP - 12

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INTRODUCTION

Owning a business is the dream of many Americans ... starting that business converts your dream into reality. But there is a gap between your dream and reality that can only be filled with careful planning. As a business owner, you will need a plan to avoid pitfalls, to achieve your goals and to build a profitable business.

The Checklist for Going into Business is a guide to help you prepare a comprehensive business plan and determine if your idea is feasible, to identify questions and problems you will face in converting your idea into reality and to prepare for starting your business.

Operating a successful small business will depend on

- Practical plan with a solid foundation
- Dedication and willingness to sacrifice to reach your goal
- Technical skills
- Basic knowledge of management, finance, record keeping and market analysis

As a new owner, you will need to master these skills and techniques if your business is to be successful.
IDENTIFY YOUR REASONS

As a first and often overlooked step, ask yourself why you want to own your own business. Check the reasons that apply to you.

1. Freedom from the 9-5 daily work routine ______
2. Being your own boss ______
3. Doing what you want when you want to do it ______
4. Improving your standard of living ______
5. Boredom with your present job ______
6. Having a product or service for which you feel there is a demand ______

Some reasons are better than others, none are wrong; however, be aware that there are tradeoffs. For example, you can escape the 9-5 daily routine, but you may replace it with a 6 a.m. to 8 p.m. routine.
A SELF-ANALYSIS

Going into business requires certain personal characteristics. This portion of the checklist deals with you, the individual. These questions require serious thought. Try to be objective. Remember, it is your future that is at stake!

**Personal Characteristics**

<table>
<thead>
<tr>
<th>Question</th>
<th>YES</th>
<th>NO</th>
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<tbody>
<tr>
<td>Are you a leader?</td>
<td></td>
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<tr>
<td>Do you like to make your own decisions?</td>
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<td></td>
</tr>
<tr>
<td>Do others turn to you for help in making decisions?</td>
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<td></td>
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<tr>
<td>Do you enjoy competition?</td>
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<td></td>
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<td>Do you have will power and self discipline?</td>
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<tr>
<td>Do you plan ahead?</td>
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<td></td>
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<tr>
<td>Do you like people?</td>
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<td></td>
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<tr>
<td>Do you get along well with others?</td>
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</table>

**Personal Conditions**

This next group of questions though brief is vitally important to the success of your plan. It covers the physical, emotional, and financial strains you will encounter in starting a new business.

<table>
<thead>
<tr>
<th>Question</th>
<th>YES</th>
<th>NO</th>
</tr>
</thead>
<tbody>
<tr>
<td>Are you aware that running your own business may require working 12-16 hours a day six days a week and maybe even Sundays and holidays?</td>
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<tr>
<td>Do you have the physical stamina to handle the workload and schedule?</td>
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<tr>
<td>Do you have the emotional strength to withstand the strain?</td>
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<tr>
<td>Are you prepared if needed to temporarily lower your standard of living until your business is firmly established?</td>
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<tr>
<td>Is your family prepared to go along with the strains they too must bear?</td>
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<td></td>
</tr>
<tr>
<td>Are you prepared to lose your savings?</td>
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</tbody>
</table>
PERSONAL SKILLS AND EXPERIENCE

Certain skills and experience are critical to the success of a business. Since it is unlikely that you possess all the skills and experience needed you'll need to hire personnel to supply those you lack. There are some basic and special skills you will need for your particular business.

By answering the following questions you can identify the skills you possess and those you lack (your strengths and weaknesses).

YES       NO

1. Do you know what basic skills you will need in order to have a successful business? _____ _____

2. Do you possess those skills? _____ _____

3. When hiring personnel will you be able to determine if the applicants' skills meet the requirements for the positions you are filling? _____ _____

4. Have you ever worked in a managerial or supervisory capacity? _____ _____

5. Have you ever worked in a business similar to the one you want to start? _____ _____

6. Have you had any business training in school? _____ _____

7. If you discover you don't have the basic skills needed for your business will you be willing to delay your plans until you've acquired the necessary skills? _____ _____
FINDING A NICHE

Small businesses range in size from a manufacturer with many employees and millions of dollars in equipment to the lone window washer with a bucket and a sponge. Obviously the knowledge and skills required for these two extremes are far apart but for success they have one thing in common: each has found a business niche and is filling it.

The most critical problems you will face in your early planning will be to find your niche and determine the feasibility of your idea. Get into the right business at the right time is very good advice but following that advice may be difficult. Many entrepreneurs plunge into a business venture so blinded by the dream that they fail to thoroughly evaluate its potential.

Before you invest time effort and money the following exercise will help you separate sound ideas from those bearing a high potential for failure.
IS YOUR IDEA FEASIBLE?

1. Identify and briefly describe the business you plan to start.

____________________________________________________________________________________
____________________________________________________________________________________
____________________________________________________________________________________
____________________________________________________________________________________

2. Identify the product or service you plan to sell.

____________________________________________________________________________________

3. Does your product or service satisfy an unfilled need?  Yes _____ No _____

4. Will your product or service serve an existing market in which demand exceeds supply? Yes _____ No _____

5. Will your product or service be competitive based on its quality, selection, price or location? Yes _____ No _____

Answering yes to any of these questions means you are on the right track; a negative answer means the road ahead could be rough.
MARKET ANALYSIS

For a small business to be successful the owner must know the market. To learn the market you must analyze it, a process that takes time and effort. You don't have to be a trained statistician to analyze the marketplace nor does the analysis have to be costly.

Analyzing the market is a way to gather facts about potential customers and to determine the demand for your product or service.

The more information you gather the greater your chances of capturing a segment of the market. Know the market before investing your time and money in any business venture.

These questions will help you collect the information necessary to analyze your market and determine if your product or service will sell.

<table>
<thead>
<tr>
<th></th>
<th>YES</th>
<th>NO</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Do you know who your customers will be?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2. Do you understand their needs and desires?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>3. Do you know where they live?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>4. Will you be offering the kind of products or services that they will buy?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5. Will your prices be competitive in quality and value?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>6. Will your promotional program be effective?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>7. Do you understand how your business compares with your competitors?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>8. Will your business be conveniently located for the people you plan to serve?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>9. Will there be adequate parking facilities for the people you plan to serve?</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

This brief exercise will give you a good idea of the kind of market planning you need to do. An answer of no indicates a weakness in your plan so do your research until you can answer each question with a yes.
So far this checklist has helped you identify questions and problems you will face converting your idea into reality and determining if your idea is feasible. Through self-analysis you have learned of your personal qualifications and deficiencies and through market analysis you have learned if there is a demand for your product or service.

The following questions are grouped according to function. They are designed to help you prepare for "Opening Day."

### Name and Legal Structure

<table>
<thead>
<tr>
<th>YES</th>
<th>NO</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Have you chosen a name for your business?</td>
<td>_____ _____</td>
</tr>
<tr>
<td>2. Have you chosen to operate as sole proprietorship, partnership or corporation?</td>
<td>_____ _____</td>
</tr>
</tbody>
</table>

### Your Business and the Law

A person in business is not expected to be a lawyer but each business owner should have a basic knowledge of laws affecting the business. Here are some of the legal matters you should be acquainted with:

<table>
<thead>
<tr>
<th>YES</th>
<th>NO</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Do you know which licenses and permits you may need to operate your business?</td>
<td>_____ _____</td>
</tr>
<tr>
<td>2. Do you know the business laws you will have to obey?</td>
<td>_____ _____</td>
</tr>
<tr>
<td>3. Do you have a lawyer who can advise you and help you with legal papers?</td>
<td>_____ _____</td>
</tr>
</tbody>
</table>
| 4. Are you aware of
  - Occupational Safety and Health Administration (OSHA) requirements? | _____ _____ |
  - Regulations covering hazardous material? | _____ _____ |
  - Local ordinances covering signs snow removal etc.? | _____ _____ |
  - Federal Tax Code provisions pertaining to small business? | _____ _____ |
  - Federal regulations on withholding taxes and Social Security? | _____ _____ |
  - State Workmen's Compensation laws? | _____ _____ |
Protecting Your Business

It is becoming increasingly important that attention be given to security and insurance protection for your business. There are several areas that should be covered. Have you examined the following categories of risk protection?

- Fire
- Theft
- Robbery
- Vandalism
- Accident liability

Discuss the types of coverage you will need and make a careful comparison of the rates and coverage with several insurance agents before making a final decision.

Business Premises and Location

1. Have you found a suitable building in a location convenient for your customers?  
2. Can the building be modified for your needs at a reasonable cost?  
3. Have you considered renting or leasing with an option to buy?  
4. Will you have a lawyer check the zoning regulations and lease?

Merchandise

1. Have you decided what items you will sell or produce or what service(s) you will provide?  
2. Have you made a merchandise plan based upon estimated sales to determine the amount of inventory you will need to control purchases?  
3. Have you found reliable suppliers who will assist you in the start-up?  
4. Have you compared the prices quality and credit terms of suppliers?
Business Records

1. Are you prepared to maintain complete records of sales income and expenses accounts payable and receivables?  

2. Have you determined how to handle payroll records tax reports and payments?  

3. Do you know what financial reports should be prepared and how to prepare them?
A large number of small businesses fail each year. There are a number of reasons for these failures but one of the main reasons is insufficient funds. Too many entrepreneurs try to start and operate a business without sufficient capital (money). To avoid this dilemma you can review your situation by analyzing these three questions:

1. How much money do you have?
2. How much money will you need to start your business?
3. How much money will you need to stay in business?

Use the following chart to answer the first question:

**CHART 1 - PERSONAL FINANCIAL STATEMENT**

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>ASSETS</strong></td>
<td></td>
</tr>
<tr>
<td>Cash on hand</td>
<td></td>
</tr>
<tr>
<td>Savings account</td>
<td></td>
</tr>
<tr>
<td>Stocks, bonds, securities</td>
<td></td>
</tr>
<tr>
<td>Accounts/notes receivable</td>
<td></td>
</tr>
<tr>
<td>Real estate</td>
<td></td>
</tr>
<tr>
<td>Life insurance (cash value)</td>
<td></td>
</tr>
<tr>
<td>Automobile/other vehicles</td>
<td></td>
</tr>
<tr>
<td>Other liquid assets</td>
<td></td>
</tr>
<tr>
<td><strong>TOTAL ASSETS</strong></td>
<td></td>
</tr>
</tbody>
</table>

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>LIABILITIES</strong></td>
<td></td>
</tr>
<tr>
<td>Accounts payable</td>
<td></td>
</tr>
<tr>
<td>Notes payable</td>
<td></td>
</tr>
<tr>
<td>Contracts payable</td>
<td></td>
</tr>
<tr>
<td>Taxes</td>
<td></td>
</tr>
<tr>
<td>Real estate loans</td>
<td></td>
</tr>
<tr>
<td>Other liabilities</td>
<td></td>
</tr>
<tr>
<td><strong>TOTAL LIABILITIES</strong></td>
<td></td>
</tr>
</tbody>
</table>

**NET WORTH (Assets minus Liabilities)**
Chart 2 will help you answer the second question: How much money will you need to start your business? The chart is for a retail business; items will vary for service construction and manufacturing firms.

The answer to the third question (How much money will you need to stay in business?) must be divided into two parts: immediate costs and future costs.

**CHART 2 - START-UP COST ESTIMATES**

- Decorating, remodeling
- Fixtures, equipment
- Installing fixtures, equipment
- Services, supplies
- Beginning inventory cost
- Legal, professional fees
- Licenses, permits
- Telephone utility deposits
- Insurance
- Signs
- Advertising for opening
- Unanticipated expenses

**TOTAL START-UP COSTS**

From the moment the door to your new business opens a certain amount of income will undoubtedly come in. However this income should not be projected in your operating expenses. You will need enough money available to cover costs for at least the first three months of operation. Chart 3 will help you project your operating expenses on a monthly basis.

**CHART 3 - EXPENSES FOR ONE MONTH**

- Your living costs
- Employee wages
- Rent
- Advertising
- Supplies
- Utilities
- Insurance
- Taxes
- Maintenance
- Delivery/transportation
- Miscellaneous

**TOTAL EXPENSES**
Now multiply the total of Chart 3 by three. This is the amount of cash you will need to cover operating expenses for three months. Deposit this amount in a savings account before opening your business. Use it only for those purposes listed in the above chart because this money will ensure that you will be able to continue in business during the crucial early stages.

By adding the total start-up costs (Chart 2) to the total expenses for three months (three times the total cost on Chart 3) you can learn what the estimated costs will be to start and operate your business for three months. By subtracting the totals of Charts 2 and 3 from the cash available (Chart 1) you can determine the amount of additional financing you may need if any. Now you will need to estimate your operating expenses for the first year after start-up. Use the Income Projection Statement (Appendix A) for this estimate.

The first step in determining your annual expenses is to estimate your sales volume month by month. Be sure to consider seasonal trends that may affect your business. Information on seasonal sales patterns and typical operating ratios can be secured from your trade associations.

NOTE: The relationships among amounts of capital that you invest, levels of sales, each of the cost categories, the number of times that you will sell your inventory (turnover) and many other items form financial ratios. These ratios provide you with extremely valuable checkpoints before it's too late to make adjustments. In the reference section of your local library are publications such as The Almanac of Business and Industrial Financial Ratios to compare your performance with that of other similar businesses. For thorough explanations of these ratios and how to use them follow up on the sources of help and information mentioned at the end of this publication.

Next determine the cost of sales. The cost of sales is expressed in dollars. Fill out each month's column in dollars, total them in the annual total column, and then divide each item into the total net sales to produce the annual percentages. Examples of operating ratios include cost of sales to sales and rent to sales.
AFTER START-UP

The primary source of revenue in your business will be from sales but your sales will vary from month to month because of seasonal patterns and other factors. It is important to determine if your monthly sales will produce enough income to pay each month's bills.

An estimated cash flow projection (Chart 4) will show if the monthly cash balance is going to be subject to such factors as

- Failure to recognize seasonal trends
- Excessive cash taken from the business for living expenses
- Too rapid expansion
- Slow collection of accounts if credit is extended to customers

Use the following chart to build a worksheet to help you with this problem. In this example all sales are made for cash.

**CHART 4 - ESTIMATED CASH FLOW FORECAST**

<table>
<thead>
<tr>
<th></th>
<th>Jan</th>
<th>Feb</th>
<th>Mar</th>
<th>Apr</th>
<th>May</th>
<th>Jun</th>
<th>etc</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash in bank (1st of month)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Petty cash (1st of month)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Anticipated cash sales</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total receipts</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total cash &amp; receipts</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Disbursements for month</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(rent, loan payments, utilities, wages, etc.)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash balance (end of month)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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</tbody>
</table>
CONCLUSION

Beyond a doubt preparing an adequate business plan is the most important step in starting a new business. A comprehensive business plan will be your guide to managing a successful business. The business plan is paramount to your success. It must contain all the pertinent information about your business; it must be well written, factual and organized in a logical sequence. Moreover it should not contain any statements that cannot be supported.

If you have carefully answered all the questions on this checklist and completed all the worksheets you have seriously thought about your goal. But . . . there may be some things you may feel you need to know more about.

Owning and running a business is a continuous learning process. Research your idea and do as much as you can yourself but don't hesitate to seek help from people who can tell you what you need to know.
INFORMATION RESOURCES

The SBA offers an expansive network of business resources to assist small business customers. Use these resources to help build a successful business.

**Small Business Training Network (SBTN)**
The SBA operates a virtual campus featuring numerous free online courses. The courses cover a variety of topics, including how to start a business, finance, business planning, marketing, management, technology, government contracting and many other topics. Approximately 1,500 small business customers each day register for SBA’s free online courses.

**Small Business Development Centers (SBDC)**
The Office of Small Business Development Centers (SBDC) provides management assistance to current and prospective small business owners. SBDCs offer one-stop assistance to individuals and small businesses by providing a wide variety of information and guidance in central and easily accessible branch locations. The program is a cooperative effort of the private sector, the educational community and federal, state and local governments and is an integral component of Entrepreneurial Development's network of training and counseling services.

**SCORE**
SCORE (Counselors to America’s Small Business) is a resource partner of the SBA dedicated to entrepreneur education and the formation, growth and success of small businesses nationwide. There are more than 10,500 SCORE volunteers in 374 chapters operating in over 800 locations who assist small businesses with business counseling and training. SCORE also operates an active online training and counseling program.

**Women's Business Centers (WBC)**
Women's Business Centers represent a national network of nearly 100 educational centers designed to assist women. WBCs help entrepreneurs, especially women who are economically or socially disadvantaged, to start and grow successful small businesses.

**SBA District Offices**
In addition to its resource partners, the SBA operates full service district offices in every state of the country. Locate the district office closest to you.

**Other Targeted Resources**

<table>
<thead>
<tr>
<th></th>
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<tbody>
<tr>
<td>How to Prepare a Business Plan</td>
<td></td>
</tr>
</tbody>
</table>

**URL Directory of Hyperlinks**

<table>
<thead>
<tr>
<th>Resource</th>
<th>URL</th>
</tr>
</thead>
<tbody>
<tr>
<td>SCORE</td>
<td><a href="http://www.score.org/index.html">http://www.score.org/index.html</a></td>
</tr>
</tbody>
</table>
### SBA District Offices


<table>
<thead>
<tr>
<th>Have a Question?</th>
</tr>
</thead>
<tbody>
<tr>
<td>E-Mail SBA - <a href="mailto:answerdesk@sba.gov">answerdesk@sba.gov</a></td>
</tr>
<tr>
<td>Ask a <a href="http://www.score.org">SCORE counselor</a> online</td>
</tr>
<tr>
<td>Find a <a href="http://www.sba.gov/localresources/index.html">SBA district office</a> near you</td>
</tr>
<tr>
<td>Find a <a href="http://www.sba.gov/localresources/index.html">SBDC office</a> near you</td>
</tr>
</tbody>
</table>
# APPENDIX

## INCOME PROJECTION STATEMENT

<table>
<thead>
<tr>
<th>Industry %</th>
<th>J F M A M J J A S O N D</th>
<th>Annual total</th>
<th>Annual %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total net sales (revenues)</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Cost of sales</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Gross profit</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Gross profit margin</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

**Controllable expenses**

- Salaries/wages: -
- Payroll expenses: -
- Legal/accounting: -
- Advertising: -
- Automobile: -
- Office supplies: -
- Dues/subscriptions: -
- Utilities: -
- Miscellaneous: -

**Total controllable expenses**: -

**Fixed expenses**

- Rent: -
- Depreciation: -
- Utilities: -
- Insurance: -
- Licenses/permits: -
- Loan payments: -
- Miscellaneous: -

**Total fixed expenses**: -

**Total expenses**: -

Net profit (loss) before taxes: -

Taxes: -

Net profit (loss) after taxes: -
The income projection (profit and loss) statement is valuable as both a planning tool and a key management tool to help control business operations. It enables the owner-manager to develop a preview of the amount of income generated each month and for the business year, based on reasonable predictions of monthly levels of sales, costs and expenses.

As monthly projects are developed and entered into the income projection statement, they can serve as definite goals for controlling the business operation. As actual operating results become known each month, they should be recorded for comparison with the monthly projections. A completed income statement allows the owner-manager to compare actual figures with monthly projections and to take steps to correct any problems.

Industry Percentage

In the industry percentage column, enter the percentages of total sales (revenues) that are standard for your industry which are derived by dividing

\[ \text{cost/expense items by total net sales x 100\%} \]

These percentages can be obtained from various sources, such as trade associations, accountants or banks. The reference librarian in your nearest public library can refer you to documents that contain the percentage figures, for example, Robert Morris Associates' Annual Statement Studies (1 Liberty Place, Philadelphia PA 19103)

Industry figures serve as a useful benchmark against which to compare cost and expense estimates that you develop for your firm. Compare the figures in the industry column to those in the annual percentage column.

Total Net Sales (Revenues)

Determine the total number of units or products or services you realistically expect to sell each month in each department at the prices you expect to get. Use this step to create the projection to review your pricing practices.

- What returns, allowances and markdowns can be expected?
- Exclude any revenue that is not strictly related to the business.

Cost of Sales

The key to calculating your cost of sales is that you do not overlook any costs that you have incurred. Calculate cost of sales for all products and services used to determine total net sales. Where inventory is involved, do not overlook transportation costs. Also include any direct labor.

Gross Profit

Subtract the total cost of sales from the total net sales to obtain gross profit.

Gross Profit Margin.

The gross profit margin is expressed as a percentage of total sales (revenues) it is calculated by dividing

\[ \text{gross profits by total net sales} \]
Controllable Expenses

- *Salary expenses* -- Base pay plus overtime.
- *Payroll expenses* -- Include paid vacations, sick leave, health insurance, unemployment insurance and social security taxes.
- *Outside services* -- Include costs of subcontracts, overflow work and special or one-time services.
- *Supplies* -- Services and items purchase for use in the business.
- *Repairs and maintenance* -- Regular maintenance and repair, including periodic large expenditures such as painting.
- *Advertising* -- Include desired sales volume and classified directory advertising expenses.
- *Car, delivery and travel* -- Include charges if personal car is used in business, including parking, tolls, buying trips, etc.
- *Accounting and legal* -- Outside professional services.

Fixed Expenses

- *Rent* -- List only real estate used in the business
- *Depreciation* -- Amortization of capital assets.
- *Utilities* -- Water, heat, light, etc.
- *Insurance* -- Fire or liability on property or products. Include workers' compensation.
- *Loan repayments* -- Interest on outstanding loans.
- *Miscellaneous* -- Unspecified; small expenditures without separate accounts.
Net Profit (loss) (before taxes) → Subtract total expenses from gross profit

Taxes → Include inventory and sales taxes, excise tax, real estate tax, etc.

Net Profit (loss) (after taxes) → Subtract taxes from net profit (before taxes)

Annual Total → For each of the sales and expense items in your income projection statement, add all the monthly figures across the table and put the results in the annual total column
Ten Frequently Asked Questions for Micro and Home-Based Business Start-Up

Glenn Muske, Ph.D.
Home-Based and Micro Business Specialist

Questions? Questions are something every person starting or wanting to start a business has. And as soon as one question is answered another one arises. In fact, usually several questions exist all at the same time. Yet of all the questions that are asked, ten are the most frequent among entrepreneurs.

1. What business should I start?
2. Do I have what it takes to operate a home-based business?
3. What do I do first? Where do I start?
4. How should I set up my business? Should I be a sole proprietor?
5. What permits or licenses do I need?
6. How do I get people to buy my product/service?
7. What is a business plan and why do I need one?
8. What are the alternatives to help me finance my business?
9. What records do I need and how long do I keep them?
10. Where can I go for help?

1. What business should I start?

This is often the first question asked. You are the only person who can answer the question, “What business is best for me?” Begin with an exploration of your skills, abilities, and talents. Then ask, “How might I turn those skills and interests into a business?” Finally, consider if there is a market for the proposed product or service.

In reviewing the options available, consult with local experts and other business owners. Check with potential customers — are they interested enough to pay for the product or service proposed? The question is market need.

Your chance of success increases when you match a product or service with its potential market, whether local, statewide, national, or international.

2. Do I have what it takes to operate a home-based business?

This question is of great concern, yet the future entrepreneur often spends little time thinking about the answer. It is a question that should be answered prior to starting a business and the answer can only come from you. To answer “Do I have what it takes?” requires an objective appraisal of your own skills, abilities, and talents, as well as an assessment of your strengths, weaknesses, and personal situation.

Examine your skills, abilities, and talents and compare them to those of successful entrepreneurs:

- Am I a self starter?
- Do I get along well with others?
- Can I make good decisions?
- Do I have the physical and emotional stamina to run a business?
- How well do I plan and organize?
- Can I maintain my motivation?
- Can I work alone?
- Can I blend the business with the family?

Typically, the successful business owner will have one or more of the following qualities:

- Sound management practices
- Industry experience and/or support
- Technical experience and or support
- Planning ability

Few people start a business possessing all these qualities. Do an honest assessment of your own talents, skills, and experience. Then look for ways to compensate in areas that are weak. Compensating can mean tak-
Business start-up involves several early tasks. Remember to take your time and plan carefully. Do not rush through these or any other start up tasks. Some of the first tasks are:

- Selection and registration of the business name
- Deciding where to locate the business
- Getting the necessary licenses and permits
- Developing a business plan and a marketing plan
- Setting up production
- Determining a pricing schedule

4. How should I set up my business? Should I be a sole proprietor?

Most home-based and micro businesses are formed as sole proprietorships. The advantages of being a sole proprietor are simplicity and business income just becomes part of your personal tax return. The disadvantage is unlimited personal liability exposure.

Other legal business structure choices in Oklahoma include: Partnerships, general or limited; Corporations and S corporations; and Limited Liability companies or partnerships.

Each of these have various advantages and disadvantages depending on the situation. Contact expert legal and accounting help to determine which is the best legal structure for your business.

5. What permits or licenses do I need?

When aspiring business owners asks this question, they typically are asking about one of four issues: (1) licenses and permits required for the business; (2) zoning; (3) sales and use tax permits; or (4) employer identification numbers.

Licensing and permitting regulations vary from business to business, city to city, and state to state. Some businesses have minimal laws and regulations governing them and others are tightly controlled. Sources of assistance include the local county Cooperative Extension Service, the local city or county clerk’s office, Small Business Development Centers, and the local Chamber of Commerce. Also, check with the Service Corp of Retired Executives and the Small Business Administration. Often information can be obtained from the State Department of Commerce, local colleges/universities, and the business and industry services consultant at many vocational-technical schools. Remember that in some cases both you as an individual and the business itself must have separate licenses.

Zoning is a concern for all businesses. An excellent place to start with zoning questions is with the local city or county clerk’s office. Zoning is sometimes a greater problem for home-based business owners. Governing bodies, typically the local city or county, are cautious in allowing a business to operate in residential areas. They want to avoid problems with traffic, noise, fumes, signs, or parking. Obtain the proper zoning permit prior to opening your business. If businesses are prohibited, learn if there is a waiver provision or if the ordinance can be changed. Do not just start the business. Without the necessary permit or waiver, local authorities can close the business immediately. As the owner, you can face civil and /or criminal penalties. Even with the proper permits, the maintenance of good relations with neighbors is good business.

6. How do I get people to buy my product/service?

Typically, the business owner wants to know that people will buy his or her product or service. Without sales and the resulting income, it is impossible to pay the bills. Sales are a part of overall marketing efforts. Market research finds out who the customers are and what the customers want. The idea is to meet the customers’ needs—to sell what they want to buy.

The Oklahoma Cooperative Extension Service has developed marketing materials, “Mapping Your Marketing Future,” to help address the following marketing issues: (1) product—what are you producing and what benefits does it offer? (2) production—how is it produced, at what rate, and what raw materials and time are used? (3) price—at what price can the product or service be sold? (4) promotion—how will potential customers know about the product or service? (5) place—where is the business located and what distribution channels will be used? and (6) perception or image—how should the customer see the business and the product/service provided? All of these issues are a part of getting people to buy. Sales do not just happen. Sales happen because of an active marketing program. Marketing is essential for the survival of the business.

7. What is a business plan and why do I need one?

A business plan is the firm’s résumé and its goals and objectives. Develop a business plan as much for
yourself as for the partners, investors, and bankers involved with the business.

The business plan identifies the product/service, the market, and the management team. The plan defines where the business plans to operate and your business experience. Parts of the plan include a market study, promotional strategies, current and projected balance sheets, income statements, and cash flow analysis. It outlines how, when, and where financial support will be obtained and outlines a plan to repay those loans. It provides general operating information. A business plan helps clarify where the business is now, where it has been, and where it is going.

Business plans have three different uses. They are (1) feasibility plans and marketing plans; (2) operating/procedural plans for financial needs, production schedules, and marketing goals; and (3) tools to secure loans or outside capital.

There are many resources, such as Small Business Development Centers and the Service Corps of Retired Executives, available to help develop a business plan. Computer software programs that can guide plan development are available. Workshops for developing a business plan are offered by universities, community colleges, and vo-tech schools.

8. What are the alternatives to help me finance my business?

Your commitment of personal funds is often the first financing step. It is an indicator of how serious you are about the business. Risking personal money conveys your confidence to investors.

Personal investment sources of capital include savings, current cash flow, second job, home equity or equity from other property or assets, retirement accounts, personal lines of credit, and personal credit cards. All of these options include certain risks.

In addition to personal funds, family members and friends may be a source of financial help. Remember that successful loans from friends or relatives begin with a written document. The document must clearly define the amount of the loan, interest rates, payment dates, amounts, etc. All parties should agree to and sign the document.

Another financing option is to add a partner. Partnership terms also must be clear and in writing. Incorporation of the business is another way to raise equity financing. Such a decision is complex. Legal and accounting help should be obtained before taking such a step. Typically, the company must have a history before an investor will consider investing.

Another source of funds is commercial banks and other financial institutions. Loans can also be obtained from commercial finance companies and local development companies. However, venture capital firms and life insurance companies are typically not useful for the micro business owner.

An excellent source of financing information is your banker and the Small Business Administration. In Oklahoma, some vo-techs, as well as the local Chamber of Commerce and the Oklahoma Department of Commerce, have financing information. Another source of information is business incubators. Contact the local Chamber of Commerce about incubator locations.

Finally, Rural Enterprises, Inc. can offer financing assistance in most of Oklahoma.

One hint to minimize the amount of money borrowed is to consider leasing equipment and space instead of purchasing it. Also, it may be possible to rent equipment that is needed only for a limited time.

9. What records do I need and how long must I keep them?

The answer to this question is, “It depends.” The records needed to manage the business and the records the IRS wants to see may differ. For tax purposes, the IRS requires records that will allow for preparation and documentation of a completed tax return. The business owner is interested in where and how income is generated and where expenses are incurred.

There are, however, basic financial records all businesses keep: journals and ledgers, such as a checkbook register, accounts receivable, accounts payable, records of sales, inventory, cash receipts, and cash disbursements. Records must also document mileage, meal expenses, and entertainment. If the business hires employees, additional records are required.

Remember that all financial records are historical documents. This includes tax returns and the documentation for those returns. Business documents such as filing of the business name, incorporation/partnership papers, sales tax permit, federal employer identification number, and insurance records must be retained indefinitely. Some of these records, such as incorporation
papers, tax permits, etc. must be kept for three or more years after the business closes. For yearly tax returns, the IRS says to keep the records for three years after the filing of that year’s taxes. Records involving property must be kept for the entire time the property is owned, plus an additional three years minimum.

10. Where can I go for help?
There are a wide variety of local state and national resources to help answer these and other questions. The local county Cooperative Extension Office is a start. Ask for the State and National Resource Directory for Small, Micro and Home-Based Businesses.
Also, help is available from the Oklahoma Cooperative Extension Service (telephone 405-744-9931 and on the web at http://fcs.okstate.edu/microbiz).

Other sources include:
Small Business Administration  
800-827-5722 
www.sba.gov
Small Business Development Centers  
800-522-6154 (ask for the nearest office)  
www.osbdc.org
Service Corps of Retired Executives (SCORE)  
800-827-5722 (ask for nearest office)  
www.sba.gov
Business Information Center - OKC  
405-232-2376
Oklahoma Department of Commerce  
800-879-6552
Oklahoma Tax Commission  
800-522-8165  
www.oktax.state.ok.us
Rural Enterprises, Inc.  
800-658-2823  
www.ruralenterprises.com
Internal Revenue Service  
(Form SS-4, Employer Identification Number)  
800-829-3676  
www.irs.gov

Summary
These ten questions represent only the beginning questions the business owner faces. Business owners may also need answers about insurance, intellectual property issues, employee issues, and independent contractors, to name a few issues. The resources listed in this fact sheet are excellent places to get help for the additional questions you will have. Take advantage of these resources available to you, the business owner.

Resources

Other Reading

The information provided here is not intended as professional legal or accounting help. Contact an attorney and an accountant for advice specific to your business.
Lesson 3.2: Business Plan

Estimated time: An hour and a half.

Overview

Lesson 3.2 will help participants to understand the importance of creating a business plan. Participants will learn to define and to describe the components of a business plan. At end of the lesson is expected that participants will be able to draft a business plan. Participants will be provided with access to resources that can help to develop a more detailed business plan.

Objectives

1. Understand what a business plan is
2. Understand why to prepare a business plan is important
3. Understand the purpose of a business plan
4. Know the components of a business plan
5. Be able to prepare a draft business plan

Assessment

Participants will be encouraged to actively participate by asking questions and sharing their personal experiences. Participants will take notes on provided presentation handouts and will suggest new topics to be addressed in future presentations.

Equipment, Supplies, and Materials

1. Power Point presentation Lesson 3.2
2. Handouts for Lesson 3.2 (Business Plan) with space for notes
3. Paper and marker to write participants comments
4. Business plan template
5. Balance sheet, Income statement and cash flow templates (optional)
References


Classroom Procedures

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
<tbody>
<tr>
<td>Slide 1: Welcome</td>
<td>• Facilitator welcomes the participants and outlines the program and process of the workshop</td>
</tr>
<tr>
<td>Slides 2 – 3: Introduction</td>
<td>• Overview of the topic and the objectives of the presentation</td>
</tr>
<tr>
<td>Slide 4: What is a business plan?</td>
<td>• Define what business plan is</td>
</tr>
<tr>
<td></td>
<td>• Explain what a clear business plain contain</td>
</tr>
<tr>
<td>Slide 5: What is the purpose of a business plan?</td>
<td>• List the two main purposes of a business plan</td>
</tr>
<tr>
<td>Slide 6: Why is planning important?</td>
<td>• Ask for a volunteer to answer the questions in the slide</td>
</tr>
<tr>
<td>Slide 7: Why to prepare a business plan?</td>
<td>• Explain why a business plan is useful</td>
</tr>
<tr>
<td></td>
<td>• Encourage people to have someone to review their business plan (use the tip at the bottom of the slide)</td>
</tr>
<tr>
<td>Slide 8: What to avoid in a business plan?</td>
<td>• List what to avoid and give the potential solution (what to do)</td>
</tr>
</tbody>
</table>
## Classroom Procedures Continued

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
<tbody>
<tr>
<td>Slides 9 - 10: Business Plan Components</td>
<td>• Define business plan emphasizing all the components</td>
</tr>
<tr>
<td>Slides 11 - 20: Components</td>
<td>• Describe each component and give some examples when relevant</td>
</tr>
</tbody>
</table>
| Slides 21 - 24: Financial Management    | • The facilitator should ask participants if they are familiar with Microsoft Excel. If so, the facilitator should use the balance sheet, income statement and cash flow templates to show how with little input and effort they can get quick picture of the financial situation of their business.  
• Also, the facilitator can print the templates and give three to each participant (one for each tool) and let them to enter the information by hand (at discretion of the facilitator) |
| Slides 25: Draft Business Plan          | • Facilitator should divide the group in sub-groups of three to four people.                                             |
|                                          | • Using the SBA_BP template participants should write a business plan.                                                    |
|                                          | • They can use information for any of the participants in the group.                                                     |
|                                          | • This activity can take from 15 to 20 minutes.                                                                         |
| Slides 26 - 27: Summarize presentation  | Quick review about:                                                                                                    |
|                                          | • What a business plan is                                                                                               |
|                                          | • What the components are                                                                                                |
|                                          | • Review the financial tools                                                                                           |
| Questions                                | Answer any specific questions                                                                                          |
| Website (If internet is available)       | • Facilitator should enter to http://www.sba.gov/smallbusinessplanner/index.html and quickly explore the web-site     |
Sources of Additional Information

2. My own business online course  
3. How to start a business  
   [http://www.uark.edu/ua/mngrisk/Fact%20Sheets/English/How%20to%20start%20a%20business.pdf](http://www.uark.edu/ua/mngrisk/Fact%20Sheets/English/How%20to%20start%20a%20business.pdf)
4. Net Worth Statement 
5. Manage Your Risk  [www.manageryourrisk.net](http://www.manageryourrisk.net)
7. The agriculture, fisheries and small business website (AgPlan). Free Software  
8. Samples of business planes  [http://www.bplans.com/samples/sba.cfm](http://www.bplans.com/samples/sba.cfm)
10. Small business develop center  
12. Small business development training network  
   [http://www.sba.gov/services/training/onlinecourses/index.html](http://www.sba.gov/services/training/onlinecourses/index.html)

Contact Information

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Division of Agriculture  
501-671-2175  
[rrainey@uaex.edu](mailto:rrainey@uaex.edu)
Developing a Business Plan

Lesson 3.2

Overview

- Help participants to understand the importance of creating a business plan.
- Define and describe the components of a business plan.
- Provide access to resources that can help to develop a business plan.

Objectives

1. Understand what a business plan is
2. Understand why to prepare a business plan is important
3. Understand the purpose of a business plan
4. Know the components of a business plan
5. Be able to prepare a draft business plan
What is a Business Plan?

A Business Plan is a written outline that evaluates all aspects of the economic viability of your business. In other words, it is the roadmap that helps you improve the management of your business.

According to the (SBA, 2009) a clear business plan explains:

- Who you are
- Why you are in business
- What you do
- How you do it
- Where you operate
- How you generate profits
- How your customers are
- Why your business is important

Purpose of a Business Plan?

- According to McCorke and Bevers a business plan has two purposes:

1. Help the business management team make decisions to meet the specified objectives and goals; and

2. Help sell the feasibility of the business to bankers and other potential investors when requesting needed capital.

Why is Planning important?

According to the U.S. Small Business Administration (SBA, 2009) you should answer the following questions before writing a business plan:

- What services or products does your business provide?
- What needs does it fill?
- Who are the potential customers of your service or product?
- Why should they buy it from you?
- How will you reach your potential customers?
- Where will you get the financial resources to start or run your business?
Why to Prepare a Business Plan?

- A business plan is useful in many ways:
  - It will define and focus your objective using appropriate information and analysis.
  - It uncovers omissions and/or weaknesses in your planning process.
  - It demonstrates the business has a plan and is well managed.
  - It is a selling tool when dealing with important relationships including your banks, lenders and investors.

  Tip: Write down the names, addresses and phone numbers of key people that might review your business plan. For instance, family members, banker, lawyer, attorney, potential customers, investors, etc.

What to Avoid in a Business Plan?

Avoid

1. Not placing some reasonable limits on long-term, future projections. (Long-term means over one year.)
2. Few business plans correctly anticipate how much money and time will be required.
4. Use of sophisticated and complicate language.

Try this

1. Stick with short-term objectives and modify the plan as your business progresses.
2. Be extremely conservative in predicting capital requirements, timelines, sales and profits.
3. Write down your strategies in the event of business adversities.
4. Make it easy to read and understand. Use simple language in explaining the issues.

Business Planning

- The Business Plan format is a systematic assessment of all the factors critical to your business purpose and goals.

Business Plan Components

Here are some suggested topics you can tailor into your plan:
- Table of contents
- Executive summary
- Business description and mission
- Definition of the market
- Description of services and products
- Organization and management
- Marketing and sales strategies
- Financial Management

Table of contents

- Brings organization to the business plan
- List key sections
- Assist the reader in locating specific sections

Executive Summary

- Provides an overview of:
  - who you are,
  - what you do
  - why you do it.
- Write this last. It is just a page or two of highlights.
Business Description and Mission

- Mission statement.
  - Who the company is and what it stands for
- Vision statement
  - Outlines what the company wants to be in the future.
- Business goals and objectives
  - Business goals should describe what you want from your business
- Business Profile
  - Define and describe your intended business and exactly how you plan to go about it. Focus on the market you plan to serve

Definition of the Market

- Describe and give an outlook of your business industry
  - Industry Analysis
  - Industry Participants
  - Market Trends
  - Market Growth
- Describe the specific customer needs that your business will satisfy
  - Highlight your competitive position within your industry, and describe how you are positioned to be successful.

Description of Services or Products

- Describe what you are selling
- Explain product pricing (Pricing strategy)
- Describe how your product or service is competitive
- Focus on customer benefits
Organization and Management

- Describe how the company is organized
- Explain how things get done
- Document that you have the management and personnel resources necessary to run your business or a plan to obtain them
- Communicate that the business has a sound production management strategy
- Include bios of key company managers and their management responsibilities

Marketing Plan and Sales Strategies

- Your marketing plan describes (Eggers and Popp, 2009)
  - what you are marketing,
  - how you will market your products,
  - when you will market your products,
  - to whom you will sell your products
- It also describes what is occurring in the broader market regarding your products and your competitors and discuss how that will impact your business

Marketing Plan and Sales Strategies

- According to McCorkle and Bevers, the plan should give some analysis of:
  - current market situation
  - how the market will be like in the next 3 to 5 years
- This type of long-range market analysis can:
  - address projected U.S. production
  - total supply and demand,
  - federal farm programs,
  - cycles and other factors.
Marketing Plan and Sales Strategies

- To create new customers try to:
  - Build relationships with your customers
  - Be different and stand out from the competition
  - Offer goods and services the customers want at best place, time and right quantities
  - Establish a fair and competitive price

Marketing and Sales Strategies

- Create a marketing strategy by:
  - Identifying groups you can best serve
  - Understanding customers needs
  - Adapting to the changes in the market

- Explain your market strategic specific to the four P’s of marketing:
  - Promotion
  - Place
  - Production
  - Price

Financial Management

- Communicate your business’ financial situation by using the following tools:
  - Balance sheet – solvency
  - Income statement – profitability
  - Cash flow plan – liquidity

- Describe the assumptions you used to make your financial projections.
Financial Management

- Balance sheet – measures business value

  Assets – Liabilities = Net Worth

  Example - Balance Sheet Template (SBA, 2009)

---

Financial Management

- Income Statement – measures how a business has performed over a specific period of time

  Revenue – Expenses = Profit/Loss

  Example - Income Statement Template (SBA, 2009)

---

Financial Management

- Cash Flow – monthly statement of cash on hand, incoming cash and expenses

  Example - Cash Flow Template (SBA, 2009)
Example – Draft a Business Plan Template (SBA, 2009)

According to Eggers and Popp (2009) a business plan should:
- Have an executive summary
- Be concise and to the point
- Be reviewed by someone with experience
- Communicate clearly what you do, how you do it and why you do it

Remember to use the business plan
- Distribute copies to those involved in business
- Review plan periodically
- Monitor progress
- Keep records
- Compare actual outcomes to projected outcomes
- Make changes to plan as needed
References


https://agrilifebookstore.org/tmppdfs/viewpdf_1506_4744.pdf?CFID=1139654&CFTOKEN=51100911&spresoid=00300566c73a3f823308360010a93c73d

North Carolina State University. Basic elements of a Business Plan
http://transylvania.ces.ncsu.edu/content/Busplanbasics&source=transylvania

U.S. Small Business Administration (2009)
http://www.sba.gov/smallbusinessplanner/index.html

Sources of Additional Information

U.S. Small Business Administration
http://www.sba.gov/smallbusinessplanner/index.html

How to write a business plan
http://aap1.sba.gov/training/study/index.htm

My own business online course
http://www.myownbusiness.org/certcourse/downloads_non.html

How to start a business
http://www.uark.edu/ua/mngrisk/Fact%20Sheets/English/How%20to%20start%20a%20business.pdf

Net Worth Statement

Manage Your Risk
www.managemyrisk.net

FinPack Business Plan.

The agriculture, fisheries and small business website (AgPlan) Free Software

Samples of business plans
http://www.bplans.com/samples/sba.cfm

Section 3-60
Sources of Additional Information

Counselor's to America's Small Business. http://www.score.org/index.html
Small business development center
http://www.sba.gov/aboutsba/sbaprograms/sbdc/sbdclocator/SBDC_LOCATOR.html
Women’s business center
Small business development training network
http://www.sba.gov/services/training/onlinecourses/index.html

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Five Important Tips
Before You Start!

1. The business plan should tell a compelling story about your business, explaining who, what, when, where, how and why.
2. Your plan should be focused and clear. It’s not about the number of pages or style of the cover.
3. The plan should define specific business objectives and goals with general parameters to guide the organization.
4. Writing a business plan should force logic and discipline into a business.
5. A good business plan is a living document. It should be updated regularly.
<table>
<thead>
<tr>
<th>Section</th>
<th>Title</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Table of Contents</td>
</tr>
<tr>
<td>2</td>
<td>Executive Summary</td>
</tr>
<tr>
<td>3</td>
<td>Business Description &amp; Vision</td>
</tr>
<tr>
<td>4</td>
<td>Definition of the Market</td>
</tr>
<tr>
<td>5</td>
<td>Description of Products and Services</td>
</tr>
<tr>
<td>6</td>
<td>Organization &amp; Management</td>
</tr>
<tr>
<td>7</td>
<td>Marketing and Sales Strategy</td>
</tr>
<tr>
<td>8</td>
<td>Financial Management</td>
</tr>
<tr>
<td>9</td>
<td>Appendices</td>
</tr>
</tbody>
</table>
## Executive Summary

<table>
<thead>
<tr>
<th>This section should:</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>• Be written last</td>
<td>• Provide an enthusiastic snapshot of your company,</td>
</tr>
<tr>
<td></td>
<td>explaining who you are, what you do and why</td>
</tr>
<tr>
<td></td>
<td>• Be less than 2 pages</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>After reviewing this section the reader should:</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>• Want to learn more about your business</td>
<td>• Have a basic understanding about your company</td>
</tr>
</tbody>
</table>

Start here…
# Business Description & Vision

| This section should include: | • Mission statement (business purpose)  
|                            | • Company vision (statement about company growth)  
|                            | • Business goals and objectives  
|                            | • Brief history of the business  
|                            | • List of key company principals |

| After reviewing this section the reader should know: | • Who the business is and what it stands for  
|                                                       | • Your perception of the company’s growth & potential  
|                                                       | • Specific goals and objectives of the business  
|                                                       | • Background information about the company |

Start here.....
## Definition of the Market

<table>
<thead>
<tr>
<th>This section should:</th>
<th></th>
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</thead>
<tbody>
<tr>
<td>• Describe your business industry and outlook</td>
<td></td>
</tr>
<tr>
<td>• Define the critical needs of your perceived or existing market</td>
<td></td>
</tr>
<tr>
<td>• Identify your target market</td>
<td></td>
</tr>
<tr>
<td>• Provide a general profile of your targeted clients</td>
<td></td>
</tr>
<tr>
<td>• Describe what share of the market you currently have and/or anticipate</td>
<td></td>
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</tbody>
</table>

<table>
<thead>
<tr>
<th>After reviewing this section the reader should know:</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>• Basic information about the industry you operate in and the customer needs you are fulfilling</td>
<td></td>
</tr>
<tr>
<td>• The scope and share of your business market, as well as who your target customers are</td>
<td></td>
</tr>
</tbody>
</table>

Start here…..
## Description of Products and Services

<table>
<thead>
<tr>
<th>This section should:</th>
<th>❑ Specifically describe all of your products and services</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>❑ Explain how your products and services are competitive</td>
</tr>
<tr>
<td></td>
<td>❑ If applicable, reference a picture or brochure of your</td>
</tr>
<tr>
<td></td>
<td>products, which would be included in the plan’s appendix</td>
</tr>
</tbody>
</table>

| After reviewing this section the reader should know:        | ❑ Why you are in business                                  |
|                                                            | ❑ What your products and services are and how much they    |
|                                                            |   sell for                                                 |
|                                                            | ❑ How and why your products & services are competitive     |

Start here.....
# Organization & Management

<table>
<thead>
<tr>
<th>This section should:</th>
<th></th>
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</thead>
<tbody>
<tr>
<td>• Provide a description of how your company is organized as well as an organization chart, if available</td>
<td></td>
</tr>
<tr>
<td>• Describe the legal structure of your business (proprietorship, partnership, corporation, etc.)</td>
<td></td>
</tr>
<tr>
<td>• Identify necessary or special licenses and/or permits your business operates with</td>
<td></td>
</tr>
<tr>
<td>• Provide a brief bio description of key managers within the company</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>After reviewing this section the reader should know:</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>• The legal form of ownership for your business</td>
<td></td>
</tr>
<tr>
<td>• Who the leaders are in your business as well as their roles</td>
<td></td>
</tr>
<tr>
<td>• The general flow of operations within the firm</td>
<td></td>
</tr>
</tbody>
</table>

Start here…..
# Marketing and Sales Strategy

**This section should:**
- Identify and describe your market – who your customers are and what the demand is for your products & services
- Describe your channels of distribution
- Explain your sales strategy, specific to pricing, promotion, products and place (4Ps)

**After reviewing this section the reader should:**
- Who your market is and how you will reach it
- How your company will apply pricing, promotion, product diversification and channel distribution to sell your products and services competitively

Start here.....
### Financial Management

<table>
<thead>
<tr>
<th>This section should include:</th>
<th>New Business</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Click here:</strong> for automated Balance Sheet template</td>
<td>• Estimate of start-up costs</td>
</tr>
<tr>
<td><strong>Click here:</strong> for automated Income Statement template</td>
<td>• Projected balance sheet (1 year forward)</td>
</tr>
<tr>
<td><strong>Click here:</strong> for automated Cash Flow Statement template</td>
<td>• Projected income statement (1 year forward)</td>
</tr>
<tr>
<td></td>
<td>• Projected cash flow statement (12 months forward)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Existing Business</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Balance sheets (last 3 years)</td>
</tr>
<tr>
<td>• Income statements (last 3 years)</td>
</tr>
<tr>
<td>• Cash flow statement (12 months)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>If Applying for a Loan</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Current personal financial statement on each principal</td>
</tr>
<tr>
<td>• Federal tax return for prior year</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>After reviewing this section the reader should:</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Have a good understanding regarding the financial capacity and/or projections for your company</td>
</tr>
</tbody>
</table>

Start here…..
## Appendices

| This section should include as attachments:               | • Company brochures                                                                 |
|                                                       | • Resumes of key employees                                                          |
|                                                       | • List of business equipment                                                        |
|                                                       | • Copies of press articles and advertisements (if available)                        |
|                                                       | • Pictures of your business location and products (optional)                        |
|                                                       | • Information supporting the growth of your industry and/or products (optional)     |
|                                                       | • Key business agreements, such as lease, contracts, etc. (optional)                |

Start here…..
This automated form is made available compliments of CCH Business Owner's Toolkit

[Your Business Name]
Balance Sheet
[Mmm Dd, 200X]

<table>
<thead>
<tr>
<th>Assets</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Current Assets:</strong></td>
<td></td>
</tr>
<tr>
<td>Cash</td>
<td>$0</td>
</tr>
<tr>
<td>Accounts Receivable</td>
<td>$0</td>
</tr>
<tr>
<td>Less: Reserve for Bad Debts</td>
<td>0 0</td>
</tr>
<tr>
<td>Merchandise Inventory</td>
<td>0</td>
</tr>
<tr>
<td>Prepaid Expenses</td>
<td>0</td>
</tr>
<tr>
<td>Notes Receivable</td>
<td>0</td>
</tr>
<tr>
<td><strong>Total Current Assets</strong></td>
<td>$0</td>
</tr>
<tr>
<td><strong>Fixed Assets:</strong></td>
<td></td>
</tr>
<tr>
<td>Vehicles</td>
<td>0</td>
</tr>
<tr>
<td>Less: Accumulated Depreciation</td>
<td>0 0</td>
</tr>
<tr>
<td>Furniture and Fixtures</td>
<td>0</td>
</tr>
<tr>
<td>Less: Accumulated Depreciation</td>
<td>0 0</td>
</tr>
<tr>
<td>Equipment</td>
<td>0</td>
</tr>
<tr>
<td>Less: Accumulated Depreciation</td>
<td>0 0</td>
</tr>
<tr>
<td>Buildings</td>
<td>0</td>
</tr>
<tr>
<td>Less: Accumulated Depreciation</td>
<td>0 0</td>
</tr>
<tr>
<td>Land</td>
<td>0</td>
</tr>
<tr>
<td><strong>Total Fixed Assets</strong></td>
<td>$0</td>
</tr>
<tr>
<td><strong>Other Assets:</strong></td>
<td></td>
</tr>
<tr>
<td>Goodwill</td>
<td>0</td>
</tr>
<tr>
<td><strong>Total Other Assets</strong></td>
<td>$0</td>
</tr>
<tr>
<td><strong>Total Assets</strong></td>
<td>$0</td>
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</tbody>
</table>

<table>
<thead>
<tr>
<th>Liabilities and Capital</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Current Liabilities:</strong></td>
<td></td>
</tr>
<tr>
<td>Accounts Payable</td>
<td>$0</td>
</tr>
<tr>
<td>Sales Taxes Payable</td>
<td>0</td>
</tr>
<tr>
<td>Payroll Taxes Payable</td>
<td>0</td>
</tr>
<tr>
<td>Accrued Wages Payable</td>
<td>0</td>
</tr>
<tr>
<td>Unearned Revenues</td>
<td>0</td>
</tr>
<tr>
<td>Short-Term Notes Payable</td>
<td>0</td>
</tr>
<tr>
<td>Short-Term Bank Loan Payable</td>
<td>0 0</td>
</tr>
<tr>
<td><strong>Total Current Liabilities</strong></td>
<td>$0</td>
</tr>
<tr>
<td><strong>Long-Term Liabilities:</strong></td>
<td></td>
</tr>
<tr>
<td>Long-Term Notes Payable</td>
<td>0</td>
</tr>
<tr>
<td>Mortgage Payable</td>
<td>0</td>
</tr>
<tr>
<td><strong>Total Long-Term Liabilities</strong></td>
<td>0</td>
</tr>
<tr>
<td><strong>Total Liabilities</strong></td>
<td>0</td>
</tr>
</tbody>
</table>

**Capital:**
- Owner's Equity: 0
- Net Profit: 0

**Total Capital**: 0

**Total Liabilities and Capital**: $0
## Income Statement

**For the Year Ended [Mmmm Dd, 200X]**

### Revenue:
- **Gross Sales**: $0.00
- **Less: Sales Returns and Allowances**: $0.00
- **Net Sales**: $0.00

### Cost of Goods Sold:
- **Beginning Inventory**: $0.00
- **Add: Purchases**: $0.00
  - **Freight-in**: $0.00
  - **Direct Labor**: $0.00
  - **Indirect Expenses**: $0.00
  - **Total**: $0.00
- **Less: Ending Inventory**: $0.00
- **Cost of Goods Sold**: $0.00
- **Gross Profit (Loss)**: $0.00

### Expenses:
- **Advertising**: $0.00
- **Amortization**: $0.00
- **Bad Debts**: $0.00
- **Bank Charges**: $0.00
- **Charitable Contributions**: $0.00
- **Commissions**: $0.00
- **Contract Labor**: $0.00
- **Credit Card Fees**: $0.00
- **Delivery Expenses**: $0.00
- **Depreciation**: $0.00
- **Dues and Subscriptions**: $0.00
- **Insurance**: $0.00
- **Interest**: $0.00
- **Maintenance**: $0.00
- **Miscellaneous**: $0.00
- **Office Expenses**: $0.00
- **Operating Supplies**: $0.00
- **Payroll Taxes**: $0.00
- **Permits and Licenses**: $0.00
- **Postage**: $0.00
- **Professional Fees**: $0.00
- **Property Taxes**: $0.00
- **Rent**: $0.00
- **Repairs**: $0.00
- **Telephone**: $0.00
- **Travel**: $0.00
- **Utilities**: $0.00
- **Vehicle Expenses**: $0.00
- **Wages**: $0.00
- **Total Expenses**: $0.00

### Net Operating Income
- **Net Operating Income**: $0.00

### Other Income:
- **Gain (Loss) on Sale of Assets**: $0.00
- **Interest Income**: $0.00
- **Total Other Income**: $0.00

### Net Income (Loss)
- **Net Income (Loss)**: $0.00
<table>
<thead>
<tr>
<th></th>
<th>[Month]</th>
<th>[Month]</th>
<th>[Month]</th>
<th>[Month]</th>
<th>[Month]</th>
<th>Total</th>
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<td><strong>Beginning Cash Balance</strong></td>
<td>$0</td>
<td>$0</td>
<td>$0</td>
<td>$0</td>
<td>$0</td>
<td>$0</td>
</tr>
<tr>
<td><strong>Cash Inflows (Income):</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accts. Rec. Collections</td>
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<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Loan Proceeds</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Sales &amp; Receipts</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Other</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
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<tr>
<td><strong>Total Cash Inflows</strong></td>
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<td>$0</td>
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<td>$0</td>
<td>$0</td>
<td>$0</td>
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<td>$0</td>
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<tr>
<td><strong>Cash Outflows (Expenses):</strong></td>
<td></td>
<td></td>
<td></td>
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<td>Bank Service Charges</td>
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<td>Miscellaneous</td>
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<tr>
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<td>0</td>
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<td>Payroll Taxes</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
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<td>Professional Fees</td>
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<td>0</td>
<td>0</td>
<td>0</td>
</tr>
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<td>Taxes &amp; Licenses</td>
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<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Utilities &amp; Telephone</td>
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<td>0</td>
<td>0</td>
<td>0</td>
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<tr>
<td><strong>Subtotal</strong></td>
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<td>$0</td>
<td>$0</td>
<td>$0</td>
<td>$0</td>
<td>$0</td>
</tr>
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<td><strong>Other Cash Out Flows:</strong></td>
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<td></td>
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<td></td>
</tr>
<tr>
<td>Capital Purchases</td>
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</tr>
<tr>
<td>Loan Principal</td>
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<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Owner's Draw</td>
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<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
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<tr>
<td>Other</td>
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<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
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</tr>
<tr>
<td><strong>Subtotal</strong></td>
<td>$0</td>
<td>$0</td>
<td>$0</td>
<td>$0</td>
<td>$0</td>
<td>$0</td>
</tr>
<tr>
<td><strong>Total Cash Outflows</strong></td>
<td>$0</td>
<td>$0</td>
<td>$0</td>
<td>$0</td>
<td>$0</td>
<td>$0</td>
</tr>
<tr>
<td><strong>Ending Cash Balance</strong></td>
<td>$0</td>
<td>$0</td>
<td>$0</td>
<td>$0</td>
<td>$0</td>
<td>$0</td>
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</tbody>
</table>
Lesson 3.3: Financial Record Keeping

Estimated time: One hour.

Overview

Lesson 3.3 will inform participants about some basic credit usage statistics for farmers and ranchers and introduce concepts of financial record keeping. Participants will learn who farms, who uses debt and the main sources of credit. The 5 C’s of Credit will help give prospective entrepreneurs information about seeking lines of credit to help operate the business. The key components of a good financial record keeping system will be discussed and participants will consider the effectiveness of using a computer for this task. They will understand the differences between cash and accrual accounting, learn a good source for basic financial statements is the extension office and cover some Do’s and Don’ts for farm record keeping.

Objectives

1. List the Five C’s of Credit
2. Identify the requirements for a sound financial record keeping system
3. Recognize the benefits of having a computer
4. Evaluate the appropriateness of different record keeping options
5. Compare and contrast cash vs. accrual accounting
6. List some Do’s and Don’ts for farm record keeping

Assessment

Participants will view the presentation on financial basics and participate throughout with question and answer. The presenter will engage the audience to keep their interest and attention focused on the materials. Participants will take notes on provided handouts and will be encouraged to read the provided materials and visit listed websites for more information.

Equipment, Supplies, and Materials

1. Power Point presentation Lesson 3.3
2. Notes pages Lesson 3.3
3. Additional reading materials and links
References


Classroom Procedures

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
<tbody>
<tr>
<td>Slides 2-3: Introduction - give an overview of the topics to be covered in the presentation and outline the learning objectives.</td>
<td>• Engage the audience by asking them about their operations: who owns a small farm? Who operates a hobby farm? Large farm? Retirement? • Assess prior knowledge by asking how many participants have a record keeping system for the business • Who uses a computer for record keeping? • Who uses a computer for financial analysis? • Does anyone use the financial statements provided by the County Extension Office?</td>
</tr>
<tr>
<td>Slides 4: Introduce Financial Information for Farmers and Ranchers</td>
<td>• This slide sets the stage for slides 5-14 • Present information on farmer demographics, the major users of debt and sources of credit. • You'll expand on the credit topic by present the 5 C's of credit, discuss lending relationships and preparation for approval</td>
</tr>
<tr>
<td>Slide 5: Who Farms</td>
<td>• These are general categories of farm demographics • This may be a bit outdated, but the general breakdown probably holds true • Notice “Lifestyle” farms are the largest category. These would be your hobby farms and farms that are not the primary source of income for the family • Small family farms are 25 percent of the total farms</td>
</tr>
<tr>
<td>Slide 6: Who Uses Debt</td>
<td>• This table lists some general information about which farmer groups use debt • Large farms are the greatest users of debt. These farms are going to have more capital and labor costs in general • Young and beginning farmers also are large users of debt. Possibly due to start up capital requirements.</td>
</tr>
<tr>
<td>Slide 7: Sources of Credit</td>
<td>• This chart breaks shows sources of credit for farms. • Commercial banks and Farm Credit Systems are the largest sources • With the ever changing credit system in the U.S. this breakdown may be different from year to year.</td>
</tr>
</tbody>
</table>
### Classroom Procedures Continued

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
</table>
| **Capital**         | 1. What are some the primary sources of capital for your business? Financial and real assets.  
2. The creditor is looking for the owner to have sufficient equity in the company.  
3. If you have a significant stake in the company, you'll see it through. |
| **Capacity (Cash Flow)** | 1. Will you be able to meet your debt obligations and cover your family needs?  
2. The business needs to generate enough cash flow to repay the loan. |
| **Character**       | 1. Credit history is very important in today’s economy.  
2. Take steps to rebuild it and seek advice from your financial advisor or CPA.  
3. Banks want to know that if things go wrong, that you will be there and do your best to ensure that the company honors its commitments to the bank. |
| **Collateral**      | 1. Do you have the adequate equity to leverage your assets against the line of credit you are seeking?  
2. The reason the bank is interested in collateral is as a secondary source of repayment of the loan. |
| **Conditions**      | 1. Will the lender require you to meet certain performance standards? Gross income goals?  
2. The bank wants to be sure of the future viability of the business.  
3. Bankers need your help to identify and understand these key risks.  
4. Be prepared to articulate what you see as the primary threats to your business, and how and why you are comfortable with the presence of these risks, and what you are doing to protect the company. |

---

Slides 8-13: the 5 C’s of Credit
### Classroom Procedures Continued

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
</table>
| Slide 14: Prepare for Approval | - Careful consideration and preparation according to the 5 C’s will help you prepare for a successful loan application  
- Know your credit score  
- Other items to move the process forward for towards approval  
  1. Financial analysis with projections  
  2. Appraisals and evaluations  
  3. Business plan review  
  4. How will you mitigate risk?  
    a. Protecting assets  
    b. Protecting income |
| Slides 15-18: The Importance of Good Financial Record Keeping | - This begins a new section of the presentation: Financial Record Keeping  
- Starting a business is hard work and many businesses fail  
- Slide 16: these are the bare minimum requirements for your business  
- Slide 17: to maintain a solid financial record keeping system, there are additional requirements  
  1. Balance Sheet - presents a picture of the firm at one point in time. The balance sheet shows three things: assets, liabilities and net worth.  
  2. Income Statement - The income statement shows how the firm performed in the period between the two balance sheets (i.e., during the quarter or during the year). The income statement shows three things. These are outputs, costs and incomes.  
  3. Cash Flow Statement - The cash flow plans the future inflows and outflows of cash in the firm over a specific time period. It also shows cash in the business at the start of the period and cash left in the business at the end of the period.  
  4. Enterprise Budgets - Budgeting is trying to plan future expenditures and match these in some way with future sales and other dollar inflows. It is one of the most important functions in running a firm. No one knows the future, so budgeting results will usually be wrong. But it is essential to try.  
- Slide 18: Briefly review the length of time requirements for record keeping |
Classroom Procedures Continued

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
<tbody>
<tr>
<td>Slides 19-23: Record Keeping Alternatives</td>
<td>• The law may not require it, but in order to protect your business and keep it on solid financial ground, keep good records</td>
</tr>
<tr>
<td></td>
<td>• Paper records are an option</td>
</tr>
<tr>
<td></td>
<td>• Who uses a computer for record keeping?</td>
</tr>
<tr>
<td></td>
<td>• Computerized records offer many advantages</td>
</tr>
<tr>
<td></td>
<td>• Summarizing and manipulating data</td>
</tr>
<tr>
<td></td>
<td>• Graphs and charts are useful when examining difficult to understand or large amounts of data</td>
</tr>
<tr>
<td></td>
<td>• Statements can be generated from records data entered</td>
</tr>
<tr>
<td>Slides 24-28: How to Get Started</td>
<td>• Did you know your County Extension Office has financial statements?</td>
</tr>
<tr>
<td></td>
<td>• You must commit time and money to a good financial record keeping system</td>
</tr>
<tr>
<td></td>
<td>• Assess your needs</td>
</tr>
<tr>
<td></td>
<td>• Cash accounting more common in small businesses, transactions recorded when cash comes in and out of hand</td>
</tr>
<tr>
<td></td>
<td>• Accrual accounting records items when they are earned and claim deductions when expenses are owed</td>
</tr>
<tr>
<td></td>
<td>• Easy example of accrual is not paying taxes on an annuity until you withdraw funds</td>
</tr>
<tr>
<td></td>
<td>• Several good software packages available</td>
</tr>
<tr>
<td>Slides 29-31: Do’s and Don’ts for Farm Records</td>
<td>• Record keeping needs to be done in a timely fashion and is a crucial part of a successful agribusiness.</td>
</tr>
<tr>
<td></td>
<td>• Actively keep records - don’t procrastinate</td>
</tr>
<tr>
<td></td>
<td>• Record keeping is a very important part of the business so treat it like a REAL job</td>
</tr>
<tr>
<td></td>
<td>• Be honest with yourself and your business. Don’t play with balance sheets to make the business look better. You need accurate financials to make solid business decisions.</td>
</tr>
<tr>
<td></td>
<td>• Put someone else in charge or hire someone if you have to</td>
</tr>
<tr>
<td></td>
<td>• Keep records updated</td>
</tr>
<tr>
<td></td>
<td>• Keep business and your personal records and account separate. This will allow for transparency and avoid errors in financial analysis</td>
</tr>
<tr>
<td></td>
<td>• Record keeping is important - it is vital to the success of your business so take the time to do it right.</td>
</tr>
</tbody>
</table>
Classroom Procedures Continued

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
<tbody>
<tr>
<td>Handout: Essential Tools for Running a Firm</td>
<td>• Encourage participants to read the handout and to visit the sites for additional information.</td>
</tr>
<tr>
<td></td>
<td>• There are many links listed to reading materials and templates for starting your record keeping system</td>
</tr>
</tbody>
</table>

Sources of Additional Information

1. Setting Up a Record Keeping System. Ohio State University.  
   http://ohioline.osu.edu/cd-fact/1152.html


   http://www.smallbusinessnotes.com/operating/finmgmt/financialstmts/gettingstarted.html


   http://www.agmrc.org/business_development/operating_a_business/finance/financial_statements.cfm


   http://www.smallbusinessnotes.com/operating/finmgmt/cashmanagement.html


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Overview

- Who farms, who uses debt and main sources of credit
- The 5 C's of Credit give prospective entrepreneurs information about seeking lines of credit to help operate the business
- There are several components to any good financial record keeping system
- Computers and numerous software packages out there
- County extension agents are a good source for beginning farm financial statements
- Remember the Do’s and Don’ts for farm record keeping

Objectives

1) List the Five C’s of Credit
2) Identify the requirements for a sound financial record keeping system
3) Recognize the benefits of having a computer
4) Evaluate the appropriateness of different record keeping options
5) Compare and contrast cash vs. accrual accounting
6) List some Do’s and Don’ts for farm record keeping
Financial Information for Farmers and Ranchers

- Who farms
- Who uses debt
- Sources of credit
- 5 C’s of credit
- Lending relationships
- Prepare for approval

Who Farms

Chart Source: John J. Hays, Farm Credit Council

Who Uses Debt

<table>
<thead>
<tr>
<th>Type</th>
<th>Number</th>
<th>In Debt</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Young</td>
<td>152,156</td>
<td>79,294</td>
<td>52.1%</td>
</tr>
<tr>
<td>Beginning</td>
<td>444,588</td>
<td>203,856</td>
<td>45.9%</td>
</tr>
<tr>
<td>Small</td>
<td>1,764,786</td>
<td>680,588</td>
<td>18.6%</td>
</tr>
<tr>
<td>Large</td>
<td>146,340</td>
<td>129,609</td>
<td>88.6%</td>
</tr>
<tr>
<td>Female</td>
<td>161,328</td>
<td>43,882</td>
<td>27.2%</td>
</tr>
<tr>
<td>Minority</td>
<td>47,483</td>
<td>15,519</td>
<td>52.2%</td>
</tr>
</tbody>
</table>
Sources of Credit

Chart Source: John J. Hays, Farm Credit Council

5 C’s of Credit

- Capital
- Capacity (or Cash Flow)
- Character
- Collateral
- Conditions

5 C’s of Credit

- Capital
  - The amount of your net worth
  - It is determined by total assets minus total liabilities
  - This represents your investment in the operation

Section 3-86
5 C's of Credit

- **Capacity (or Cash Flow)**
  - Your ability to repay your debts and meet other obligations such as family needs

- **Character**
  - Is measured by considering many factors such as credit history, responsible use of credit, management practices (risk, financial, marketing, etc.)

- **Collateral**
  - What assets are pledged to the lender to protect the lender in the event of default
5 C’s of Credit

- **Conditions**
  - Requirements a lender makes a part of the loan agreement
  - Some conditions are in the form of performance requirements a borrower has to meet or maintain

Prepare for Approval

- Consider the 5 C’s
- Basic information when applying for credit approval

- Full approval
  - Financial analysis with projections
  - Appraisals and evaluations
  - Business plan review
  - Risk management considerations
    - Protecting assets
    - Protecting income

New Business Statistics

- 40% of start-up businesses fail within the first year
- Within 5 years 80% will have failed
- Of those that survive the first 5 years, 80% will fail within 10 years

Section 3-88
Financial Records Needed

- Minimum requirements
  - Inventory of assets and liabilities
  - Transaction journal listing income & expenses
  - Copies of tax forms filed
  - Employment records

A “good” financial record keeping system:
- The minimum requirements, plus
- Balance sheet
- Accrual adjusted income statement
- Cash flow statement
- Enterprise budgets

These should be timely, accurate and complete!

Financial Record Maintenance

<table>
<thead>
<tr>
<th>Record Type</th>
<th>Retention Period</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cancelled checks</td>
<td>3 to 6 years</td>
</tr>
<tr>
<td>Investment records</td>
<td>6 years</td>
</tr>
<tr>
<td>Loan agreements</td>
<td>Until updated</td>
</tr>
<tr>
<td>Receipts for large purchases</td>
<td>Until item is sold</td>
</tr>
<tr>
<td>Service contracts and warranties</td>
<td>Until item is sold</td>
</tr>
<tr>
<td>Tax returns</td>
<td>6 years from filing date</td>
</tr>
</tbody>
</table>
Record-Keeping Alternatives

- Except in a few cases, the law does not require any specific kind of records
- You can choose any record keeping system suited to your business
  - Should at least show your income for your tax year.
  - Keep a complete and separate set of records for each business in which you are involved.

Record-Keeping Alternatives

- The most important use for a computer on the farm is for:
  - Financial record keeping
  - Analysis

Record-Keeping Alternatives

- Computerized Records
  - Increasingly affordable
  - Especially useful for manipulating data
    - Cash-flow statements
    - Profit and Loss statements
    - Graphs and charts
Advantages of Computer Records

- Immediate availability of key reports
- Improved planning and budgeting capability
- Improved asset purchase decisions
- Pinpointing and elimination of unprofitable enterprises

Record-Keeping Alternatives

- Hand kept records
  - Suitable for smaller, less complex operations
- “Farm Account Books”
  - Good for small and part-time farmers
  - Provides a record of all basic information
  - Available through:
    - Cooperative Extension Services
    - Ag Lenders (USDA-FSA)
    - Farm management firms

Financial Statements

- Ask your Cooperative Extension Service for:
  - Crop & Livestock planning budgets
  - Balance sheets
  - Cash flow statements
  - Equipment inventory list
How to get Started

- Identify your needs
- Commit financially to what you need
- Commit the time

Cash Versus Accrual Accounting

- Cash Accounting Systems
  - Income recorded when the money is in your possession
  - Expense recorded when the goods and services are actually paid for

- Accrual Accounting Systems
  - Attempts to match expenses with generated revenue
  - Identifies income and expenses with specific periods of time, without regard to the date of cash receipt or payment

Commercial Software Products

- Quicken
  - User friendly
  - Widely available
  - Inexpensive
  - www.agecon.okstate.edu/quicken/

- QuickBooks
  - Double-entry accounting
  - Handles payroll
Commercial Software Products

- **Farmworks**
  - Can integrate field level and whole-farm records

- **FINPACK**
  - Excellent tool for developing
    - Balance Sheets
    - Budgets
    - Cash-Flows
  - Provides key financial measures

Do’s and Don’ts for Farm Records

- **Don’t:**
  - Wait until 2010 to do 2009 bookkeeping
  - You will forget things
  - And, it’s a real pain
  - Act like record keeping isn’t a REAL job
  - Play with balance sheet values
  - Ignore balance sheet trends

Do’s and Don’ts for Farm Records (cont’d)

- **Do:**
  - Keep records
  - Put someone in charge
    - Preferably someone who likes to do it
    - Provide the right tools
    - Provide dedicated space and environment
    - Hire it done if you have to
Do's and Don'ts for Farm Records (cont’d)

- Do:
  - Keep records updated
  - Keep business and personal accounts separate
  - Consider record-keeping a vital part of your business

Handout

Essential Tools for Running a Firm
Florida State Extension

- Good summary of the essentials

References


Sources of Additional Information

Setting Up a Record Keeping System. Ohio State University.
http://ohioline.osu.edu/cd-fact/1152.html

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Borrowing in a Risky Environment. Texas A&M University Extension.

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Liabilities Schedule. Oklahoma Cooperative Extension Service.
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The Essential Financial Tools for Running a Firm

P.J. van Blokland

Abstract

The paper is intended to provide the owner of an agricultural firm with the essential financial tools for running the business. Each tool is outlined and illustrated with an example. The paper starts with the historical tools, which include the firm's objectives, balance sheet and income statement and follows with the tools necessary to analyse these statements. These analytical tools examine the liquidity, solvency, profitability, efficiency and repayment capacity of the firm. The results of this analysis are used to re-examine the firm's objectives. The paper then employs the historical performance and the objectives to map out the future of the firm. The maps include enterprise and firm budgets and the cash flow budget. The results are compared with the firm's objectives which may be altered again as the budgeting results appear.

Key Words

Objectives, financial statements, liquidity, solvency, profitability, efficiency, repayment capacity, enterprise, firm and cash flow budgeting.

Objective

The objective of this paper is to present a description and a succinct discussion of the financial tools needed by an owner of an agricultural firm to assist in making sensible financial decisions. The owner and the manager are assumed to be the same person. Each tool is outlined sufficiently to follow the major points in using the tool.

Introduction

Management in any job is basically using information to make decisions to help the firm meet its objectives. Objectives must be written down and quantified in terms of numbers and time. "Make a profit" is not an objective. "Make $100,000 net income by the end of December three years hence" is. The manager needs to know where the firm stands today and how it got there. Therefore a lot of good management consists of linking the past with the future by making sound decisions today. This paper will present some of the main financial tools that do this linking. These tools are outlined in Figure 1.

The tools provide the information necessary to make most of the production, marketing and
financing decisions in the firm. The figure starts with the information that the manager thinks he needs. This information is digested and used to write the firm's objectives. The figure then separates into two parts. The left hand side, or the recording section, shows what has happened to the firm over time. These events were recorded and analysed to write the objectives of the firm. The right hand side, or the management section, shows what might happen to the firm if it meets its current and future objectives. The left and right hand sides are linked by monitoring. In other words, by comparing what actually happened with what the manager thought would happen. He must make decisions on any differences between the two. There will, of course, always be a difference for no one is clairvoyant. The real job is to take appropriate action on this difference.

For instance, suppose that the manager thought, based on historical performance, that his second quarter cash sales margin over cash costs would be $400,000, and the margin actually was $300,000. He is $100,000 short and had probably committed that $100,000 to future uses. He may have lined up resources for that purpose and now has bills to pay. He has to find out why there was a cash margin difference of 25% and what he should do about it (doing nothing is still a decision). This is not easy but it is real management. These tools will help in this decision-making process and, if necessary, help modify future objectives.

**The Balance Sheet**

The balance sheet presents a picture of the firm at one point in time. This is important to digest. Because the balance sheet is a snapshot of the firm on a single day, the firm's owners, sensibly and legally, make this statement look as good as they can to impress their readers. People dress well when they are interviewed or inspected. Firm owners do the same thing when they produce their balance sheet.

The balance sheet shows three things: assets, liabilities and equity or net worth. Assets are what the firm has. These possessions are usually divided into three categories in agriculture: current, intermediate and long term. Current assets are assets that can be or soon will be turned into cash. They include items like inventory for sale, supply inventory, cash, cash equivalents (e.g., savings accounts, stocks, bonds, mutual funds) and receivables. Intermediate assets usually consist of vehicles, equipment, machinery, breeding stock, plants and trees between one and seven years old, and nonpermanent buildings and structures. Long term assets typically are plants and trees over seven years old, permanent buildings and land.

Liabilities are what the firm owes. These also have three categories. Short term liabilities are what the firm owes in the period between the most recent and the next balance sheet. This period is every three months for firms with quarterly statements and every twelve months for firms with annual statements. Current liabilities list bills which must be paid in the next three months for quarterly reports or bills that must be paid over the next year for firms with annual reports. Current liabilities include the principal and interest on operating loans, payables and the current principal and interest portion of intermediate and long term debt. (i.e., what the firm owes in the next period on its notes and mortgages). Intermediate liabilities are what the firm owes on notes after deducting the current portion of the debt. Likewise long term liabilities are the remaining mortgages owed after meeting the current portion. Equity is what the firm owns. It is calculated by subtracting all the liabilities from the firm's assets. Consequently it is a residual and is found by subtraction. For example, if assets are $2.5 million and liabilities are $1.5 million, the firm's equity is $1 million. Equity is a key number for managerial scrutiny. Owners want to see steady equity growth, period after period. Equity is used in various ratios to see how the firm handles debt. For
example, leverage ratio is defined as total debt divided by equity. In the above instance, the ratio is $1.5 million divided by $1 million, or 1.5. This means the firm owns $1 for every $1.5 of debt. If the ratio increases, there is more debt owed per dollar owned and its risk has increased. If the ratio falls, the firm has reduced its risk.

The balance sheet can be used to compare how the categories or any or all of the assets and liabilities have changed from one period to the next, and the effect of these changes on the firm's equity. The balance sheet is illustrated in Table 1.

**The Income Statement**

The income statement shows how the firm performed in the period between the two balance sheets (i.e., during the quarter or during the year). The income statement shows three things. These are outputs, costs and incomes, each with its own section. The income statement is perhaps the most important statement to analyse in a firm. It shows how the manager used resources and what he got from their use. This analysis can often separate good managers from "other" managers, by showing the returns they received from their resource investments.

The first section of the income statement shows gross output. Gross output is what the firm produced. It includes sales, the change in the supply and for-sale inventory from one balance sheet to the next, other firm income and change in receivables. Gross output should increase over time and the proportion of sales making up gross output should be consistently high. This is because gross output can increase in one period with inventory sales, but this inventory must be replaced later on.

The second section of the income statement shows costs. Costs are divided into three main groups. The most important group is cash costs, which often make up 75% of any agricultural firm's total costs. Cash costs are defined as items paid with cash. These include supplies, labour, interest, fuel, repairs, insurance, rents and marketing expenses. Cash costs are usually divided into four or five major categories for analysis. For example, some firms may find the following categories useful: 1) chemicals and fertilizers; 2) labour, social security and associated taxes and expenses; 3) marketing expenses; 4) interest (Table 2). The categories will probably vary with the firm. There is no standard. The concept is to try to account for at least 80% of the firm's cash costs in these categories in order to track each category over time.

Gross output minus cash costs equals gross margin. Gross margin shows whether the firm can cover its cash costs and, if it can, how much is left to cover the rest of its commitments. Gross margin can be used for tracking individual enterprises and the whole firm. It is useful to follow the trends in gross margin of the different enterprises and use this information to make changes in enterprise operation.

The second cost group is depreciation. This cost is essentially the annual rate allowed by the IRS to write off depreciable capital assets. Depreciation is a real cost though it is not paid by the firm until it replaces its capital assets. The capital assets that can be depreciated include machinery, vehicles and buildings as well as breeding stock and orchards after they start producing. Consequently, until these assets are replaced, the depreciation allowances by the IRS add cash to the firm. This "additional" cash is most easily seen in the cash flow.

The third cost group is overhead. This group is usually disregarded by firms or used as a catch all for miscellaneous items. All overhead items can be put in either cash or depreciation costs. But because overhead is relatively unproductive compared with the other two cost groups, overhead should be recorded separately. Overhead items include all office expenses, business education and publications, lawyer and accountant fees, business travel and client entertainment. There is a tendency for firms to expand their overhead in good years when that money might be better spent on cash cost items. Therefore it is advisable to track the percentage shares of the three cost groups over time to see where the firm's expenditures go. For example, a "typical" full time Florida farm firm today might have 75% of its costs as cash, 18% as depreciation and the remaining 7% as overhead. Any marked deviation from the firm's historical trends needs investigation and explanation.
Cash plus depreciation plus overhead costs equals total costs. Gross output minus total costs equals net firm income. A positive net firm income shows the firm has covered all its costs. But net firm income is not profit. The firm still has other commitments. Net firm income is essentially equivalent to taxable income for a noncorporation because property taxes, road taxes and other firm taxes are included in cash costs. A high net firm income means higher income taxes, which might encourage the manager to purchase some needed depreciable capital asset. Depreciation reduces the net firm income and consequently the tax bill.

Net firm income minus the owners' income and social security taxes provides net income. This is the bottom line of any firm. To see how a firm is doing, follow its net income over time. A firm's net income can only be used for three things. These are the owners' salaries, re-investing in the firm and principal payments. Owners' salaries means what the owners withdraw for their living expenses including vacations, purchases for private items, education, etc. Owners' salaries are the corporate equivalent of dividends. Any firm capital purchases must also come from net income. These purchases are the same as re-investing in the firm. Finally, principal payments are settled with the firm's net income. The corporate equivalent of principal plus investments is called retained earnings.

The statement of owner equity links the period between the beginning and ending balance sheets with the income statement to show how owner equity has changed over time. Table 3 shows the linkages for a quarterly set of statements. Owner equity is a key number to monitor. It shows how much of the firm belongs to the owners. Equity growth probably ranks second to net income as the most important firm indicator of success.

This statement has three useful pieces of information. It shows firstly how equity is increased by paying off principal and investing in the firm (adding retained earnings in accounting language). Secondly, it shows how equity is depleted by taking salary from the firm. And thirdly, it shows how inflation and deflation affect equity as asset values change. The following example illustrates these functions.

The statement starts with the equity recorded in the beginning balance sheet, say on December 31. Assume equity on this date is $500,000. The net income from the income statement for the next quarter, i.e., January 1 to March 31, is added to this equity. With a net income of $50,000, equity increases to $550,000. Subtract owners' salaries of $20,000, and the revised equity is now $550,000 - $20,000, or $530,000. So firm equity increased during the quarter by $30,000. This increase resulted from paying off principal and re-investing. (Note that the $50,000 net income went on $20,000 salary and $30,000 principal and investing.)

The second function of the statement shows that equity was depleted $20,000 by withdrawing $20,000 salary. Obviously, the more the owners withdraw the less the equity growth will be. This may seem trite but it is an important point. Owners have to have enough to live on and to enjoy themselves. Only they can decide whether the increased enjoyment is worth the reduction of equity growth. This statement shows the relative effects clearly. Some 40% of the quarter's net income went to salary, so the remaining 60% was available to increase equity.
The third function of the statement shows the changes in asset valuation due to external factors. These externals are usually combined under the rubric of inflation. It is possible for a firm's equity growth to be entirely due to inflation. If, for example, land prices double, the firm's real estate is worth twice as much as it was before and equity growth is correspondingly impressive. And as inflation decreases and equity growth correspondingly falls, the firm does not look so good. This artificial type of equity growth must be realised to avoid bad decisions. In order to calculate asset valuation changes correctly, the manager needs a balance sheet recording both book and market value valuations of assets.

Book value can be measured in three ways, depending on type of asset. One measure is what the owner has invested in the items. This measure will apply to most of the firm's inventory items. For example, valuing a 10-inch plant at $4.50 because this is the sum of the cash, depreciation and overhead costs and management that went in it. A second way to measure book value is to use the recent purchase price of the item. This measurement is often used for nondepreciable assets. For example, valuing recently bought land at the purchase price of $3,500 per acre. The third way to measure book value is to use the current depreciated value of the asset. For example, a three year old tractor that was originally purchased for $70,000 and is depreciated at $10,000 per year, now has a book value of $40,000.

The market value of an asset is what the firm could get for that asset if it were sold in the period between the two balance sheets. Market value is usually greater than book value. Current assets are valued at either what has been invested in them (book value), or what they could be sold for in the market place. Suppose the book value of these assets is $90,000 and the market value is $120,000. There is a difference between the two of $30,000. Suppose that the book value of the intermediate assets was $150,000 and their market value was $200,000, for a difference of $50,000. Likewise the book value of the long term assets is $400,000 and the market value is $600,000, with a difference of $200,000.

This last sentence needs elaboration. Land assets dominate the total assets of agriculture. Land cannot be depreciated, so the "book" value of the land is either the original purchase price or, if it was purchased generations ago, the latest assessment of the value of the land. The market value is what the land can fetch in today's market. It is usually land values that signal inflation in agricultural markets.

So the book value of all the firm's assets is $90,000 + $150,000 + $400,000 = $640,000. The market value of its assets is $120,000 + $200,000 + $600,000 = $920,000. The difference between the two is $280,000. Taxes will be due on the differences in the non-current assets if they are sold. With a tax bracket of 20%, the tax due is \([($600,000 + $200,000) - ($150,000 + $400,000) \times 0.20]) = $50,000.\)

Assume that all these asset values are shown in the beginning balance sheet. If liabilities are $140,000, then the cost or book equity is $640,000 - $140,000 = $500,000. The book equity is the equity earned by the firm up to that point in time. The market value equity is $920,000 - $140,000 = $780,000. This equity is what the owners would get if they sold all their assets and met all their pre-tax liabilities. Therefore the gain in equity from the value difference alone is $670,000 - $390,000 = $280,000. Subtract the tax of $50,000 that would be due from selling these assets, = $230,000. This $230,000 is what is called the valuation equity or the amount that equity has increased solely due to increases in the value of the firm's assets.

Assume also that the ending balance sheet records a valuation equity of $260,000. The gain in the quarter, from changes in asset valuation only, is $260,000 - $230,000 = $30,000. Table 4 summarizes the three functions of the statement of owner equity.

The firm's equity increased $30,000 during the quarter from the firm's production. But it also increased $60,000 from changes in the valuation of the firm's assets. The former shows the results of the manager's work and the latter also shows the value of this work as well as the external factors, driven largely by inflation. Owners can use either or both numbers as they like. The important thing is to know...
The Essential Financial Tools for Running a Firm

the difference between the two and what the causes of these differences were.

**Analytical Tools**

The historic performance of the firm has been presented in balance sheets, income statements and the statement of owner equity. These statements must now be analysed. There are five basic toolboxes used in analysis. Each box contains several different tools. These toolboxes are: 1) the liquidity toolbox, 2) the solvency toolbox, 3) the profitability toolbox, 4) the efficiency toolbox, and 5) the repayment capacity toolbox.

**Liquidity**

This toolbox provides the tools necessary to see how "liquid" the business is. In other words, how difficult is it to raise cash? The definition of liquidity is the ability to meet liabilities when they become due. The due liabilities are the current liabilities listed in the balance sheet. The cash to pay them comes from the current assets listed in the same balance sheet. There must be enough of these, as cash, to pay current liabilities. If there are, the firm is liquid. If there are not, the firm is illiquid. All firms must stay liquid. Cash is their most important asset. Managers must spend a lot of time making certain that their firms are safely liquid.

**Working Capital**

Working capital is one of the major tools in the liquidity toolbox. It is calculated by subtracting current liabilities from current assets. For example, if the firm's current assets are $80,000 and current liabilities are $50,000, there is $30,000 working capital. In other words, after paying all the due debts, there is $30,000 left. The firm is liquid and that is good news.

**Quick Working Capital**

Some current assets may not be quite as liquid as others. For instance, growing crops are not as easy to sell (i.e., not as liquid, as crops waiting to go to market). And nothing is as liquid as cash. This is the meaning of liquidity. Quick working capital is a tool that takes the "stickiness" of some of the current assets into account, to give a more realistic picture of what cash is actually available. Only current assets which can be sold quickly without a discount are included. Items which can be sold quickly include cash, savings, investments in stocks, and most mutual funds, receivables that can be realistically realised quickly and any inventory that is at, or close to, the point of sale. There will be times when the working capital of a firm looks substantial, but the quick working capital is negative. In other words, the firm is not as liquid as it originally looked.

**Current Ratio**

The current ratio is calculated by dividing current assets by current liabilities. Thus if the current ratio of a firm at a specific point in time is 1.25 to 1, this means there is $1.25 to cover every $1 of debt due. Most firms will find it safe to keep their current ratio between two and three, meaning that they have $2 to $3 available to cover current liabilities. If the ratio falls below two, the manager should make sure that he can get liquid when he needs to. And if the ratio rises above three, he then has cash available for investing.

**Current Debt Ratio**

The current debt ratio is found by dividing current liabilities by the total liabilities of the firm. It shows what proportion of all the firm's debt, both principal and interest, is due in the next period. For example, if current liabilities are $35,000 and total debt is $150,000, the current debt ratio = $35,000/$150,000 = 0.23. This means that 23 cents of every dollar owed is due in the following period. Obviously it is hard to generalise about any "correct" ratio because it depends completely on the firm's debt load. But for a typical firm with a normal debt load, it is probably useful to keep the ratio below 0.1. A current debt ratio of 0.1 means that the firm must pay some 10% of its total debt in the next period. Most firms will find this a difficult objective to achieve.

**Solvency**

Solvency is a long-run concept. It shows whether the firm can meet all its debts if it sells all its assets. If the assets are greater than the liabilities, the firm is
solvent. If they are not, the firm is insolvent or bankrupt.

**Equity**

This is the single best measurement of solvency. If the firm has equity, it is solvent. Perhaps the most useful indicator of a firm's progress is a good equity trend.

**Leverage Ratio**

The leverage ratio is calculated by dividing total debt by equity. For example, if the firm's total debts are $200,000 and equity is $100,000, the leverage ratio is 200,000/100,000 or two. In other words, the firm has $2 in debt for every $1 that it owns. Most firms should keep this ratio below one. However it obviously depends on the situation the firm is in and the objectives and ages of the owners. Usually younger owners will have higher leverage ratios than older owners because the young tend to borrow more. A high leverage ratio is nothing to be ashamed of. It is something to reduce.

**Profitability**

Profitability is a word that everyone recognises but few people define. Profitability is concerned with the returns obtained over time from some form of investing. For example, the annual return on assets or equity will reflect the profitability of those investments. Profit is perhaps an easier term. A common sense measure of profit might be net firm income or net income. The distinction between profitability and profit is important. Whether the profit is good or not depends on the amount of investment it took to get it.

**Return on Equity (ROE)**

This is an important trend to follow. It shows the return on owned money in the firm. It is calculated using the formula:

\[
\frac{(\text{Net income} - \text{owners' salaries}) \times 100}{\text{beginning equity}}
\]

Suppose the firm's net income for the quarter was $40,000. The owner withdrew $16,000 for salary and the equity at the start of the quarter was $300,000. The firm's ROE is therefore \((40,000 - 16,000) \times 100 / 300,000 = 8\%\).

The question to ask is whether this profitability indicator is the best return the owner could get for investing his money. Or are there higher achievable returns for investing in something with much the same risk and requiring the same skills? This is a question that only the owner can answer. If the owner loves what he currently does to earn 8\% when he knows there are better opportunities available, then his decision should be respected.

**Return on Assets (ROA)**

This tool is calculated using the formula:

\[
\frac{(\text{Net firm income} + \text{interest paid} - \text{owners' salary}) \times 100}{\text{beginning assets}}
\]

The interest paid on debts is added back because the firm has borrowed money to buy assets and is paying interest as a cost of borrowing. The interest represents the return from that part of an asset financed by borrowed money. Part of the asset is financed with debt and part with equity and the manager wants to know the total return on that asset. Hence the interest must be added back to calculate the total return. Hopefully it will be greater than the cost of borrowing. It is not sensible to borrow at 10\% if the investment is returning 6\%. This will happen if ROE is less than ROA. The firm is earning less than it is paying to borrow funds.

Suppose the firm had a net firm income of $50,000 during the quarter, paid interest of $10,000 and withdrew salary of $16,000. The assets at the beginning of the quarter were $600,000. The ROA is therefore:

\[
\frac{(50,000 + 10,000 - 16,000) \times 100}{(600,000)} = 7.33\%.
\]

**Efficiency**

This is perhaps the most familiar toolbox to agriculturalists. Most efficiency tools refer to the relationship between inputs and outputs. Examples include yields per acre, feed per pound of liveweight gain, cash costs per bushel, sales per week, boxes picked per hour of labour, etc. These types of tools
are often kept by each firm and will not be presented here, except to emphasise their importance.

**Operation Ratios**

This tool is particularly useful in examining how costs change over time. It uses percentage ratios that always add to 100%. The components are: 1) cash costs excluding interest, 2) depreciation, 3) interest, 4) owners' taxes and social security, 5) other costs not already counted, and 6) net income. All of these components come from the income statement. Adding the six components together gives the firm's gross output. For example, see Table 5.

The interpretation is that 17% of the firm's gross output results in net income, 58% goes on cash costs excluding interest, 10% on interest and so on. Put another way, for every dollar that the firm generated in that quarter, 17 cents was net income, 58 cents went on cash costs excluding interest, etc. The most useful thing about this tool is spotting trends. If, for example, interest costs took an increasing share of each gross output dollar, the manager has some decisions to make.

**Asset Turnover**

Firms have to know how quickly they turn their assets over to generate output. The basic definition for asset turnover is Gross Output / Average Total Assets. The greater the ratio, the better the assets are used. For example, if the firm produces $1,000,000 gross output in a year and its average asset valuation was $5 million, the turnover ratio is 20%. One fifth of its assets turn over annually. But because of the almost unique asset fixity in agriculture (i.e., the land domination of assets) another denominator might be more useful. For those firms who have more than 30% of their total asset values in land, remove land from the denominator and work with the remaining assets. Then compare the turnovers with and without land.

**Repayment Capacity**

There are three main repayment capacity measurements and they all focus on how the firm can pay its debts. Note that these three measures ignore both the principal and interest of operating debt. It is assumed that operating debt will be repaid as the output it financed is sold. So unless any operating debt is carried over from the previous period, it is excluded from the formulae.

**Coverage Ratio**

The coverage ratio is calculated using the following formula:

\[
\frac{\text{net income} + \text{depreciation} + \text{interest} - \text{owners' salaries and taxes}}{\text{annual principal and interest payments}}.
\]

The higher the ratio, the easier it is for the firm to meet its debt commitments. If the ratio is one, it can just meet them. It also means that the firm is living, to some extent, off depreciation to service the debt. In other words the firm cannot replace any of the capital depreciation with new purchases. Anything greater than one gives the firm room to do other things.

For example, with a net income of $40,000, depreciation of $11,000, interest of $10,000, owners' salaries and taxes of $26,000 and principal payments of $13,000, the coverage ratio of this firm is:

\[
\frac{40,000 + 11,000 + 10,000 - 26,000}{13,000 + 10,000} = 1.52.
\]

The coverage ratio of 1.52 means that the firm can meet all its current debt obligations and still have 52 cents available for other uses.

**Capital and Debt Margin**

This ratio is essentially the next step up from the coverage ratio. It shows whether the firm can both meet its debt and afford to replace the capital assets lost in producing its net income. The capital and debt margin =

\[
\frac{\text{net income} + \text{depreciation} - \text{owners' salaries and taxes} - \text{principal payments}}{\text{net income} + \text{depreciation} - \text{owners' salaries and taxes}}.
\]

For example, using the numbers from the previous example, the capital and debt ratio of this firm is:

\[
\frac{40,000 + 11,000 - 26,000 - 13,000}{40,000 + 11,000 - 26,000} = 12,000.
\]
which means that there is $12,000 available after paying its current debt obligations and covering depreciation.

**Debt to Income Ratio**

The debt to income ratio is calculated using the following formula:

\[
\text{average total liabilities} / \text{net firm income}.
\]

The average total liabilities is calculated from adding the liabilities of the beginning and ending balance sheets together and dividing by two. The ratio shows the number of times that the firm’s debt exceeds its net firm income. For example, if liabilities are $300,000 and the net firm income is $50,000, the ratio is six. This means that, at the current rate, it would take six years for the income to equal debt. If the ratio falls to five, then its income leverage is reduced and the firm has reduced its risk. If the ratio rises, then income leverage is increasing, increasing the firm's risk because it becomes increasingly difficult to service this debt from current income.

**Summary of What Did Happen**

Managers, by necessity, use past performance to see how the firm is doing. This synopsis, using balance sheets, income statements and statements of owner equity, provides the raw data for the five analytical tools of liquidity, solvency, profitability, efficiency and repayment capacity. The manager is expected to produce answers from this analysis that will show whether the firm is meeting its objectives and to help formulate new objectives. But, unfortunately, analysis is neither entirely scientific nor precise. Analyzing the financial health of a firm involves experience and intelligent guesswork in much the same way that a doctor assesses and makes conclusions on the physical health of a patient.

Perhaps the most important part of this assessment is to estimate what the firm or the patient will look like in the future. It is this estimate that produces the objectives of the firm by bringing past performance and future predictions together. Analysis of past performance and knowledge of the present situation formulates what the firm can do in the future. These future predictions use the tools on the right hand side of Figure 1, and will be presented now.

**Budgeting**

Budgeting is trying to plan future expenditures and match these in some way with future sales and other dollar inflows. It is one of the most important functions in running a firm. No one knows the future, so budgeting results will usually be wrong. But it is essential to try. A budget is a map for the future of the firm and no one should go on a journey into the unknown without a map. And as with a journey, budgeting estimates change as circumstances change. The procedure is to start with budgeting the firm's individual enterprises. These enterprises are then added together to make the firm budget. The firm budget is then used to produce the cash flow for the firm.

**Enterprise Budget**

A generalized enterprise budget is shown in Table 6. Realize that the blanks under each category are where the individual items making up that category are entered. For example, the items of fertilizer, chemicals, labour, etc., would go under cash costs. Realize also that the sums of the different categories are shown by a capital letter.

There are a lot of things to discuss in this table. Firstly, sales have proxied for gross output. If it is possible to budget the gross output of the enterprise, inventory changes and all, it should be done. But as sales are usually easier to estimate, and as they typically make up at least 90% of the enterprise gross output, they are a good proxy for gross output.

Secondly, the table shows that each enterprise has to play its part in meeting all the firm's outlays. Some items like the cash costs are directly applicable to an individual enterprise. For example, the fertilizer applied to a specific crop is charged entirely to that crop. Others, like depreciation, are not as directly applicable, in that resources like machinery are usually shared among all the enterprises. So some form of cost sharing needs to be done to allocate this type of cost to the enterprise. In other words, items like depreciation must be prorated. The alternative is to diligently record the number of hours etc. that an
individual machine (for example) spends on each enterprise. This practice is rarely realistic, though it would usually provide better information.

The practical alternative is to have a simple method of cost sharing and later modify it as experience is gained. One of the simplest methods is to share the item in the same proportion as sales are shared. For instance, suppose a firm gets 70% of its sales from one enterprise and 30% from a similar enterprise. The depreciation could then be prorated between the two enterprises 70% and 30%. And if later experience shows that the smaller enterprise uses slightly more of the firm's depreciable capital assets per unit of output than the larger enterprise, the prorated shares might change to 65% and 35%. The sales percentage model is just one method. Sharing according to cash costs is another possibility. So is sharing based on experience. The important point is that each enterprise must cover these prorated items in order to contribute to the firm's profit.

Thirdly, the table shows that each enterprise must contribute to owners' taxes, salary and principal payments. This contribution is obviously essential, but is unfortunately not often seen in a specific firm's enterprise budget. The prorating method should be simple, and modified as experience dictates. Again, the essential point is that each enterprise must be able to cover these items. If it cannot, then the budget should be reassessed. This means examining the costs and the prorated numbers including the projected salaries. If the reassessment does not produce a positive number to re-invest in the firm, the manager needs to consider how much longer he wants to produce this enterprise because it is currently not paying its way.

Assume that the enterprise does generate a positive "L," and that the firm owner is considering its production. A positive L is a necessary but not yet sufficient reason to produce it. Fourthly and finally, there are at least four questions to answer now before the enterprise is produced. These are: 1) are there enough resources available to produce it? In other words, is there sufficient land, labour, debt and equity capital and managerial ability available? 2) is there a market for this enterprise and what must the firm do to get the enterprise to that market? 3) what must be done to the enterprise before it is marketable? For example, how must it be prepared, graded, packaged, transported etc? 4) what are the production, financing and marketing risks involved (yield; cost and price volatility; capital availability as well as the effects of weather, pests, diseases, breakdowns, strikes, etc.)?

If the answers to these four questions look good, then: 1) repeat the process with other possible enterprises, 2) select the ones that look the most profitable, and 3) combine these enterprises into a firm budget.

**Combining Selected Enterprises to Make a Firm Budget**

The procedure is to firstly, list the enterprises in a table; secondly, complete the row names in the table; thirdly, calculate the net enterprise incomes from each enterprise and, finally, add across the table to produce the firm budget. The net enterprise summation provides the net firm income and the salary, principal and re-investing totals show how the firm's net income is budgeted. A reasonable layout for this exercise is shown in Table 7, which also includes the projected numbers for the five enterprises and a total.

The table shows the contribution of each enterprise to the firm and how each contribution is shared among the outlays. Thus the owner expects the firm to have around $800,000 in sales, to pay some $470,000 in cash costs, use up about $115,000 of capital assets as depreciation and to prorate the $45,000 overhead between the enterprises as shown in the table. Consequently the owner will have to pay around $34,000 in income and social security taxes, leaving a net income of $136,000, which is allocated as shown between salaries, principal and re-investing in the firm.

**The Firm Cash Flow**

The cash flow is a planning tool stemming from the firm budget. It is also the final planning tool, before resources are allocated to produce the firm's enterprises. The cash flow plans the future inflows and outflows of cash in the firm over a specific time period. It also shows cash in the business at the start
of the period and cash left in the business at the end of the period. Examples of cash coming into the business include sales, new borrowing, other firm income and new equity. Examples of cash leaving the business include cash costs, principal payments, owners' salaries, asset purchases and owners' income taxes and social security.

The cash flow does three things. It predicts, monitors and presents decision-making data. It predicts the future cash inflows and outflows within specific time periods, usually monthly. It monitors these monthly predictions by comparing the monthly estimates with what actually happened during the month. Finally it helps the manager to make decisions on the difference between the predicted results and the actual results. For example, suppose August sales were predicted to be $60,000, but were actually $40,000, or 33% less than the estimate. What decision should the manager make? The answer, of course, depends on why the sales were down. If it was because the market price fell, or yields or quality was down, then some future adjustments will be necessary. But if the output was not quite ready for sale, then perhaps only September's numbers should be adjusted.

If cash is unavailable when it is expected, there is more than sales to consider. Cash outflows were originally matched to the inflows. If inflows fall, then cash commitments such as debt service, payables and salaries cannot be met. Consequently other cash sources must be tapped to meet these commitments. A properly used cash flow shows what is happening and suggests what the consequences will be when predictions have to be changed. The cash flow is constantly changing and provides the manager the cash map necessary for cash management.

Cash flow forms vary and no one basic form fits every firm. It is more important to have a good cash flow system than worry about form uniformity. A good system should run for three years and as it becomes increasingly difficult to predict that far in advance, each year will present less detail than the year before. For example, the first year of the system typically uses monthly columns, the second uses quarters and the third an annual column only. Rows can also be simplified. The monthly columns would show, for example, the different types of chemicals to be used in individual rows, while the third year annual column might show all the chemicals combined in a single row.

There is nothing wrong with designing an individual system that fits a specific firm. It seems reasonable for firms that essentially operate six months a year to have more columns, weekly or monthly, in their busy times and perhaps have the remainder of the year reflected by quarters. The important point is that a cash flow must be used constantly to be useful. Including unnecessary detail is almost as bad as excluding vital data. Always keep 12 months ahead in each of the three cash flows in the system. When one month passes, introduce the same month in the following year. And as a quarter expires, predict the following quarter in the second cash flow.

A simplified cash flow layout is shown in Table 8. This can be modified to fit the system in any firm.

Any one of these row names can be divided into its components, to provide detail or summarised to present a succinct picture. It may also be useful to use a separate loan section in the above table to itemise each loan and keep a running total of the current debt situation. The cash flow times debt repayments. It shows when there is cash and when there is no cash. Use it to present sensible debt scheduling to lenders. It is the firm cash flow rather than the lender which shows what can be done in paying interest and principal. Make sure that all parties involved understand this.

The cash flow also incorporates new events. As events change so will the firm results. Thus the cash flow must be changed constantly to reflect these changes and to reflect increasing knowledge of what will happen to cash inflows and cash outflows. The alterations show the results of the changes.

The cash flow shows when the firm can afford to buy assets. If the cash is not there and the asset is needed, it shows the consequences of increasing the debt load. It also shows how much salary can be drawn by the owners and the consequences of paying salary rather than spending the cash on other things.
Monitoring compares predictions with what actually happened. Predictions will be wrong, and the further away the predictions, the less accurate they may be. But the firm has to buy and use resources such as fertiliser and labour before it produces sales and make a hoped for profit. These are normal business risks. The cash flow helps to think through this process. A good cash flow shows more than just predictions. It also shows the actuals, side by side with the predictions. Table 9 shows the next step.

This cash flow has three sets of columns, shown in the Table 9 as "item," "July" and "January to July." It also simply illustrates some rows rather than presenting them all. The Table 9 layout is used for the nearby cash flow only. One set of columns (Item) lists the row names as before. The second (July) lists the predicted monthly cash results, the actual monthly cash results and the difference between them. The final set (January to July) lists these same three columns for the year to date. The idea behind this final set of columns is to prevent over-reaction to temporary events when the firm is basically still on track. Thus decisions should be made from the last column in Table 9 rather than the monthly difference column.

For example, there were no sales in July when the prediction was $40,000. This could be alarming, but the last column shows that the firm is only 8% down in sales for the year to date. So if the product was not quite ready for sale in July, then there is not much to worry about. Sales predictions have been pretty good. (Another story if there were other reasons for no sales in July, such as poor quality or price falls). Costs are also well predicted. The reason for no principal payments in July was because there were no July sales. The only problem with these numbers is that salary is higher than was predicted and this needs to be watched.

It is probably more useful to use percentages than numbers to express the differences between predicted and actuals. Percentages summarise the differences better. For example, a reduction in sales of $1 million looks startling, but if it is equivalent to a 3% drop, this does not seem too bad. So the essential purpose of the cash flow is to make decisions doing the cash flow and working with it. Producing,
Table 1. A simple balance sheet.

<table>
<thead>
<tr>
<th>Assets</th>
<th>Liabilities + Equities</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Current</strong></td>
<td><strong>Current</strong></td>
</tr>
<tr>
<td>cash + cash equivalents</td>
<td>payables</td>
</tr>
<tr>
<td>sale inventory</td>
<td>operating loans</td>
</tr>
<tr>
<td>supply inventory</td>
<td>current portion of notes</td>
</tr>
<tr>
<td>other inventory</td>
<td>current portion of mortgages</td>
</tr>
<tr>
<td>receivables</td>
<td>other loans</td>
</tr>
<tr>
<td><strong>Immediate</strong></td>
<td><strong>Intermediate</strong></td>
</tr>
<tr>
<td>vehicles</td>
<td>vehicle notes</td>
</tr>
<tr>
<td>equipment</td>
<td>equipment notes</td>
</tr>
<tr>
<td>temporary buildings</td>
<td>building notes</td>
</tr>
<tr>
<td><strong>Long term</strong></td>
<td><strong>Long term</strong></td>
</tr>
<tr>
<td>permanent buildings</td>
<td>building mortgages</td>
</tr>
<tr>
<td>land</td>
<td>land mortgages</td>
</tr>
<tr>
<td></td>
<td>Equity</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>TOTAL</strong></td>
</tr>
</tbody>
</table>

Table 2. An income statement.

<table>
<thead>
<tr>
<th>GROSS OUTPUT</th>
</tr>
</thead>
<tbody>
<tr>
<td>sales</td>
</tr>
<tr>
<td>other income to firm</td>
</tr>
<tr>
<td>change in supply inventory</td>
</tr>
<tr>
<td>change in sales inventory</td>
</tr>
<tr>
<td>change in receivables</td>
</tr>
</tbody>
</table>
Table 2. An income statement.

<table>
<thead>
<tr>
<th>TOTAL</th>
<th>CASH COSTS</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>category 1. e.g. chemicals and fertilisers</td>
</tr>
<tr>
<td></td>
<td>category 2. e.g. all hired labor expenses</td>
</tr>
<tr>
<td></td>
<td>category 3. e.g. transportation, fuel, repairs</td>
</tr>
<tr>
<td></td>
<td>category 4. e.g. all marketing expenses</td>
</tr>
<tr>
<td></td>
<td>category 5. e.g. all other cash costs</td>
</tr>
<tr>
<td>TOTAL</td>
<td>GROSS OUTPUT - CASH COSTS = GROSS MARGIN</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>DEPRECIATION</th>
</tr>
</thead>
<tbody>
<tr>
<td>vehicles</td>
</tr>
<tr>
<td>machinery and equipment</td>
</tr>
<tr>
<td>buildings</td>
</tr>
<tr>
<td>all other depreciable assets</td>
</tr>
<tr>
<td>TOTAL</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>OVERHEAD</th>
</tr>
</thead>
<tbody>
<tr>
<td>office expenses</td>
</tr>
<tr>
<td>salaries and fees</td>
</tr>
<tr>
<td>business travel</td>
</tr>
<tr>
<td>entertainment</td>
</tr>
<tr>
<td>all other overhead</td>
</tr>
<tr>
<td>TOTAL</td>
</tr>
</tbody>
</table>

| TOTAL COSTS |
### Table 2. An income statement.

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>cash</td>
<td></td>
</tr>
<tr>
<td>depreciation</td>
<td></td>
</tr>
<tr>
<td>overhead</td>
<td></td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td></td>
</tr>
<tr>
<td><strong>GROSS OUTPUT - TOTAL COSTS</strong></td>
<td>= NET FIRM INCOME</td>
</tr>
<tr>
<td><strong>OWNERS’ TAXES</strong></td>
<td></td>
</tr>
<tr>
<td>income taxes</td>
<td></td>
</tr>
<tr>
<td>social security taxes</td>
<td></td>
</tr>
<tr>
<td>other taxes</td>
<td></td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td></td>
</tr>
<tr>
<td><strong>NET FIRM INCOME - OWNERS’ TAXES</strong></td>
<td>= NET INCOME</td>
</tr>
<tr>
<td><strong>NET INCOME</strong></td>
<td></td>
</tr>
<tr>
<td>principal payments</td>
<td></td>
</tr>
<tr>
<td>re-investing</td>
<td></td>
</tr>
<tr>
<td>owners’ salaries</td>
<td></td>
</tr>
</tbody>
</table>

### Table 3. Statement of owner equity.

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>BEGINNING BALANCE</td>
<td></td>
</tr>
<tr>
<td>SHEET DECEMBER 31</td>
<td></td>
</tr>
<tr>
<td>ENDING BALANCE</td>
<td></td>
</tr>
<tr>
<td>SHEET MARCH 31</td>
<td></td>
</tr>
<tr>
<td>INCOME STATEMENT JANUARY 1 TO MARCH 31</td>
<td></td>
</tr>
<tr>
<td>STATEMENT OF OWNER EQUITY JANUARY 1 TO MARCH 31</td>
<td></td>
</tr>
</tbody>
</table>
Table 4. Summary of statement of owner equity.

<table>
<thead>
<tr>
<th>COMPONENT</th>
<th>BOOK</th>
<th>MARKET</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner equity in beginning balance sheet</td>
<td>500,000</td>
<td>780,000</td>
</tr>
<tr>
<td>1. Net income during the quarter</td>
<td>plus 50,000</td>
<td>50,000</td>
</tr>
<tr>
<td>2. Salary taken during quarter</td>
<td>minus (20,000)</td>
<td>(20,000)</td>
</tr>
<tr>
<td>3. Change in valuation equity</td>
<td></td>
<td></td>
</tr>
<tr>
<td>ending balance sheet</td>
<td>+$260,000</td>
<td></td>
</tr>
<tr>
<td>beginning balance sheet</td>
<td>-$230,000</td>
<td></td>
</tr>
<tr>
<td>total change</td>
<td>plus 30,000</td>
<td>30,000</td>
</tr>
<tr>
<td>Owner equity in ending balance sheet</td>
<td>530,000</td>
<td>840,000</td>
</tr>
<tr>
<td>Change in owner equity</td>
<td>plus 30,000</td>
<td>60,000</td>
</tr>
</tbody>
</table>

Table 5. A statement illustrating operation ratios.

<table>
<thead>
<tr>
<th>COMPONENT</th>
<th>$</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>cash costs, excl. interest</td>
<td>70,000</td>
<td>58</td>
</tr>
<tr>
<td>depreciation</td>
<td>10,000</td>
<td>9</td>
</tr>
<tr>
<td>interest</td>
<td>12,000</td>
<td>10</td>
</tr>
<tr>
<td>taxes and S.S.</td>
<td>4,000</td>
<td>3</td>
</tr>
<tr>
<td>overhead</td>
<td>4,000</td>
<td>3</td>
</tr>
<tr>
<td>net income¹</td>
<td>20,000</td>
<td>17</td>
</tr>
</tbody>
</table>
Table 5. A statement illustrating operation ratios.

<table>
<thead>
<tr>
<th>COMPONENTS</th>
<th>$</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>GROSS OUTPUT</td>
<td>120,000</td>
<td>100</td>
</tr>
</tbody>
</table>

\[1\] This is the residual from subtracting all the costs from the gross output.

Table 6. A general enterprise budget.

<table>
<thead>
<tr>
<th></th>
<th>$ per UNIT</th>
</tr>
</thead>
<tbody>
<tr>
<td>SALES</td>
<td></td>
</tr>
<tr>
<td>Anticipated (yield______) x anticipated (price______)</td>
<td>=A</td>
</tr>
<tr>
<td>COSTS AND INDICATORS</td>
<td></td>
</tr>
<tr>
<td>(1) Cash costs</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td>Total cash costs</td>
<td>=B</td>
</tr>
<tr>
<td>GROSS MARGIN (A) - (B)</td>
<td>=C</td>
</tr>
<tr>
<td>(2) Depreciation</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Depreciation</td>
<td>=D</td>
</tr>
<tr>
<td>(3) Overhead (prorated)</td>
<td>=E</td>
</tr>
<tr>
<td>TOTAL COSTS (B) + (D) + (E)</td>
<td>=F</td>
</tr>
<tr>
<td>NET ENTERPRISE INCOME (A)-(F)</td>
<td>=G</td>
</tr>
<tr>
<td>(4) Owners' estimated taxes and SS (prorated)</td>
<td>=H</td>
</tr>
</tbody>
</table>
Table 6. A general enterprise budget.

<table>
<thead>
<tr>
<th>NET INCOME (G) - (H)</th>
<th>=I</th>
</tr>
</thead>
<tbody>
<tr>
<td>MINUS (PRORATED)</td>
<td></td>
</tr>
<tr>
<td>1) salary to owners</td>
<td>=J</td>
</tr>
<tr>
<td>2) principal payments</td>
<td>=K</td>
</tr>
<tr>
<td>EQUALLS</td>
<td></td>
</tr>
<tr>
<td>amount left for buying assets</td>
<td>i.e., =L</td>
</tr>
</tbody>
</table>

\[(I) - (J+K)\]

Table 7. Enterprise and firm budgets: a methodology.

<table>
<thead>
<tr>
<th>CATEGORIES</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>SALES</td>
<td>250</td>
<td>200</td>
<td>150</td>
<td>100</td>
<td>100</td>
<td>800</td>
</tr>
<tr>
<td>Cash costs</td>
<td>150</td>
<td>120</td>
<td>80</td>
<td>60</td>
<td>60</td>
<td>470</td>
</tr>
<tr>
<td>Depreciation</td>
<td>36</td>
<td>29</td>
<td>22</td>
<td>14</td>
<td>14</td>
<td>115</td>
</tr>
<tr>
<td>Overhead</td>
<td>14</td>
<td>11</td>
<td>8</td>
<td>6</td>
<td>6</td>
<td>45</td>
</tr>
<tr>
<td>TOTAL COSTS</td>
<td>200</td>
<td>160</td>
<td>110</td>
<td>80</td>
<td>80</td>
<td>630</td>
</tr>
<tr>
<td>NET ENTER INCOME</td>
<td>50</td>
<td>40</td>
<td>40</td>
<td>20</td>
<td>20</td>
<td>170</td>
</tr>
<tr>
<td>owner income</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>tax + s.s.</td>
<td>10</td>
<td>8</td>
<td>8</td>
<td>4</td>
<td>4</td>
<td>34</td>
</tr>
<tr>
<td>NET INCOME</td>
<td>40</td>
<td>32</td>
<td>32</td>
<td>16</td>
<td>16</td>
<td>136</td>
</tr>
<tr>
<td>salary</td>
<td>15</td>
<td>13</td>
<td>10</td>
<td>6</td>
<td>6</td>
<td>50</td>
</tr>
<tr>
<td>principal</td>
<td>12</td>
<td>10</td>
<td>8</td>
<td>5</td>
<td>5</td>
<td>40</td>
</tr>
<tr>
<td>re-investing</td>
<td>14</td>
<td>12</td>
<td>8</td>
<td>6</td>
<td>6</td>
<td>46</td>
</tr>
</tbody>
</table>
Table 8. A basic cash flow layout.

<table>
<thead>
<tr>
<th></th>
<th>Time Period 1</th>
<th>Time Period 2</th>
</tr>
</thead>
<tbody>
<tr>
<td>opening cash balance</td>
<td></td>
<td></td>
</tr>
<tr>
<td>CASH IN</td>
<td></td>
<td></td>
</tr>
<tr>
<td>sales</td>
<td></td>
<td></td>
</tr>
<tr>
<td>other cash income</td>
<td></td>
<td></td>
</tr>
<tr>
<td>new borrowing</td>
<td></td>
<td></td>
</tr>
<tr>
<td>new equity additions</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total cash available</td>
<td>(A)</td>
<td></td>
</tr>
<tr>
<td>CASH OUT</td>
<td></td>
<td></td>
</tr>
<tr>
<td>cash costs</td>
<td></td>
<td></td>
</tr>
<tr>
<td>owners' salaries</td>
<td></td>
<td></td>
</tr>
<tr>
<td>asset purchases</td>
<td></td>
<td></td>
</tr>
<tr>
<td>principal payments</td>
<td></td>
<td></td>
</tr>
<tr>
<td>owners' taxes and SS</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total cash spent</td>
<td>(B)</td>
<td></td>
</tr>
<tr>
<td>(A) - (B) = closing cash balance</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Table 9. The proper cash flow ($'000).

<table>
<thead>
<tr>
<th>ITEM</th>
<th>July</th>
<th>January to July</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>predict</td>
<td>actual</td>
</tr>
<tr>
<td>sales</td>
<td>40,000</td>
<td>0</td>
</tr>
<tr>
<td>costs</td>
<td>30,000</td>
<td>32,000</td>
</tr>
</tbody>
</table>
Lesson 3.4: The Balance Sheet

Estimated time: One hour.

Overview

Lesson 3.4 is an introduction to the balance sheet: definitions, components, and purpose. You will learn to manage your own business balance sheet and use it on a regular basis. At the end of this lesson, you will prepare a sample balance sheet and calculate values.

Objectives

1. Understand definitions associated with accounting.
2. Read and interpret the balance sheet.
3. Be able to create and use your own balance sheet.

Assessment

At the end of the period, the class will complete an example balance sheet of Dave and Dolly Dairy Farm together. This example will combine the principles and definitions studied so the student can realize the application of the balance sheet and its interconnected components. A key to the balance sheet example will be sent with the students to reference and for additional study.

Equipment, Supplies, and Materials

1. Power Point presentation Lesson 3.4
2. Notes pages Lesson 3.4
3. Handout “Dave and Dolly Dairy Farm BLANK” (in-class example)
4. Handout “Dave and Dolly Dairy Farm KEY”

References

# Classroom Procedures

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
<tbody>
<tr>
<td>Slides 2-3: Overview and objectives</td>
<td>• Lead discussion to assess previous knowledge.</td>
</tr>
<tr>
<td></td>
<td>• Do you use a balance sheet regularly?</td>
</tr>
<tr>
<td></td>
<td>• What information is included in it?</td>
</tr>
<tr>
<td></td>
<td>• What is its purpose or bottom line?</td>
</tr>
<tr>
<td>Slide 4: Definition of the balance sheet</td>
<td>• When do you think most people prepare a balance sheet? Why?</td>
</tr>
<tr>
<td></td>
<td>• Ask for examples of something “owned” and “owed.”</td>
</tr>
<tr>
<td>Slides 5-7: Assets &amp; liabilities</td>
<td>• Ask for and answer questions after slide 8 to make sure students understand the concept before continuing.</td>
</tr>
<tr>
<td>Slide 10: Equation of the balance sheet</td>
<td>• Emphasize the importance of understanding this equation. It is the purpose of creating the balance sheet and the “bottom line.”</td>
</tr>
<tr>
<td>Slides 11-18: Liquidity and solvency</td>
<td>• Although students do not have to memorize equations, the concepts are important because they apply to both the balance sheet and the income statement.</td>
</tr>
<tr>
<td></td>
<td>• Information from the balance sheet is necessary to complete the income statement, including these ratios.</td>
</tr>
<tr>
<td>Slide 19: Dave and Dolly Dairy Farm example</td>
<td>• Click the link to bring up the document.</td>
</tr>
<tr>
<td></td>
<td>• Pass out BLANK version of handout.</td>
</tr>
<tr>
<td></td>
<td>• Have the students work on it independently for five minute, and then ask for specific questions.</td>
</tr>
<tr>
<td></td>
<td>• Go over each section individually.</td>
</tr>
<tr>
<td>End of class: Finish example and ask for final questions.</td>
<td>• Make sure to give students the Dave and Dolly Dairy Farm KEY handout before they leave so that they can refer to it to study the balance sheet example further.</td>
</tr>
</tbody>
</table>
Sources of Additional Information

   http://www.smallbusinessnotes.com/operating/finmgmt/financialstmts/gettingstarted.html
   http://www.agmrc.org/business_development/operating_a_business/finance/financial_statements.cfm

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Lesson 3.4 is an introduction to the balance sheet: definitions, components, and purpose. You will learn to manage your own business balance sheet and use it on a regular basis. At the end of this lesson, you will prepare a sample balance sheet and calculate values.

Objectives

1. Understand definitions associated with accounting
2. Read and interpret the balance sheet
3. Be able to create and use your own balance sheet
Financial Statements are Essential

Managers, investors, and other internal groups want the answers to two important questions:

- How well did the operation perform?
- Where does the operation stand?

Definition of the Balance Sheet

- A snapshot of the financial status of a business at a point in time.
- A summary of what is owned versus what is owed.
- An estimation of net worth (owner equity) by valuing and categorizing assets and liabilities.
- The figures on a balance sheet can change daily, but it is usually calculated and filed yearly or quarterly.

Assets

- Asset: an economic resource of an operation that can be sold to generate cash or used to produce other goods, e.g. stocks, crops, machinery, land, livestock.
  - Current: more liquid assets which are used or sold within one year
  - Non-current: more illiquid assets; usually those used to produce other goods; anything that is not a current asset

Section 3-120
**Liabilities**

- Liability: an obligation or debt owed to another, e.g., bills, mortgages, loans, accounts payable, interest or principal payments.
  - Current: debts that become due within one year
  - Non-current: any debt or payment that is not due within one year

**Intermediate Assets and Liabilities**

- For farm businesses, non-current assets and liabilities are usually further divided into “intermediate” and “long-term.”
  - Intermediate: have a usable/payable life of 1–10 years, e.g., breeding livestock, trucks, short term loans.
  - Long term: have a usable life of more than 10 years, e.g., buildings, land, mortgages.

**Owner Equity**

- Owner Equity: the amount of money left for the owner if all assets were sold and all liabilities paid; synonymous with “net worth.”
Changes in Owner Equity

- A change does occur
  - If a profit or loss occurs
  - If capital is invested or withdrawn
  - If values of assets change
- A change does not occur
  - If cash is used to purchase inputs
  - If loan are taken out to purchase inputs

Equation of the Balance Sheet

Assets = Liabilities + Owner Equity
or
Owner Equity = Assets – Liabilities

Liquidity

- Liquidity: a short-run concept; ability to pay debts as they become due without disrupting day to day operations; ability to generate cash as necessary.
  - Current ratio
  - Working capital
  - Debt structure
**Current Ratio**

\[
\text{Current Ratio} = \frac{\text{current asset value}}{\text{current liability value}}
\]

- Current ratio = 1: sufficient assets to cover debt, but no safety margin
- Current ratio < 1: business is illiquid
- Current ratio > 1: business is liquid
- Current ratio > 2: business is excessively liquid

**Working Capital**

\[
\text{Working Capital} = \text{current assets} - \text{current liabilities}
\]

- Not a ratio; the absolute value of how much money is left (safety margin) if all current assets are sold and all current liabilities are paid.
- Amount could be used to purchase new inputs.
- It is important to relate the value of working capital to the size of the business.

**Debt Structure**

\[
\text{Debt Structure} = \left( \frac{\text{current liabilities}}{\text{total liabilities}} \right) \times 100
\]

- The percentage of liabilities that are current – due within one year.
Solvency

- Solvency: a long-run concept; ability to pay all debts if assets were sold. If liabilities > assets, the business is insolvent; if assets > liabilities, the business is solvent.
  - Debt: asset ratio
  - Equity: asset ratio
  - Leverage ratio

Equity: Asset Ratio

Equity : Asset Ratio = \( \frac{\text{owner equity}}{\text{total assets}} = 1 - D : A \) ratio

- The portion of the business owned by the owner.
  - \( 1 \geq E/A \geq 0 \)
  - \( E/A < 0 \): business is insolvent
  - \( E/A = 1 \): assets = owner equity = no debt
- The largest value is preferred.

Debt: Equity or Leverage Ratio

Debt : Equity Ratio = \( \frac{\text{total liabilities}}{\text{owner equity}} \)

- Proportion of lenders to owner financing of the business.
  - \( D/E > 1 \): business is insolvent
  - \( D/E = 1 \): equal investment of capital
  - \( D/E < 1 \): owner owns more than is owed
  - \( D/E = 0 \): assets = owner equity = no debt
- The smallest value is preferred.
**Debt:Asset Ratio**

Debt : Asset Ratio = \( \frac{\text{total liabilities}}{\text{total assets}} = \frac{D}{E} \times \frac{E}{A} \)

- The portion of the business owned by lenders.
  - D/A > 1: business is insolvent
  - D/A = 1: owner equity is zero
  - D/A < 1: business is solvent
- The smallest value is preferred.

**Balance Sheet Example**

- Dave and Dolly Dairy Farm

**References**


Sources of Additional Information


http://www.smallbusinessnotes.com/operating/finmgmt/financialstmts/gettingstart.html

Basic Rules for Financials. Business Owner’s Toolkit.

http://www.agmrc.org/business_development/operating_a_business/finance/financial_statements.html

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**Lesson 3.5 Balance Sheet Example: Dave and Dolly Dairy Farm**

Table 1. Farm financial information for balance sheet of Dave and Dolly Dairy Farm, cost-basis.

<table>
<thead>
<tr>
<th>Items as of January 1, 2009:</th>
<th>Comment</th>
</tr>
</thead>
<tbody>
<tr>
<td>a. Checking account balance is $13,245</td>
<td></td>
</tr>
<tr>
<td>b. Saving account balance is $2,350</td>
<td></td>
</tr>
<tr>
<td>c. Inherited 340 acres of land in 1974 worth $800 per acre at the time</td>
<td></td>
</tr>
<tr>
<td>d. Accrued interest on equipment loans is $2,278</td>
<td>intermediate loan</td>
</tr>
<tr>
<td>e. Have 20 steer calves @ $420 per head</td>
<td>lvstck/comm sale</td>
</tr>
<tr>
<td>f. Owe bank $120,000 for a 160 acre tract with $10,000 principal due in 12/09</td>
<td></td>
</tr>
<tr>
<td>g. Own 160 acre tract of land originally cost $160,000 when purchased in 1996</td>
<td></td>
</tr>
<tr>
<td>h. Bought 340 acres of farmland at $400 per acre in 1992</td>
<td></td>
</tr>
<tr>
<td>i. Built milk barn and parlor at a cost of $44,000 on 340 acres bought in 1992</td>
<td>improvements</td>
</tr>
<tr>
<td>j. Owe $1,800 on crop loan for fertilizer, seed, chemicals</td>
<td>operating loan</td>
</tr>
<tr>
<td>k. Property taxes for all real estate due 4/09 are $4,200</td>
<td></td>
</tr>
<tr>
<td>l. Accrued interest on land loans is $10,177</td>
<td>long term liability</td>
</tr>
<tr>
<td>m. Owe bank $28,000 on JD no-till planter with $7,000 principal due 12/09</td>
<td></td>
</tr>
<tr>
<td>n. Have 3,000 bushels of corn in storage worth $2.50 per bushel</td>
<td></td>
</tr>
<tr>
<td>o. T. Donahue owes $2,800 for custom baling</td>
<td>acc’t. receivable</td>
</tr>
<tr>
<td>p. Book value of tractors and all equipment as of 1/1/09 was $240,000</td>
<td>mach. beg. value</td>
</tr>
<tr>
<td>q. Purchased a new JD 150 HP tractor last spring for $35,000 with $14,000 loan. Principal payment of $6,000 due 11/09</td>
<td>inter. asset, value added</td>
</tr>
<tr>
<td>r. Principal payments of $15,400 on all intermediate loans due during 2009</td>
<td>other CL-A</td>
</tr>
<tr>
<td>s. 860 gal of diesel fuel at $1.75 on hand</td>
<td>supplies on hand</td>
</tr>
<tr>
<td>t. Principal payments of $25,000 due on all real estate loans during 2009</td>
<td>other CL-B</td>
</tr>
<tr>
<td>u. Tractors and equipment depreciation during 2008 was $52,000</td>
<td>Inter. asset depr.</td>
</tr>
<tr>
<td>v. $15,000 principal payment due 10/09 on 340 acre land mortgage (with milk barn) with $98,000 principal</td>
<td></td>
</tr>
<tr>
<td>w. Farm trucks are worth $18,000</td>
<td></td>
</tr>
<tr>
<td>x. Owe H. Smith $4,800 on 4 heifers with $2,400 due this year</td>
<td></td>
</tr>
<tr>
<td>y. Lease 40 acres @ $80 per acre</td>
<td>current liability</td>
</tr>
<tr>
<td>z. Have 30 large round bales of hay @ $25 per bale</td>
<td></td>
</tr>
<tr>
<td>aa. Have 3 tons of fertilizer on hand at $180 per ton</td>
<td></td>
</tr>
<tr>
<td>ab. Accrued interest on current liabilities is $520</td>
<td></td>
</tr>
<tr>
<td>ac. Have 120 dairy cows @ $2,100 per head</td>
<td></td>
</tr>
<tr>
<td>ad. Have 20 springing heifers @ $1,200 per head</td>
<td></td>
</tr>
</tbody>
</table>
### Statement of: Dave and Dolly Dairy Farm (example)

#### Balance Sheet

**1. Current Assets**

<table>
<thead>
<tr>
<th>Description</th>
<th>Unit Value</th>
<th>Date Due</th>
<th>Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Steer calves</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Large round bales of hay</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>investments in growing crops</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Supplies on hand</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fertilizer, 3 tons @ $180</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>860 gals. of diesel fuel @ 1.75</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**2. Intermediate Assets** (Assets not normally sold during the year)

<table>
<thead>
<tr>
<th>Description</th>
<th>Number</th>
<th>Unit Value</th>
<th>Date Due</th>
<th>Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dairy cows</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Springing heifers</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>personal vehicles</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>trucks</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>mach. beg ($) (+) val add ($)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(-) value disp. ($) (-) depr. $</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>securities - not readily marketable</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>retirement accounts</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>intermediate assets from attached schedules</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**3. Long Term Assets** (Real Estate & Improvements)

<table>
<thead>
<tr>
<th>Description</th>
<th>Purchase</th>
<th>Year Acquired</th>
</tr>
</thead>
<tbody>
<tr>
<td>home place @ $600/ac</td>
<td></td>
<td>1974</td>
</tr>
<tr>
<td>new milk barn and parlor</td>
<td></td>
<td>1992</td>
</tr>
<tr>
<td>1st nat bank 160 acres</td>
<td></td>
<td>Dec-09</td>
</tr>
<tr>
<td>1st nat ban 340 w barn</td>
<td></td>
<td>Oct-09</td>
</tr>
</tbody>
</table>

**4. Current Liabilities** (Due in less than 1 year)

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount Owed</th>
<th>Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>daily wages</td>
<td></td>
<td></td>
</tr>
<tr>
<td>supplies on hand</td>
<td></td>
<td></td>
</tr>
<tr>
<td>fuel</td>
<td></td>
<td></td>
</tr>
<tr>
<td>fertilizer</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**5. Total Current Liabilities**

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount Owed</th>
<th>Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>daily wages</td>
<td></td>
<td></td>
</tr>
<tr>
<td>supplies on hand</td>
<td></td>
<td></td>
</tr>
<tr>
<td>fuel</td>
<td></td>
<td></td>
</tr>
<tr>
<td>fertilizer</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**6. Intermediate Liabilities** (Due in 1 - 10 years)

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount Owed</th>
<th>Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>daily wages</td>
<td></td>
<td></td>
</tr>
<tr>
<td>supplies on hand</td>
<td></td>
<td></td>
</tr>
<tr>
<td>fuel</td>
<td></td>
<td></td>
</tr>
<tr>
<td>fertilizer</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**7. Long Term Liabilities** (Due in more than 10 years)

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount Owed</th>
<th>Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>daily wages</td>
<td></td>
<td></td>
</tr>
<tr>
<td>supplies on hand</td>
<td></td>
<td></td>
</tr>
<tr>
<td>fuel</td>
<td></td>
<td></td>
</tr>
<tr>
<td>fertilizer</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Lesson 3.5: The Income Statement

*Estimated time: One hour.*

**Overview**

Lesson 3.5 is an introduction to the income statement: definitions, components, and purpose. You will learn to manage your own business income statement and use it on a regular basis. At the end of this lesson, you will prepare a sample income statement and calculate values.

**Objectives**

1. Understand definitions associated with accounting.
2. Read and interpret the income statement.
3. Be able to create and use your own income statement.

**Assessment**

At the end of the period, the class will complete an example income statement of Robert and Roberta Roberts together. This example will combine the principles and definitions studied so the student can realize the application of the income statement and its interconnected components. A key to the income statement example will be sent with the students to reference and for additional study.

**Equipment, Supplies, and Materials**

1. Power Point presentation Lesson 3.5
2. Notes Pages Lesson 3.5
3. Handout “Robert and Roberta Roberts BLANK” (in class example)
4. Handout “Robert and Roberta Roberts KEY”

**References**

### Classroom Procedures

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
<tbody>
<tr>
<td>Slides 2-3: Overview and objectives</td>
<td>• Lead discussion to assess previous knowledge.</td>
</tr>
<tr>
<td></td>
<td>• Do you use an income statement regularly?</td>
</tr>
<tr>
<td></td>
<td>• What information is included in it?</td>
</tr>
<tr>
<td></td>
<td>• What is its purpose or bottom line?</td>
</tr>
<tr>
<td>Slide 4: definition of income statement – remember the balance sheet</td>
<td>• Balance sheet – assets and liabilities at a point in time</td>
</tr>
<tr>
<td>Slide 7: clarify cash vs. accrual</td>
<td>• Cash accounting is simpler than accrual and is most commonly used</td>
</tr>
<tr>
<td></td>
<td>• Accrual is a more accurate measure and is a bit more difficult, but it is preferred</td>
</tr>
<tr>
<td>Slide 11: why is cash used to purchase depreciable assets not an expense in the first year?</td>
<td>• During the first year, the asset does not depreciate. Its value is its purchase value. During year 2, depreciation of the asset is an expense and the book value of the asset is substituted for its purchase price.</td>
</tr>
<tr>
<td>Slide 12: difference between NFI and NFIO</td>
<td>• The only difference between NFI and NFIO is the value of the sale of capital assets (also see next slide)</td>
</tr>
<tr>
<td>Slide 14: NFI vs. NFIO</td>
<td>• Clarify that NFIO is a more accurate measure of income and NFI is not used for any calculations</td>
</tr>
<tr>
<td>Slide 18: Profitability ratios</td>
<td>• Allow comparisons between operations of differing sizes</td>
</tr>
<tr>
<td>Slide 19: reinforce balance sheet and income statement relationship</td>
<td>• Income statement can not be completed without balance sheet.</td>
</tr>
<tr>
<td></td>
<td>• Denominator from beginning and ending balance sheets</td>
</tr>
<tr>
<td></td>
<td>• Numerator from income statement</td>
</tr>
</tbody>
</table>
### Classroom Procedures Continued

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
</table>
| Slide 24: Robert and Roberta Roberts Example | • Click the link to bring up the document.  
• Pass out BLANK version of handout.  
• Have the students work on it independently for five minutes, and then ask for specific questions.  
• Go over each section individually. |
| End of class: finish example and ask for final questions | • Make sure to give students the Robert and Roberta Roberts KEY handout before they leave so that they can refer to it to study the balance sheet example further. |

### Sources of Additional Information


   [http://www.agmrc.org/business_development/operating_a_business/finance/financial_statements.cfm](http://www.agmrc.org/business_development/operating_a_business/finance/financial_statements.cfm)


### Contact Information

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Research Associate  
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Division of Agriculture  
479-575-5226  
nkemper@uark.edu
Lesson 3.4 is an introduction to the income statement: definitions, components, and purpose.

You will learn to manage your own business income statement and use it on a regular basis.

At the end of this lesson, you will prepare a sample income statement and calculate values.

Objectives

1. Understand definitions associated with accounting
2. Read and interpret the income statement
3. Be able to create and use your own income statement
Financial Statements are Essential

Managers, investors, and other internal groups want the answers to two important questions:

How well did the operation perform?

Where does the operation stand?

Definition of the Income Statement

- A summary of expenses and revenues over a period of time and their difference.
- A positive difference indicates a profit, while a negative difference indicates a loss.
- Calculates net farm income (NFI) and net farm income from operations (NFIO), measures of the magnitude of the profit or loss over the period.
- Also called profit-and-loss, operating, or earnings statement.
- Must have balance sheet data to construct.

Cash vs. Accrual

- Non-cash revenues and expenses are included in accrual but not cash accounting systems.
  - Depreciation is always included in either system
- Many farm businesses use cash accounting systems.
- Accrual systems are more accurate measurements.
  - Result in better management decisions
  - Preferred by Farm Financial Standards Council (FFSC)
Revenues

- Revenue: money produced by farm operations; should be recorded when the commodity is ready for sale; may be cash or non-cash revenues.
- Includes only business revenues.
- Issues: In which period was it earned? Is it a cash or non-cash revenue?

What is Included in Revenues?

- Cash
  - Sale of commodities
  - Performance of services
  - Gain/loss on sale of capital assets
- Non-cash
  - Accounts receivable
  - Inventory

What are NOT Revenues?

- Gifts or inheritance
- Loans
- Non-farm income
- Investments
**Expenses**

- The cost of all inputs used to produce your goods or services; may be cash or non-cash expenses.
- Decreases in ownership claims arising from delivering goods or services or using up assets.

**What is Included in Expenses?**

- Cash
  - Cost of inputs for farm goods or services
  - Interest payment on loans
- Non-cash
  - Depreciation of capital assets
  - Accounts payable
  - Accrued expenses (e.g. property taxes)
  - Prepaid expenses (e.g. fuel, seed, fertilizer)
  - Accrued interest

**What are NOT Expenses?**

- Principal payments on loans
- Personal expenditures (food, clothing, etc.)
- Cash used to purchase depreciable assets in the first year of ownership
Sale of Capital Assets

For non-depreciable assets:
- Gain/loss = sale price – cost
  - (+) implies an increase in market value
  - (–) implies a decrease in market value

For depreciable assets:
- Gain/loss = sale price – book value
  - (+) implies too much depreciation was taken
  - (–) implies too little depreciation was taken

Equations of the Income Statement

NFIO = Revenue – Expenses

and

NFI = NFIO ± gain/loss on sale of capital assets

Difference between NFI and NFIO

- Net farm income from operations: returns to the owner to compensate unpaid (not included in income statement) labor, management, and equity capital used to produce NFIO; an absolute dollar value that must be analyzed based on the size of the operation.
- Net farm income: the same as NFIO but includes gain/loss on sale of capital assets.
- NFIO is a more precise measure of profit or loss.
Relationship Between Balance Sheet and Income Statement

OC Labor and OC Management

- OC: the estimated amount the unpaid owner’s labor could have earned elsewhere for that time
- OCLMT: the estimated amount the unpaid owner’s management could have earned elsewhere for that time
- OC + OCLMT: the “salary” the owner would have been paid for his labor and management
- These values must be estimated on a farm-to-farm basis

Absolute Measures of Profitability

- NFI and NFIO
- Returns to equity = NFIO – OC – OCLMT
- As owner “salary” increases, returns to equity decrease and vice versa.
- Returns to debt capital = total interest expense
- The cost of borrowing money
- Returns to assets = returns to equity + returns to debt = [NFIO – OC – OCLMT] + total interest expense
- Includes all capital – both owner and lender
Profitability Ratios

- Measures of the efficiency of a business in using its resources to produce profit or income; a business can have a poor profitability rating if their profit is small relative to the size of the business.
  - Rate of return on assets (ROA)
  - Rate of return on debt capital (ROD)
  - Rate of return on equity (ROE)
  - Operating profit margin ratio (OPMR)

Income Statement and Balance Sheet Relationship

For ROA, ROD, and ROE:
- The denominator comes from the balance sheets from the beginning and end of the income statement period.
- Ex: for ROA, the denominator is “average assets,” which equals “(beginning + ending assets) / 2”
- The numerator comes from the current income statement.

ROE

\[ \text{ROE} = \frac{\text{returns to equity}}{\text{average equity}} \times 100 \]

- A percentage measure of the rate of return on owner capital
- Ex: if ROE = 8.5%, owner earns 8.5 cents per dollar of revenue.
**ROD**

ROD = \( \frac{\text{total interest expense}}{\text{average liabilities}} \times 100 \)

- A percentage measure of the rate of return on debt capital; to lenders
- Ex: if ROD = 7.2%, lender earns 7.2 cents per dollar of revenue

**ROA**

ROA = \( \frac{\text{returns to assets}}{\text{average assets}} \times 100 \)

- Also called rate of return on investment (ROI)
- A percentage measure of the rate of return to both owner and lenders
- Ex: if ROA = 5.5%, business assets earn 5.5 cents per dollar of revenue

**OPMR**

OPMR = \( \frac{\text{operating profit}}{\text{total revenue}} \times 100 \)

- Operating profit is the same as returns to assets: \([\text{NFIO} – \text{OC}_L – \text{OC}_\text{MGT}] + \text{interest expense}\)
- A higher OPMR means more profit per dollar of revenue, ex: OPMR = 15.8% means that for every dollar of revenue, 15.8 cents remains as profit

Section 3-140
References


Sources of Additional Information


Contact Information

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kmcg@uark.edu

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Nathan Kemper  
Research Associate  
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479-575-5226  
kemper@uark.edu
Acknowledgements

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USDA/RMA under Award Number 08IE08310225-C

We also gratefully acknowledge additional support from

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of any information disclosed in this document.
### Lesson 3.4 Income Statement Example: Robert and Roberta Roberts

<table>
<thead>
<tr>
<th>Item</th>
<th>January 1, 2009 - December 31, 2009</th>
<th>Amount ($)</th>
<th>Comment</th>
</tr>
</thead>
<tbody>
<tr>
<td>a</td>
<td>Sales of corn to local elevator</td>
<td>130,443</td>
<td>write-in income</td>
</tr>
<tr>
<td>b</td>
<td>Sold hay to neighbor</td>
<td>32,611</td>
<td>write-in income</td>
</tr>
<tr>
<td>c</td>
<td>Sales of feeder steers</td>
<td>342,876</td>
<td>market livestock</td>
</tr>
<tr>
<td>d</td>
<td>Sales of livestock products</td>
<td>118,117</td>
<td></td>
</tr>
<tr>
<td>e</td>
<td>Government payments received</td>
<td>106,332</td>
<td></td>
</tr>
<tr>
<td>f</td>
<td>Other farm income</td>
<td>20,254</td>
<td></td>
</tr>
<tr>
<td>g</td>
<td>Purchases of feeder calves for feeding out</td>
<td>113,200</td>
<td>purchases for resale</td>
</tr>
<tr>
<td>h</td>
<td>Purchased feed for feeder calves</td>
<td>65,921</td>
<td>purchased feed grain</td>
</tr>
<tr>
<td>i</td>
<td>Amount spent on chemicals for crops</td>
<td>10,010</td>
<td></td>
</tr>
<tr>
<td>j</td>
<td>Lime and fertilizer expenses</td>
<td>34,059</td>
<td></td>
</tr>
<tr>
<td>k</td>
<td>Trucking expenses</td>
<td>36,352</td>
<td></td>
</tr>
<tr>
<td>l</td>
<td>Total cost of gas and oil</td>
<td>15,738</td>
<td></td>
</tr>
<tr>
<td>m</td>
<td>Insurance cost</td>
<td>4,791</td>
<td></td>
</tr>
<tr>
<td>n</td>
<td>Interest paid on land and machinery loans</td>
<td>32,325</td>
<td>term interest</td>
</tr>
<tr>
<td>o</td>
<td>Operating interest payments</td>
<td>18,662</td>
<td></td>
</tr>
<tr>
<td>p</td>
<td>Hired labor and wages</td>
<td>29,324</td>
<td></td>
</tr>
<tr>
<td>q</td>
<td>Machinery rent</td>
<td>4,527</td>
<td></td>
</tr>
<tr>
<td>r</td>
<td>Cropland rent payments</td>
<td>76,164</td>
<td></td>
</tr>
<tr>
<td>s</td>
<td>Repairs and maintenance</td>
<td>27,941</td>
<td></td>
</tr>
<tr>
<td>t</td>
<td>Seeds purchased</td>
<td>13,997</td>
<td></td>
</tr>
<tr>
<td>u</td>
<td>Purchased supplies</td>
<td>6,734</td>
<td></td>
</tr>
<tr>
<td>v</td>
<td>Taxes paid</td>
<td>9,633</td>
<td></td>
</tr>
<tr>
<td>w</td>
<td>Farm portion of utilities bill</td>
<td>8,575</td>
<td></td>
</tr>
<tr>
<td>x</td>
<td>Vet fees and medicine</td>
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<td></td>
</tr>
<tr>
<td>y</td>
<td>Irrigation and drying expenses</td>
<td>34,327</td>
<td>write-in expense</td>
</tr>
<tr>
<td>z</td>
<td>Farm accountant and tax preparation expense</td>
<td>9,138</td>
<td>write-in expense</td>
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<tr>
<td>aa</td>
<td>Miscellaneous expenses</td>
<td>7,387</td>
<td>write-in expense</td>
</tr>
<tr>
<td>ab</td>
<td>Depreciation</td>
<td>71,288</td>
<td></td>
</tr>
</tbody>
</table>

Robert and Roberta Roberts example courtesy Dr. Lucas D. Parsch
Associate Department Head – Curriculum & Teaching
Agricultural Economics and Agribusiness
217 Agriculture Building
1 University of Arkansas
Fayetteville, AR 72701
(479) 575-2323
lparsch@uark.edu
### Summary Balance Sheet

<table>
<thead>
<tr>
<th>Balance Sheet Item</th>
<th>1-Jan-09</th>
<th>31-Dec-09</th>
<th>Average</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current Assets</td>
<td>$33,740</td>
<td>$27,980</td>
<td>$30,860</td>
</tr>
<tr>
<td>Non-current assets</td>
<td>$1,344,268</td>
<td>$1,403,414</td>
<td>$1,373,841</td>
</tr>
<tr>
<td>Total assets</td>
<td>$1,378,008</td>
<td>$1,431,394</td>
<td>$1,404,701</td>
</tr>
<tr>
<td>Current Liabilities</td>
<td>$25,680</td>
<td>$24,450</td>
<td>$25,065</td>
</tr>
<tr>
<td>Non-current liabilities</td>
<td>$706,420</td>
<td>$688,550</td>
<td>$697,485</td>
</tr>
<tr>
<td>Total liabilities</td>
<td>$732,100</td>
<td>$713,000</td>
<td>$722,550</td>
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<tr>
<td>Equity</td>
<td>$645,908</td>
<td>$718,394</td>
<td>$682,151</td>
</tr>
<tr>
<td>Total liabilities and equity</td>
<td>$1,378,008</td>
<td>$1,431,394</td>
<td>$1,404,701</td>
</tr>
</tbody>
</table>

### Dollar Returns Measures

1. **Opportunity Cost**
   - Labor: $45,000
   - Mgt: $5,000

2. **Returns to Equity**

3. **Financial Ratios**

4. **Rates of Return (Profitability Ratios)**
   - ROD %
   - ROA %
   - ROE %
   - OPMR %

### Farm Expenses

- **Breeding Fees**
- **Spray/Chemicals**
- **Conservation Expenses**
- **Custom Hire**
- **Fertilizer and Lime**
- **Freight and Trucking**
- **Gasoline, Fuels, and Oils**
- **Insurance**
- **Term Interest**
- **Operating Interest**
- **Labor Hired**
- **Rent-Machine Rental**
- **Rent-Real Estate**
- **Repairs, Maintenance**
- **Seeds, Plants Purchased**
- **Storage, Warehousing**
- **Supplies, Purchased**
- **Taxes**
- **Utilities**
- **Vet Fees, Medicine**
- **Other Farm Expenses**

**Example Only**

Section 3-145
# Lesson 3.4 Income Statement Example: Robert and Roberta Roberts

<table>
<thead>
<tr>
<th>Item</th>
<th>January 1, 2009 - December 31, 2009</th>
<th>Amount ($)</th>
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<tbody>
<tr>
<td>a</td>
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<td>Sold hay to neighbor</td>
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<td>Vet fees and medicine</td>
<td>3,721</td>
<td></td>
</tr>
<tr>
<td>y</td>
<td>Irrigation and drying expenses</td>
<td>34,327</td>
<td>write-in expense</td>
</tr>
<tr>
<td>z</td>
<td>Farm accountant and tax preparation expense</td>
<td>9,138</td>
<td>write-in expense</td>
</tr>
<tr>
<td>aa</td>
<td>Miscellaneous expenses</td>
<td>7,387</td>
<td>write-in expense</td>
</tr>
<tr>
<td>ab</td>
<td>Depreciation</td>
<td>71,288</td>
<td></td>
</tr>
</tbody>
</table>

Robert and Roberta Roberts example courtesy Dr. Lucas D. Parsch
Associate Department Head – Curriculum & Teaching
Agricultural Economics and Agribusiness
217 Agriculture Building
1 University of Arkansas
Fayetteville, AR 72701
(479) 575-2323
lparsch@uark.edu
### Summary Balance Sheet

<table>
<thead>
<tr>
<th>Balance Sheet Item</th>
<th>1-Jan-09</th>
<th>31-Dec-09</th>
<th>Average</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current Assets</td>
<td>$33,740</td>
<td>$27,980</td>
<td>$30,860</td>
</tr>
<tr>
<td>Non-current assets</td>
<td>1,344,268</td>
<td>1,403,414</td>
<td>1,373,841</td>
</tr>
<tr>
<td>Total assets</td>
<td>1,378,008</td>
<td>1,431,394</td>
<td>1,404,701</td>
</tr>
<tr>
<td>Current Liabilities</td>
<td>25,680</td>
<td>24,450</td>
<td>25,065</td>
</tr>
<tr>
<td>Non-current liabilities</td>
<td>706,420</td>
<td>688,550</td>
<td>697,485</td>
</tr>
<tr>
<td>Total liabilities</td>
<td>732,100</td>
<td>713,000</td>
<td>722,550</td>
</tr>
<tr>
<td>Equity</td>
<td>645,908</td>
<td>718,394</td>
<td>682,151</td>
</tr>
<tr>
<td>Total liabilities and equity</td>
<td>1,378,008</td>
<td>1,431,394</td>
<td>1,404,701</td>
</tr>
</tbody>
</table>

### Dollar Returns Measures

| Opportunity Cost Labor | 45,000 |
| Opportunity Cost Mgt   | 5,000  |
| Opportunity Cost Total | 50,000 |
| Returns to Equity      | 71,749 |
| Returns to Debt        | 50,987 |
| Returns to Assets      | 122,736|
| Operating Profit       | 122,736|

### Financial Ratios

| Current Ratio | 1.31 | 1.14 | 1.23 |
| Debt:Equity   | 1.13 | 0.99 | 1.06 |
| Debt:Assets   | 0.53 | 0.50 | 0.51 |
| Equity:Assets | 0.47 | 0.50 | 0.49 |

### Rates of Return (Profitability Ratios)

| ROD %         | 7.06 |
| ROA %         | 8.74 |
| ROE %         | 10.52|
| OPMR %        | 16.35|

---

**Example Only**

Section 3-147
Lesson 3.6: Cash Flow Budgeting

Estimated time: One hour.

Overview

Lesson 3.6 is an introduction to cash flow budgeting: its components and purpose. You will learn to manage your business plans and monthly cash flow by using it on a regular basis. At the end of this lesson, you will view a cash flow budget and construct a cash flow budget for investment analysis.

Objectives

1. Identify differences between forward cash flow budgeting and a cash flow statement.
2. Identify the purpose of cash flow budgeting for investment analysis and how to use it in your farm business.
3. Construct a cash flow budget for investment analysis.
4. Apply concepts to your farm business accounting system.

Assessment

Students will construct a cash flow budget for investment analysis at the end of the period. They will take home a handout of one year’s monthly cash flow budgets and a handout of the key to the cash flow budget for investment analysis.

Equipment, Supplies, and Materials

1. Power Point presentation Lesson 3.6
3. Handout "Cash flow budget for investment analysis KEY"

References

# Classroom Procedures

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
</table>
| Slides 3-4: Overview and objectives | • Lead discussion to assess students’ previous knowledge of the subject.  
• Go over objectives. |
| Slide 5: Identify other forms of budgeting and sources and uses of cash | • Other types of budgets include partial and enterprise budgeting.  
• Cash flow budgeting also includes personal expenses and non-farm income, unlike the balance sheet and income statement. |
| After slide 7: Explain relationship between monthly cash flow budgets, cash flow budgets for investment analysis, and cash flow statements are related. | • Monthly cash flow budgets are *estimations* of future inflows and outflows so you can plan ahead.  
• Cash flow statements are the *actual* inflows and outflows and are created after the period is over. Records are important for future planning.  
• Cash flow budgets for investment analysis are created before an asset is purchased or a plan is implemented to determine if it is financially feasible and how long it will take for the investment to return a positive net cash flow. |
| Slide 11: Graphical representation of cash flows | • The farm business checking account is the central point for identifying and measuring cash flow. It is assumed that all cash moves into and out of the checking account. |
| Slide 12: Monthly example – first tab in excel worksheet | • The totals column is calculated by adding together the values for every month along a row. It is not calculated because only three months are shown.  
• Emphasize that line 56 from Jan is the value for line 1 in Feb  
• The totals column is calculated for a whole year, but the values are not all shown. |
| Slide 12: Investment analysis example – second tab in excel worksheet | • P&I: principal and interest  
• Investment analysis can be over a period of months (short term) or over a period of years (long term) as in the example.  
• Remember net cash flow = total cash inflows – cash outflows |
Sources of Additional Information

   http://www.smallbusinessnotes.com/operating/finmgmt/financialstmts/gettingstarted.html
   http://www.agmrc.org/business_development/operating_a_business/finance/financial_statements.cfm
   http://www.smallbusinessnotes.com/operating/finmgmt/cashmanagement.html

Contact Information

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Division of Agriculture  
479-575-5226  
nkemper@uark.edu
Overview

- Lesson 3.6 is an introduction to cash flow budgeting: its components and purpose
- You will learn to manage your business plans and monthly cash flow by using it on a regular basis
- At the end of this lesson, you will view a cash flow budget and construct a cash flow budget for investment analysis

Objectives

1. Identify differences between forward cash flow budgeting and a cash flow statement
2. Identify the purpose of cash flow budgeting for investment analysis and how to use it in your farm business
3. Apply concepts to your farm business accounting system
Monthly Cash Flow Budgeting

- Estimates projected cash flows as part of forward planning
- Not a substitute for any other budgeting tools
- Estimates the amount and timing of future borrowing needs and the ability to repay loans
- Concerned with the amount and timing of cash inflows and outflows but not the source or use of cash
- Can identify cash shortages so purchases can be rearranged to minimize borrowing

Cash Flow Budget for Investment Analysis

- Determines an investment’s financial feasibility
- Partial budgeting determines an investment’s economic profitability
- An investment can be financially feasible but not economically profitable and vice versa
- Estimates projected cash inflows as a result of proposed investment
- Estimates the additional amount and timing of future borrowing needs as a result of proposed investment

Cash Flow Statement

- Monitor actual cash flows from farm records
- Summarizes a firm’s cash inflows and cash outflows
- Not a measure of profit
- Done on a monthly or quarterly basis
- Purpose is the estimation of net cash flow (NCF)
- Comparison of monthly cash flow budget to cash flow statement can provide early warning of significant deviations. Determine causes Make adjustments
Equation of Cash Flow Statement

Net Cash Flow =
Total Cash Inflows – Total Cash Outflows

Cash Inflows
- Not only revenue – all cash inflows
- Includes non-farm and personal cash revenue
- Included:
  - Beginning checking account balance
  - Revenues
  - Non-farm cash receipts
  - Cash from sale of capital assets
  - Cash from new loans
- Excluded:
  - Inventory changes

Cash Outflows
- Not only expenses – all cash outflows
- Includes non-farm and personal cash expenses
- Included:
  - Principal and interest payments on loans
  - Family living expenses
  - Social security and income taxes
  - Purchase price cost of new capital items
  - Farm operating expenses
- Excluded:
  - Depreciation

Section 3-153
Cash Flow Budget Examples

- Monthly cash flow budget
- Cash flow budget for investment analysis

References


Sources of Additional Information


Contact Information

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  University of Arkansas
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- Jennie Popp, Ph.D.
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  nkemper@uark.edu
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Walmart

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express or implied, or assumes any legal liability or
responsibility for the accuracy, completeness, or usefulness
of any information disclosed in this document.
<table>
<thead>
<tr>
<th>Name: I.M. Farmer</th>
<th>Cash Flow Budget</th>
<th>Year 2010</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Total</td>
<td>Jan</td>
</tr>
<tr>
<td>1 Beginning Cash Balance</td>
<td>2,500</td>
<td>2,500</td>
</tr>
<tr>
<td>Operating receipts:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2 Grain and feed</td>
<td>160,000</td>
<td>20,000</td>
</tr>
<tr>
<td>3 Feeder livestock</td>
<td>88,000</td>
<td></td>
</tr>
<tr>
<td>4 Livestock products</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5 Other</td>
<td>5,400</td>
<td></td>
</tr>
<tr>
<td>Capital receipts:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>7 Breeding livestock</td>
<td>3,800</td>
<td></td>
</tr>
<tr>
<td>8 Machinery and equipment</td>
<td></td>
<td></td>
</tr>
<tr>
<td>9</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Non-farm income:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>10 Wages and salary</td>
<td>7,200</td>
<td>600</td>
</tr>
<tr>
<td>11 Investments</td>
<td>200</td>
<td>200</td>
</tr>
<tr>
<td>12</td>
<td></td>
<td></td>
</tr>
<tr>
<td>13 Total cash inflow</td>
<td>267,100</td>
<td>23,300</td>
</tr>
<tr>
<td>(add lines 1-12)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Operating expenses:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>14 Seed</td>
<td>5,800</td>
<td></td>
</tr>
<tr>
<td>15 Fertilizer and lime</td>
<td>26,000</td>
<td></td>
</tr>
<tr>
<td>16 Pesticides</td>
<td>4,000</td>
<td></td>
</tr>
<tr>
<td>17 Other crop expenses</td>
<td>2,600</td>
<td></td>
</tr>
<tr>
<td>18 Gas, oil, lubricants</td>
<td>3,000</td>
<td></td>
</tr>
<tr>
<td>19 Hired labor</td>
<td>6,000</td>
<td></td>
</tr>
<tr>
<td>20 Machine hire</td>
<td>800</td>
<td></td>
</tr>
<tr>
<td>21 Feed and grain</td>
<td>4,000</td>
<td>800</td>
</tr>
<tr>
<td>22 Feeder livestock</td>
<td>36,000</td>
<td></td>
</tr>
<tr>
<td>23 Livestock expenses</td>
<td>7,500</td>
<td>1,000</td>
</tr>
<tr>
<td>24 Repairs - machinery</td>
<td>3,600</td>
<td>500</td>
</tr>
<tr>
<td>25 Repairs - buildings</td>
<td>1,800</td>
<td></td>
</tr>
<tr>
<td>26 Cash rent</td>
<td></td>
<td></td>
</tr>
<tr>
<td>27 Supplies</td>
<td>1,000</td>
<td>250</td>
</tr>
<tr>
<td>28 Property taxes</td>
<td>3,400</td>
<td></td>
</tr>
<tr>
<td>29 Insurance</td>
<td>700</td>
<td>700</td>
</tr>
<tr>
<td>30 Utilities</td>
<td>600</td>
<td>50</td>
</tr>
<tr>
<td>31 Auto and pickup (farm share)</td>
<td>1,200</td>
<td>100</td>
</tr>
<tr>
<td>32 Other farm expenses</td>
<td>500</td>
<td>100</td>
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<tr>
<td>33</td>
<td></td>
<td></td>
</tr>
<tr>
<td>34</td>
<td></td>
<td></td>
</tr>
<tr>
<td>35 Total cash operating expenses</td>
<td>108,500</td>
<td>1,650</td>
</tr>
<tr>
<td>(add lines 14-34)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital expenditures:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>36 Machinery and equipment</td>
<td>60,000</td>
<td></td>
</tr>
<tr>
<td>37 Breeding livestock</td>
<td>1,000</td>
<td></td>
</tr>
<tr>
<td>38</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Section 3-157
<p>| | | | | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
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<th></th>
<th></th>
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<tbody>
<tr>
<td>39</td>
<td>Family living expenses</td>
<td>36,000</td>
<td>3,000</td>
<td>3,000</td>
</tr>
<tr>
<td>40</td>
<td>Income tax and social security</td>
<td>8,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>41</td>
<td>Other non-farm expenses</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>42</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>43</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>44</td>
<td>Scheduled debt payments:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>45</td>
<td>Current debt - principal</td>
<td>0</td>
<td></td>
<td></td>
</tr>
<tr>
<td>46</td>
<td>Current debt - interest</td>
<td>0</td>
<td></td>
<td></td>
</tr>
<tr>
<td>47</td>
<td>Noncurrent debt - principal</td>
<td>32,000</td>
<td>6,000</td>
<td></td>
</tr>
<tr>
<td>48</td>
<td>Noncurrent debt - interest</td>
<td>27,200</td>
<td>12,000</td>
<td></td>
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<tr>
<td>49</td>
<td>Total cash outflow</td>
<td>272,700</td>
<td>4,650</td>
<td>24,000</td>
</tr>
<tr>
<td>50</td>
<td>Cash available (subtract line 13 - line 48)</td>
<td>(5,600)</td>
<td>18,650</td>
<td>15,250</td>
</tr>
<tr>
<td>51</td>
<td>New borrowing:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>52</td>
<td>Current</td>
<td>92,700</td>
<td></td>
<td></td>
</tr>
<tr>
<td>53</td>
<td>Noncurrent</td>
<td>40,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>54</td>
<td>Total new borrowing</td>
<td>132,700</td>
<td></td>
<td></td>
</tr>
<tr>
<td>55</td>
<td>Payments on new current debt</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>56</td>
<td>Ending cash balance</td>
<td>31,526</td>
<td>18,650</td>
<td>15,250</td>
</tr>
<tr>
<td>57</td>
<td>Summary of debt outstanding</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>58</td>
<td>Current (beginning of $0)</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>59</td>
<td>Noncurrent (beginning of $340,000)</td>
<td>340,000</td>
<td>340,000</td>
<td>340,000</td>
</tr>
<tr>
<td>60</td>
<td>Total debt outstanding</td>
<td>340,000</td>
<td>340,000</td>
<td>340,000</td>
</tr>
</tbody>
</table>
Purchase an irrigation system on 120 acres of cropland

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
<th>Notes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost of system</td>
<td>$60,000</td>
<td></td>
</tr>
<tr>
<td>Down payment</td>
<td>$18,000</td>
<td>P&amp;I</td>
</tr>
<tr>
<td>Capital borrowed</td>
<td>$42,000</td>
<td>(Outflows)</td>
</tr>
<tr>
<td>(3 yrs @ 12%)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Additional expenses from higher input levels</td>
<td>$3,600</td>
<td>Outflows</td>
</tr>
<tr>
<td>($30 per acre)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Irrigation expenses</td>
<td>$3,000</td>
<td>Outflows</td>
</tr>
<tr>
<td>($25 per acre)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Additional revenue from yield increase</td>
<td>$16,800</td>
<td>Inflows</td>
</tr>
<tr>
<td>($140 per acre)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Long term investment - multiple year cash flow analysis
<table>
<thead>
<tr>
<th>Cash inflow</th>
<th>Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>Increase in crop income</td>
<td>→</td>
</tr>
<tr>
<td><strong>Total cash inflow</strong></td>
<td></td>
</tr>
<tr>
<td><strong>Cash outflow</strong></td>
<td></td>
</tr>
<tr>
<td>Down payment</td>
<td></td>
</tr>
<tr>
<td>Taxes and insurance</td>
<td></td>
</tr>
<tr>
<td>Additional crop expenses</td>
<td>→</td>
</tr>
<tr>
<td>Irrigation expenses</td>
<td></td>
</tr>
<tr>
<td>Principal payments</td>
<td></td>
</tr>
<tr>
<td>Interest payments</td>
<td></td>
</tr>
<tr>
<td><strong>Total cash outflow</strong></td>
<td></td>
</tr>
<tr>
<td><strong>Net cash flow</strong></td>
<td>→</td>
</tr>
<tr>
<td></td>
<td>Year</td>
</tr>
<tr>
<td>--------------------</td>
<td>-------</td>
</tr>
<tr>
<td></td>
<td>1</td>
</tr>
<tr>
<td><strong>Cash inflow</strong></td>
<td></td>
</tr>
<tr>
<td>Increase in crop income</td>
<td>16,800</td>
</tr>
<tr>
<td>Total cash inflow</td>
<td>16,800</td>
</tr>
<tr>
<td><strong>Cash outflow</strong></td>
<td></td>
</tr>
<tr>
<td>Down payment</td>
<td>18,000</td>
</tr>
<tr>
<td>Taxes and insurance</td>
<td>1,000</td>
</tr>
<tr>
<td>Additional crop expenses</td>
<td>3,600</td>
</tr>
<tr>
<td>Irrigation expenses</td>
<td>3,000</td>
</tr>
<tr>
<td>Principal payments</td>
<td>14,000</td>
</tr>
<tr>
<td>Interest payments</td>
<td>5,040</td>
</tr>
<tr>
<td>Total cash outflow</td>
<td>44,640</td>
</tr>
<tr>
<td><strong>Net cash flow</strong></td>
<td>-27,840</td>
</tr>
</tbody>
</table>
Lesson 3.7: Labor Management

*Estimated time: One hour.*

**Overview**

Lesson 3.7 will cover some important labor issues for farm business managers to consider. Occupational and worker safety will be discussed including general requirements, labor laws, some of the hazardous tasks on the farm and child labor laws. The employer-employee relationship will be covered focusing on worker’s compensation, employer’s duties and defenses and liability issues. Key concepts and practices for good farm labor management will be explored focusing on three main subject areas: compensation - including wage and hour agreements, benefits and incentives; working conditions; and the employer-employee relationship. Finally, a handout on best labor practices will be distributed and a brief overview of the findings “10 Positive Practices” will be discussed.

**Objectives**

1. Review basic occupational and worker safety information
2. Discuss labor laws and child safety issues
3. Examine the employer/employee relationship and identify the greatest areas of risk to employers
4. Review the requirements for workers compensation
5. Consider best practices in managing farm labor
6. Read the handout: Best Labor Practices

**Assessment**

Participants will view the presentation on labor management and participate throughout with question and answers. The presenter will engage the audience to keep their interest and attention focused on the materials. Participants will take notes on provided handouts and will be encouraged to read the provided materials and visit listed websites for more information. The handout: Best Labor Practices will be distributed and attendees should be encouraged to read the article to get more tips on positive practices that could improve their labor force.
Equipment, Supplies, and Materials

1. Power Point presentation Lesson 3.7
2. Notes pages Lesson 3.7
3. Additional reading materials and links
4. Handout - Best Labor Practices on Twelve California Farms

References


Classroom Procedures

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
</table>
| Introduction Slides 2-3: give an overview of the topics to be covered in the presentation and outline the learning objectives. | • Engage the audience by asking them about their operations  
• What are the biggest labor issues on your farm?  
• How do you handle worker safety issues?  
• What do you do to recruit and retain good quality workers?  
• Do you offer benefits or bonuses and other incentives? |
| Slides 4-5: OSHA and Worker Safety | • Slide 4: OSHA  
  1. How many of you have gone through an OSHA safety inspection?  
  2. Everyone wants a safe work place, but a visit from OSHA can raise concerns.  
  3. Preparing for an inspection is an important activity. OSHA's only means to enforce compliance is through inspection.  
  4. Prepare for the inspection just as you would prepare for a presentation to an important customer or client.  
• Slide 5: Farm family members are not typically counted as employees - but check because this could change |
## Classroom Procedures Continued

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| **Slide 6-9: Worker Safety - Agriculture is Dangerous** | - **Agriculture is a Dangerous Business**  
  The following factors may increase risk of injury or illness for farm workers:  
  1. **Age** – Injury rates are highest among children age 15 and under and adults over 65.  
  2. **Equipment and Machinery** – Most farm accidents and fatalities involve machinery. Proper machine guarding and doing equipment maintenance according to manufacturers’ recommendations can help prevent accidents.  
  3. **Protective Equipment** – Using protective equipment, such as seat belts on tractors, and personal protective equipment (such as safety gloves, coveralls, boots, hats, aprons, goggles, face shields) could significantly reduce farming injuries.  
  4. **Medical Care** – Hospitals and emergency medical care are typically not readily accessible in rural areas  
- **Livestock operations can pose specific threats such as manure pit collection systems**  
- **NIOSH makes several recommendations for ensuring worker safety regarding manure pits** |
| **Slides 10-11: How to Keep Workers Safe** | - **Some dangerous conditions are regulated. Check federal and state regulations.**  
  - **General Duty** - states that employers are required to keep the workplace free of recognized hazard that can cause serious injury or death  
  - **General Duty requires some specific actions by employers**  
  - **How can you improve farm safety? In general:**  
    1. Increase your awareness of hazards  
    2. Prepare for emergencies  
    3. Special attention on threats to children and elderly  
    4. Provide good tools and equipment  
    5. Read and follow equipment manuals instructions  
    6. Routinely inspect equipment  
    7. Discuss hazards with workers  
    8. Take advantage of safety equipment  
- **Better safety and health practices:**  
  1. Reduce worker fatalities, injuries, and illnesses  
  2. Reduce associated costs such as workers’ compensation insurance premiums, lost production, and medical expenses.  
  3. A safer and more healthful workplace improves morale and productivity. |
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<tbody>
<tr>
<td></td>
<td>• The FLSA covers employees whose work involves production of agricultural goods which will leave the state directly or indirectly and become a part of interstate commerce.</td>
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<td></td>
<td>• Examples of Hazardous Occupation in Agriculture</td>
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<tr>
<td></td>
<td>1. operating a tractor of over 20 PTO horsepower;</td>
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<td></td>
<td>2. operating a grain combine, hay mower, hay baler, feed grinder, auger conveyor, power post-hole digger;</td>
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<td>3. operating a fork lift, a power-driven circular, band or chain saw;</td>
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<td>4. working in a yard, pen, or stall occupied by a bull, boar, or stud horse maintained for breeding purposes;</td>
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<td></td>
<td>5. felling, buckling, skidding, loading, or unloading timber with a base diameter or more than 6 inches;</td>
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<td></td>
<td>6. working from a ladder or scaffold at a height of over 20 feet;</td>
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<td></td>
<td>7. driving an automobile to transport passengers, or riding on a tractor as a passenger or helper;</td>
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<td></td>
<td>8. handling or applying toxic agricultural chemical identified by the words &quot;danger,&quot; &quot;poison,&quot; or &quot;warning&quot; or a skull and crossbones on the label;</td>
</tr>
<tr>
<td></td>
<td>9. transporting, transferring, or applying anhydrous ammonia.</td>
</tr>
<tr>
<td>Slide 12-13: Child Safety</td>
<td></td>
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<tr>
<td>Slides 14-17: Employer Considerations</td>
<td>• Employee injuries on the job is a big risk to the business</td>
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<td></td>
<td>• Fulfill the general duties of an employer. This will help protect you by ensuring the safety of employees</td>
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<tr>
<td></td>
<td>• An employer does have some protections too</td>
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<td></td>
<td>• Briefly review the key components to an employer’s defense if an employee is injured on the job</td>
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<td>• Recommend the Office of Workers’ Compensation Programs for more information (Slide 14)</td>
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| Slides 14-17: Employer Considerations (cont.) | • Workers' compensation  
  1. Covers most, but not all, on-the-job injuries.  
  2. The workers' compensation system is designed to provide benefits to injured workers, even if an injury is caused by the employer's or employee's carelessness.  
  3. But there are some limits. Coverage may also be denied in situations involving:  
     a. self-inflicted injuries (including those caused by a person who starts a fight)  
     b. injuries suffered while a worker was committing a serious crime  
     c. injuries suffered while an employee was not on the job, and  
     d. injuries suffered when an employee's conduct violated company policy.  
• Amounts of recovery award are fixed and vary by injury and body part |
| Slides 18-19: Managing Farm Labor: | • Who can you recruit and keep good quality farm labor while competing with non-farm employers?  
• Three important areas of managing farm labor: compensation, working conditions and your relationships with your workers  
• Best Labor Practices: there are a number of ways that managers can improve on labor management  
  1. Several no- or low-cost practices  
  2. In fact, some of these low cost practices, such as respectful treatment and a reasonable work place are among those most valued by farm workers.  
  3. Others, such as bonuses and year-round employment may cost more, but also yield important benefits for farmers. |
| Slides 23-28: Compensation | • How does your compensation package compare to your competitors?  
• Is your compensation package fair?  
• Consider offering incentives at least once a year  
• Reward workers whenever possible  
• Create consistent pay levels based on skill and responsibility  
• Communicate clearly profit-sharing plans |
## Classroom Procedures Continued

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| **Slides 29-30: Working Conditions**     | • Limit stoop labor where possible  
• Do your supervisors know how to provide adequate medical attention in case of injury?  
• Eliminate possible hazards  
• High Quality tools and machinery can limit injury |
| **Slides 31-34: Employer-Employee**      | • Create and enforce policies about how employees are to be treated  
• Provide formal training for supervisors and foremen about respectful communication styles  
• Survey employees to find out what their needs are, both personal and professional  
• Be flexible with employees to a degree to take care of personal and family needs.  
• Inquire about their personal lives  
• Show appreciation and reward a job well done or completion of a project |
| **Handout: Best Labor Practices**        | • Briefly go over the list on slide 35 and encourage participants to read the handout  
• Are you implementing any of these practices?  
• Many of these are no or low cost practices that can be adopted farm wide. |
Sources of Additional Information

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    http://trmep.tamu.edu/cg/factsheets/rm8-1.pdf
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Labor Management

Lesson 3.7

Overview

- Learn important labor issues for farm business managers
- Worker safety will be discussed including labor laws, on farm hazards and child labor laws
- The employer/employee relationship will be covered focusing on compensation, duties and liability issues
- Good farm labor management practices will be explored focusing on compensation, working conditions, and the employer-employee relationship
- Best labor practices observed on California farms will be presented along with a handout

Objectives

1) Review basic occupational and worker safety information
2) Discuss labor laws and child safety issues
3) Examine the employer/employee relationship and identify the greatest areas of risk to employers
4) Review the requirements for workers compensation
5) Consider best practices in managing farm labor
6) Read the handout: 10 Positive Labor Practices
Occupational Safety

- Occupational Safety and Health Act (OSHA) ensures safe and healthy working conditions
- The OSHA act generally does not apply to agricultural work places
- Generally, OSHA doesn't apply to farm operations with less than 10 employees

Worker Safety

- Farm Family Members
  - Are farm family members counted as employees?
    - Generally no, even if they are paid
    - But, every year Congress must decide whether to cover farm family members or not, so you must stay informed

- Agriculture ranks as one of the most dangerous activities
- Farm vehicle accidents are frequent
- Farm workers must be trained on how to handle hazardous chemicals
- There are some key factors that may increase risk
  - Age, equipment and machinery, protective equipment and medical care

Section 3-171
Worker Safety

Hazardous agricultural tasks include:
- Using farm machinery
- Hay balers
- Feed grinders
- Power post-hole diggers
- Working in a farmyard pen or stall with a bull, board or stud horse kept for breeding
- Working with a sow with suckling pigs, cows with newborn calves
- Working inside manure pits

Livestock Operations

Manure pit collection systems for animal waste can be hazardous operations
- The general duty clause applies
- The national institute for occupational safety and health (NIOSH) recommends posting manure pits with hazardous warning signs that can be understood by all workers

NIOSH also suggests:
- Access points for entry to manure pits be restricted
- Air monitoring around manure pits
- Emergency rescue procedures
Worker Safety

- Regulation of Dangerous Conditions
  - Handling of anhydrous ammonia
  - Slow-moving equipment or vehicles
  - Roll-over protective structures for tractors
  - Guards or shields on agriculture equipment
  - General duty: all employers are under a general duty to keep the workplace free of recognized hazards that can cause serious injury or death

Worker Safety

- General Duty Requirements
  - Other requirements employers must comply with under the "general duty" are:
  - Posting OSHA posters
  - Informing employees of safety regulations
  - Maintain up-to-date records of injuries and illnesses
  - Report fatalities occurring on the job
  - Inform employees concerning potential hazards of chemicals

Worker Safety

- Labor Laws and the Safety of Children
  - The Fair Labor Standards Act of 1938 (FLSA) as amended, sets standards for youth employment in agriculture
  - Many children are injured every year in agriculture-related accidents
  - Children of any age cannot be used in agricultural jobs that are hazardous
Worker Safety

- Children can be Employed at Certain Ages
  - Children aged 14 – 16 can be employed if it won’t interfere with their schooling
  - Children aged 16 and above can do any agricultural task so long as it is not hazardous
  - Some children aged 12 and under can be employed alongside their adult parents

Employer Considerations

- Aside from the employer’s responsibility for the employees wages, the area of greatest risk to the employer is the risk of liability for employee injuries on the job
- By the early 1900s, every state had adopted a worker’s compensation law to cover on-the-job injuries

For More Information on Workers Compensation:

Employer Considerations

- An employer can defend him/herself against cases brought for injuries to his employees if:
  - The employee was aware of the danger
  - The injuries were caused by a co-employee
  - The employee contributed to his own injuries
Employer Considerations

- Workers’ compensation
  - Is no-fault
  - The worker doesn’t have to show that the employer was negligent – he only has to show:
    - The injury
    - The injury occurred while he was acting within the scope of his employment
    - The injury was related to his employment

Employer Considerations

- Employer’s Liability to Others
  - Employer’s can be liable to others for the acts of their employees
  - Liability is imposed if the employee acted “within the scope of employment”
  - If so, the employer and the employee will be held jointly liable
  - If you hire independent contractors and do not control their actions, you may be able to avoid liability if their actions harm another

Managing Farm Labor

- Two Issues at hand
  - Obtaining quality farm labor
  - Keeping quality farm labor
- Farmers must compete with non-farm employers for skilled workers

Section 3-175
Managing Farm Labor

- Compensation: Wage and hour agreements, fringe benefits and incentives
- Working conditions
- Employer-employee relations

Compensation

- Is your wage comparable to other employers
- What would you have to pay someone to replace your best worker
- How to pay employees
  - By hour, week or month?
  - What about overtime pay?
- Are the fringe benefits adequate and up to date?
- How do my fringe benefits compare with those of industry?
- Should I have an incentive plan?

Compensation

- Wage and hour agreements, fringe benefits and incentives
  - Are your fringe benefits adequate and up to date?
  - How do the benefits you are offering compare with those of industry?
  - Should you have an incentive plan?
**Compensation**

- **Wages**
  - Basic hourly wage plus bonus for overtime has been successful for attracting good farm workers
  - Weekly or monthly pay basis for an unstated number of hours
  - Unspecified hours could promote employee dissatisfaction
  - Added management responsibilities of going to an hourly rate of pay with stated hours
  - Hourly demands careful management and planning of jobs to eliminate busy work

- **Fringe Benefits**
  - Traditionally provided as housing, utilities, food and other items from the farm
  - Competing employers will likely include sick leave, paid vacation, hospitalization, life insurance and retirement
  - Help laborers understand the cash value of their benefits by putting a dollar value on rent, food, utilities and other benefits you provide

- **Incentive Plans**
  - Used as part of the total wage package based on:
    - Physical production – payment based on number of bushels, pounds, etc.
    - Tenure – based on length of employment
    - Gross Income – based on a percent of total sales
    - Net Income – based on a percent of taxable income
Compensation

- Incentive Plans
  - Key Principles
    - Reward employees for working in your interest
    - Paid for something within worker’s control
    - Performance based, easy to compute, prompt pay
    - Not deter your managing the farm
    - Not be a substitute for other pay methods or labor management practices
    - In writing signed by both parties

Working Conditions

- Sell your working conditions
  - Opportunity to live close to work
  - Avoid traffic hazards and commute
  - Mechanization has reduced the level of physical labor
  - Daily variety – not monotonous

Working Conditions

- Continuously improve farm working conditions
  - Look to replace “physical” labor jobs
  - Provide sanitary facilities
  - Work schedules within reasonable hours
  - Eliminate hazards to ensure safety of workers
  - Provide quality tools, buildings, machinery and equipment
Employer-Employee Relationship

- The human side of labor management
- Principals are largely psychological
  - Employees want respect and recognition
  - Employers want employees that show initiative and take pride in their work

Employer-Employee Relationship

- Respectful, dignified treatment
  - Workers must feel their jobs are important
  - Employers need to raise the dignity and status of their employees
- Belonging
  - Farm workers want to belong to a successful team
  - Essential to team effort
  - Explore ways of making employees feel that they are indeed a part of the business

Employer-Employee Relationship

- Responsibility
  - Workers usually want responsibility
  - Good way to learn the employee’s potential
- Advancement
  - Workers want opportunities to advance
  - Provided for growth in learning and status
  - Provide rewards for participation in extension meetings or short courses
Employer-Employee Relationship

- Supervision
  - Employees respond to good supervision
  - Planning and explaining the what and how of the job
  - Seeing the job is carried out
  - Carefully planned routines, clear explanations, and business-like supervision can payoff in increased productivity from workers
- Recognition
  - Word of praise may often be neglected
  - When workers do a good job, tell them so

10 Positive Practices

- Improve Working Conditions
  - Improve employee satisfaction and retention
  - Increase productivity while reducing costs
  - Improve access to markets that emphasize fair labor practices

10 Positive Practices

1. Respectful Treatment
2. Fair Compensation
3. Year-Round Employment
4. Traditional Benefits
5. Non-Traditional Benefits
6. Safe and Healthy Workplace
7. Direct Hiring and Recruitment
8. Team-Based Management Structures
9. Open Communication and Decision-Making
10. Professional Development and Advancement
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http://edis.ifas.ufl.edu/HR009

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Best Labor Practices on Twelve California Farms: Toward a More Sustainable Food System

By Ron Strochlic and Kari Hamerschlag

“What I most like about working here is the good treatment. They treat everyone as equals. They have trust in us and what we do. The trust is the most important thing.”

Central Coast farmworker

Sustainable agriculture is often compared to a three-legged stool, resting on the three “E’s” of Environment, Economy and Equity. For an agricultural system to be truly sustainable, it must be environmentally sound, economically viable and socially equitable. Nonetheless, until now, social aspects of sustainable agriculture have been eclipsed by greater attention to environmental and economic concerns. In order to more fully embrace the social side of sustainability, farmers and advocates alike need more information regarding what social sustainability means in practice, its benefits for farmers and farmworkers, and what is feasible within the context of the economic constraints facing growers. This research aims to answer some of these questions, by generating a deeper understanding of social sustainability as it relates to farm labor management.¹

Conversations with numerous sustainable growers have indicated a deep and very real desire to provide better conditions for their workers. Nonetheless, many report they do not know how to do so, most believe they cannot afford to. In order to create a road map for growers who want to do better, and demonstrate what is possible, the California Institute for Rural Studies has set out to document best practices in labor management on twelve sustainable farms in California.² These farms were selected because of their reputation for offering particularly good labor conditions. Information was gathered on site at all but two farms and consisted of in-depth semi-structured interviews with growers and/or farm managers, followed by focus groups with between eight and twelve farmworkers at each site. More than eighty farmworkers were interviewed as part of this process, providing us with valuable insights about what conditions farmworkers value most.

The findings reveal a number of ways that these farms are providing socially sustainable farm labor conditions, including a broad range of no- or low-cost practices that can easily be replicated. In fact, some of these low cost practices, such as respectful treatment, a reasonable work pace, and personal loans, are among those most valued by farmworkers. Others, such as bonuses and year-round employment may cost more, but also yield important benefits for farmers. Farmworkers in our focus groups reported numerous benefits of positive workplace conditions, including improved health, better diet and nutrition, reduced migration and more stable communities.

Growers identified a broad range of benefits of providing good farm labor conditions, including higher retention rates, reduced training and supervision costs, reduced labor short-
ages, a more skilled and invested labor force, better quality production and ultimately, higher profits. The economic constraints preventing growers from providing better labor conditions are real, and must be addressed by initiatives aimed at improving economic opportunities for farmers. However, the practices on these farms demonstrate what is possible within the context of these constraints, and how these practices can actually benefit growers’ bottom line.

The research also identifies room for improvement, even among these more progressive farms. Many growers are still not able to offer a living wage, health insurance, paid sick days, and year-round employment, while few are able to provide seasonal workers with the same benefits as permanent staff. Labor management is also highly informal, with few farms providing clear rules, procedures and policies.

With growing interest for sustainable agriculture to better address social justice concerns, we hope that the examples from these farms will provide farmers with the tools and inspiration to seek ways to improve farm labor conditions. With the emergence of certification schemes stressing social as well as environmental standards, we also hope this research will be useful in helping producers remain competitive in an increasingly socially responsible marketplace.

**Summary of Best Practices**

“The success of the farm is the people that are working on it...they are an integral part of the farm. They are key to the success of the farmer.”

Central Valley farmer

The following is a summary and specific examples of the most outstanding practices identified among the farms in our sample. We also highlight the workplace conditions and benefits that farmworkers most value. It should come as no surprise that farmworkers value what most of us have come to expect or desire from our own places of work: a living wage, respectful treatment, safe conditions, health insurance and other benefits, and the ability to advocate for improved conditions without fear of retribution. The findings reveal that, as in other industries, workers who are treated well and made to feel an integral part of the farm operation are more satisfied, more motivated and ultimately, more productive.

**Respectful Treatment**

“It’s different working here from other places. They don’t say ‘hurry up.’ They treat us well. They don’t demand that we work so fast. We like that.”

Central Valley farmworker

Respectful treatment is ultimately at the core of social equity in sustainable agriculture. This issue is of particular importance for the many farmworkers that have suffered harsh, abusive or exploitative treatment on other farms.

Respectful treatment encompasses a broad range of issues, including a humane pace of work, respectful communication styles, direct grower-worker communications, a healthy work environment, and decision-making structures that recognize the contribution and value of each worker. Contrary to our initial expectations, the farmworkers we met with consistently ranked respectful treatment on par with or higher than wages in terms of importance.

A key element of respectful treatment is the ability to work at a humane pace, without being constantly rushed. Farmworkers consistently cited tremendous relief at being able to work at their own pace, and not being told to work faster by foremen for many hours a day. As one Central Valley farm worker pointed out, “The patrón treats us magnificently. He doesn’t say hurry up. Everyone works at their own pace. In other places they are always on top of you, telling you to work faster.”

Virtually all of the farmers in our sample make a point of treating workers with respect, and have instructed supervisors to address people respectfully. As one farmer put it, “We have a ‘no yell’ policy. My supervisors are not allowed to yell at anyone.” Nevertheless, few farms provide formal training for foremen and supervisors regarding how to treat workers respectfully, or have specific policies codifying respectful treatment for workers.

**Compensation**

“We work harder here because we know that if the farm does well, we do well. At the end of the year, there are bonuses. In other place where I worked, they don’t have bonuses.”

Central Coast farmworker
Fair compensation rates a close second to respectful treatment in terms of what is most important to farmworkers. Given the precarious economics of farming, compensation is a complex issue. Only three farms in our sample offer a truly living wage. However, when all forms of compensation and benefits are taken into account—including profit-sharing, bonuses, health insurance, retirement plans, paid time off, housing support and access to food from the farm—the total value of compensation increases significantly, and more closely approximates a living wage.

All but one of the farms in our sample supplement hourly wages with profit-sharing, a key risk management strategy that allows growers to supplement wages in good years, while keeping labor costs down during bad years. Because labor accounts for approximately 60% of costs among the farms in our sample, growers have a stake in keeping those costs at a level that will ensure the farm’s continued viability.

- **Living Wage**: A diversified Central coast farm pays an average hourly wage of $9-11.25 to field workers, and between $35,000 and $45,000 per year to managers. A vineyard in Napa uses three pay levels for all workers, based on skill and responsibility: Tier A: $13.25; Tier B: 11.75 and Tier C: $11/hour.

- **Regular Pay Increases**: Three farms offer automatic cost of living increases of 5% to 10% each year.

- **Profit-Sharing**: This mid-sized diversified farm provides seasonal and permanent employees with approximately $40,000 in profit-sharing each year, the equivalent of 25 to 50 cents per hour. Profits are distributed twice per year—during the harvest and at the end of the year—as a means of thanking and incentivizing employees.

- **Overtime Pay**: This large corporate farm offers overtime after 8, not 10, hours per day, and 48—not 60, hours per week.

- **Bonuses**: This corporate farm on the Central Coastal provides a bonus of 22 cents per hour worked to everyone remaining through the harvest, amounting to roughly $400 per year.

**Year-round Work**

“We provide year-round employment. That’s huge. It means that our workers can live here with their families. This is their community now. Families go to school here. Kids learn English. They are part of the community now.”

Capay Valley farmer

Given the high levels of seasonal unemployment associated with traditional agriculture, a particularly important benefit of sustainable farms is the ability to offer year-round employment. The diversified and labor-intensive nature of sustainable agriculture allows most of the farms in our sample to provide permanent, year-round employment to at least a portion of their labor force. As a Ventura County farmer explained, “When I farmed conventionally, I had two workers for every 100 acres that I farmed. Now that I’m farming organically, I have one worker for every two acres.”

Farmworkers identified year-round employment as one of the conditions they most value, after good wages and respectful treatment. In addition to a steady income and job security, year-round work enables farmworkers to maintain a stable family life, with benefits for their children and communities. As a worker explained, “For those of us who have family here, we prefer stable, year-round work to contract work. We earn more in a year doing hourly work. If you don’t have a family it’s OK, but those of us with families prefer stable year-round work.” Of the twelve farms surveyed, all but three maintain a year-round workforce. At least five had intentionally developed year-round intensive cropping systems as a means of providing farmworkers with year-round employment.

In addition to the benefits for workers, families and their communities, a permanent workforce is also good for business. With increasing labor shortages, the growers in our sample have access to a steady supply of labor. High retention rates keep recruitment and training costs low, while year-round production increases grower revenue. Delivering high quality products year-round also enables farmers to...
retain market share among wholesalers who prefer dealing with year-round suppliers.

♦ **Year-Round Employment Strategies:** A highly diversified 75 acre farm in the Central Valley produces a range of winter crops to provide year-round employment for 40 full-time workers. A Ventura county farm plants 40 crops on 30 acres, 4 times a year, creating year-round work for 10-12 people and seasonal work for an additional 15. Another farm produces dried flowers and wreathes in the winter, and hires farm-workers for jobs such as painting and carpentry in the winter. A vineyard contracts with a neighboring olive grove to provide employment during December and January, when there is no work at the vineyard.

**Traditional Benefits**

“*Housing has been a huge issue. It’s a commitment of ours to help folks find housing. When anything is available, we snap it up. We sign a lease. We make sure the rent gets paid, even when there aren’t workers there.*”

*Capay Valley farmer*

The growers on the farms in our sample offer a broad range of traditional benefits, including health insurance, retirement plans, paid time off and free or subsidized housing. Health insurance is offered by nine of the twelve farms in our sample. Eight of the farms in our sample provide workers with some form of paid time off, including vacations and public holidays. Half of the farms in our sample offer retirement plans – in many cases even for seasonal workers – with employer matches of between three and five percent. Five farms provide free or subsidized housing, and all offer flexible scheduling, allowing employees to time off to take care of personal and family needs.

♦ **Health Insurance:** A vineyard management company covers 100% of medical, dental, vision and life insurance benefits for workers and families after an employee has worked 120 hours. A mid-sized Central Coast farm provides health and dental insurance coverage for all employees and family members after 6 months.

♦ **Holiday Pay:** Two corporate farms offer 6 paid holidays to seasonal and year-round employees, and two smaller diversified farms offer 5 paid holidays.

♦ **Vacation Pay:** One Central Coast farm offers paid vacation to all employees working until the end of the season: 5 days during year 1, 2 weeks after 3 years; and 18 days after 6 years. A mid-sized Central Valley farm offers one week vacation pay – or 50 hours paid out –after 2 years, which increases to 2 weeks – or 100 hours paid out – after 3 years.

♦ **Retirement Plans:** A vineyard provides a 100% match for permanent employee contributions up to 5% of their wages. A corporate farm contributes 3% of wages for all permanent and seasonal workers, whether or not they contribute. It matches an additional 2% for employees that contribute.

♦ **Housing:** A mid-sized farm offers low cost housing for all interested employees. A corporate farm has donated 10 acres of land and is collaborating with a non profit housing developer to build a mixed-use housing development with a health and child care center.

♦ **Bereavement Pay:** Two corporate farms offer 3 days paid bereavement leave.

♦ **Life Insurance:** One corporate farm offers life insurance; it recently doubled the amount of the benefit to cover transporting bodies back to Mexico.

♦ **Access to Benefits:** A vineyard and winery offers all permanent workers the identical benefits package as the president of the company.
Non-Traditional Benefits

“You can bring all the food home that you want. We are eating a lot of vegetables. We all have more to eat.”

Central Coast farmworker

All of the farms in our sample offer a broad range of less traditional benefits. Of those, the most highly valued by employees are personal loans and access to food from the farm.

♦ Personal Loans: Four farms offer no-interest loans of $500 to $2,000, which are paid back through payroll deductions. Two other farms offer loans through retirement plans.

♦ Business Loans: A farm in the Capay Valley helped several of its farmworkers purchase a neighboring farm, which is now a successful CSA.

♦ Food From the Farm: Eight farms encourage workers to take home food grown on the farm on a regular basis. One farmer brings coffee and pastries to his workers each morning.

♦ Assistance with Social Services: A mid-sized Capay Valley farm helped employees start an Alcoholics Anonymous group, and paid for alcohol rehabilitation treatment for an employee. A corporate farm helped build and support a childcare center for its workers’ children. Another farm allows social services agencies to conduct outreach on the farm, and pays workers for time spent attending those sessions.

♦ Tuition Assistance and Scholarship Program: This large Central Coast corporate farm offers up to $2,000 for work-related higher education for all employees, and $500-1,000 per child per year for college.

Labor Relations, Communication and Decision Making

“There you speak up if you have an issue or concern. For example, I told the foreman that I don’t want to have to bring tools to work each day; that they should be on site. I would never have said that on another farm. You could get fired for that.”

Central Coast farmworker

“Before, I worked with a contractor and I was treated badly. Here there are policies. No one says anything in a mean way. They say ‘please.’ That means a lot. When you are happier you work more.”

Central Coast farmworker

There are a range of practices that foster good communications between employers and employees. Some of these, such as safety meetings, employee orientations and employee handbooks are focused on communicating information and expectations, while others, such as regular meetings and grievance procedures, create space for worker representation and participation in decision-making processes. On most farms, there was a high level of communication and input from the team leaders and senior farm managers, but few formal mechanisms for information sharing and feedback from between supervisors and field staff.

Five farms hold regular daily, weekly or monthly meetings with employees. Three use those meetings to solicit employee feedback and discuss non-production issues such as personnel conflicts, benefits information, marketing and business operations. While workers expressed a general appreciation for practices such as formal communication mechanisms and employee manuals, these were not identified as areas of high importance.

Despite the lack of formal policies, many growers actively solicit or are open to unsolicited feedback from farmworkers. Farmers reported that worker input helped them improve farm operations and avoid costly mistakes. The opportunity to provide input also contributes to farmworkers’ feelings about being an integral part of the farm, which increases their motivation and productivity. As a
farmworker explained, “Here we have meetings from time to time, and the patrón informs us about what is happening on the farm. He takes us into account. He asks our opinion about things.” In contrast, farmworkers on one farm did not feel taken into account, which clearly made them feel less motivated. As they explained, “Here there is no opportunity to say anything. Our opinions don’t matter…the patrón decides everything.”

♦ **Formalized Policies and Employee Manuals:** Three farms have formalized policies, which are codified in bilingual English-Spanish employee handbooks.4

♦ **Grievance Procedures:** A corporate farm’s policy is for employees to first raise concerns with direct supervisors. If concerns are not adequately resolved they may go to their manager’s supervisor, and from there to the head of Human Resources, or directly to the farm’s president.

♦ **Worker Input:** This mid-sized farm holds weekly meetings, where staff can provide input regarding production issues and voice concerns about pay, personnel conflicts, etc. Another farm conducted in-person interviews with all 40 employees, soliciting feedback about housing needs, ideas for improving farm management, etc.

♦ **Information Sharing:** This vineyard holds an annual meeting for its business partners, investors and employees. All permanent and seasonal employees are paid to attend the meeting, where a Spanish interpreter is provided.

♦ **Formal Surveys:** A corporate farm has conducted several surveys measuring employee satisfaction and soliciting worker input on issues such as housing and preferences for different benefits packages.

♦ **Formal Orientation:** Three farms have formal, paid orientations, and employ Spanish-speaking human resource staff, who also provide assistance with social service referrals and legal issues, etc.

♦ **Collective Bargaining:** One farm on the Central Coastal has a contract with the United Farm Workers, and has recognized collective bargaining as the vehicle for farmworker representation in wages and benefit negotiations.

♦ **Communication:** This Capay Valley farm has a strictly enforced “no yelling” policy for supervisors.

**Recruitment and Hiring**

**Farm Labor Contractors**

“Farm Labor Contractors (FLCs) have no loyalty to the farm. They have no attachment to your business. A farmer working under the FLC system can’t really be good to his workers. He may pay a better wage, but the FLC may pocket that. The farmer loses control over the work practices. You can have abuses going on but you don’t have to be responsible for them. It’s a good way to protect yourself from liability, but it is negative in most regards.”

Central Valley farmer

Approximately 50% of California farms utilize the services of farm labor contractors (FLCs), who are notorious for low wages, poor treatment of workers, and fast, yet often poor quality work. In order to ensure good worker treatment and higher quality production, the farms in our sample prefer to hire directly. Nonetheless, fully half of those farms contract with FLCs when they require a large crew for a short period of time. In most of these cases, however, farmers take precautions to prevent abuses and ensure higher pay for workers.

This nut farm in the Central Valley negotiates above minimum wage rates for workers employed by farm labor contractors, provides safety and quality training to FLC workers, uses its own supervisors to ensure high quality work and safe, respectful conditions and requests the same FLC crew each year to ensure higher quality work.
Health and Safety Issues

“The highest and most important product of the farm is the worker’s health, safety and happiness.”

Central Valley farmer

“Here we do handweeding, but it is one to two hours maximum, and isn’t too difficult. I think it’s better to weed with hands than to use chemicals. If someone has a hurt back, he can ask for a different job.”

Central Valley farmworker

Improved health and safety are additional benefits offered by many of the farms in our sample. In addition to providing legally required trainings, many growers in our sample reiterate safety messages to employees and structure work in order to reduce accidents and worker compensation costs. Staff are often told to work at a slower pace and handweeding is limited to a few hours a day. As one farmer said, “On most farms, they tell people to work faster. We say the opposite. People are told to slow down. Quality comes first.”

Many workers cited lack of exposure to synthetic pesticides as an important and much appreciated benefit of working on organic farms. As one commented, “I like working here because there are no chemicals. On many farms where my friends work they have a lot of health problems. This is clean work.” Many also noted a reduced incidence of musculoskeletal injuries, because they are allowed, and in fact encouraged to carry heavy items with coworkers, a practice that stands in sharp contrast with their experiences on other farms. While all workers appreciate this, that is especially true for women. As a female farmworker noted, “I like the fact that we always have help and support from our compañeros, especially in helping us lift heavy boxes. On other farms it isn’t like that.”

Workers on the farms in our sample also reported access to prompt and adequate medical attention in the case of serious injuries, often not the case on many farms. Equally important, they reported being able to take the necessary time off to recover from accidents and illnesses without fear of losing their jobs, or engage in “light duty” following accidents or injuries, which they appreciate immensely.

♦ Handweeding Limitations: Two farms explicitly limit hand weeding to two hours a day.

♦ Safety Incentives: Three farms have incorporated explicit safety incentives into their annual bonus programs. A corporate farm conducts quarterly raffles for workers with a perfect safety record and an annual raffle for workers who have remained accident free during the entire year, with a grand prize of $14,000 toward the purchase of a vehicle, $8,000 towards a mortgage or home remodeling, and numerous other high value prizes. 5

♦ Safety Conditions: This stone fruit farm in the Central Valley lowered the height of trees to reduce falls from ladders. Another farm has monthly safety meetings. Virtually all farms encourage workers to share heavy loads.

What Workers Most Appreciate

Attempts to rank workplace benefits are difficult, if not impossible, since ultimately, all benefits are important. Nonetheless, the following is a rough prioritization of benefits and conditions most appreciated by farmworkers, based on the frequency, order and enthusiasm of responses to that question:

♦ Respectful treatment
♦ Slower pace of work
♦ Fair compensation
♦ Year-round employment
♦ Health insurance
♦ Personal loans
♦ Food from the farm
♦ Paid holidays and vacation
♦ Flexible work schedule
♦ Healthy and safe work environment
♦ Housing
♦ Opportunities for advancement, training and professional development
♦ Diversity of tasks
♦ Involvement in decision-making processes
♦ Clear and effective grievance procedures
Management Structures

"I really like working with the team that I'm working in. Everyone cares about each other. It is a team effort. We are all together. Everyone helps train you and shows you how to do things if you don't know how."

Capay Valley farmworker

One of the defining characteristics of the farms in our sample is a significantly more democratic, team-based approach to management and supervision than the hierarchical management structures found on many farms. Virtually all of the growers in our sample work alongside farmworkers to some degree, and have direct communication with them on a daily basis. All speak some Spanish, as well, which facilitates direct communication. Direct contact also allows farmers to get to know their workers personally, and to identify particularly motivated employees or those with special skills.

Personal relationships with growers also increase farmworkers’ sense of investment in and commitment to the farm. More importantly, perhaps, they help avoid abuses that are commonly associated with foremen. As a farmworker explained, “In other places, you never speak to or see the owner, only the mayordomo [foreman]. If the mayordomo doesn’t like you, they can tell the patrón to fire you. Here if there is a problem, you can talk directly with the farmer.” Similarly, as a grower explains, “Most employers don’t speak the language, so they employ someone who can communicate for them. That person holds a lot of power. It’s a system ripe for abuse.”

The farms in our sample also rely on “team leaders,” who provide guidance but work alongside farmworkers, rather than traditional foremen, that stand over them and “crack the whip.” The farmworkers in our sample appreciate the absence of foremen tremendously, given the harsh treatment and exploitative behavior that is often associated with that position. “In some places, there are more supervisors than there are people working. We feel pressured. Here we do the best we can without pressure.” At the same time, the absence of foremen also results in significant cost-savings for growers.

Diversity of Tasks

“There is a variety of work here. In one day, we do different tasks; picking, packing and other things. On other farms you do the same thing all day, ten hours a day.”

Capay Valley farmworker

Most of the farms in our sample produce ten or more crops, with over a third growing at least 50 different crops. This diversity leads to a greater variety of tasks for workers, who appreciate the ability to switch tasks several times a day. In addition to relieving the monotony and tedium that are often associated with production agriculture, this helps reduce health problems associated with stoop labor and repetitive stress. The diversity of tasks also creates opportunities for on-going learning, which contributes to job satisfaction. As a farmworker explained, “It’s not boring on the farm. Sometimes I have five or six tasks in a day. There are so many different tasks here that you learn about many aspects of the farm. The work changes all the time and time goes by more quickly.”

Opportunities for Professional Development and Advancement

“We learn many things that we haven’t done before. There are so many different vegetables. My compañeros teach me. In other places they don’t take the time to teach you.”

Central Coast farmworker

Most of the growers in our sample have proactively provided workers with opportunities for skills acquisition and advancement in their jobs, by promoting those with leadership or other skills to managerial or technical positions. While this strategy seems to work well in terms of promoting farmworkers to new skill categories, such as irrigation or driving a tractor, it has met with less success in terms of promotions to supervisory positions, given high levels of reluctance among farmworkers to supervise friends or family members. A large farm in our sample has attempted to address that issue by placing promoted farmworkers at sites away from friends and family. While that strategy has
been relatively successful, it is clearly not an option for most small and medium sized farms.

**Opportunities for Older Workers**

One of the outstanding characteristics of the farms in our sample is treatment of older workers. High employee retention rates have resulted in an aging workforce on many of the farms in our sample, which – given the physically demanding requirements of production agriculture – can ultimately represent a liability for employers. Nonetheless, virtually all of the growers in our sample have made a conscious decision to keep older workers on, and have sought appropriate tasks for them, rather than letting them go, as on many farms. Nonetheless, an aging workforce represents a conundrum for growers, as it will inevitably result in decreased productivity. While all the growers in our sample expressed concerns in that regard, none have come up with ways to successfully address this complex issue.

**Areas for Improvement**

One of the more sobering aspects of this research is the realization that even among these more exemplary farms, there is still much room for improvement. Some of the more profitable growers are still not able to offer a living wage, paid sick days, health insurance and year-round employment, while few are able to provide seasonal workers with the same benefits as permanent staff. Labor management on most of the farms is highly informal, with few clear rules, procedures and policies. Notably, the larger corporate farms in our study are the exception to this. Given higher revenues, these larger farms also tend to provide more comprehensive benefits. The following are some of the key areas for improvement:

- Increased opportunities for worker representation and input, through regular meetings where workers can express concerns, and regular forums for disseminating information;
- Codification of existing practices, including grievance procedures, benefits, profit-sharing plans, etc. into formal policies that are explained to employees verbally and in a Spanish language employee manual;
- More formalized systems for calculating profit-sharing, and increased transparency regarding farm level finances;
- Provision of more equitable benefits for temporary and seasonal workers;
- Formal orientations for all new employees regarding issues such as benefits, job expectations, workplace practices, grievance procedures and other policies;
- Increased incentive programs promoting employee health and safety.

**Good Labor Conditions: A Win-Win for Farmers and Farmworkers**

“Workers want two things: respect and fair compensation. When you give them that it leads to higher quality work and higher quality produce.”

*Central Coast farmer*

As is the case with other socially responsible businesses, the growers in our survey are “doing well by doing good.” Although primarily motivated by social justice concerns and a desire to “do the right thing,” virtually all report numerous economic and other benefits of providing good farm labor conditions. A satisfied, motivated, skilled and knowledgeable workforce has resulted in increased retention rates, reduced recruitment, training and supervision costs; higher quality products and ultimately, higher revenues and profits.

Many of the farms in our sample obtain price premiums by delivering high quality produce, which is dependent on a committed workforce. As a farmer operating a Community-Supported Agriculture operation explained, “When people open our boxes, we want them to appreciate that hands that really cared touched the food. To do that, we need workers who are trained and motivated.” Because many aspects of agricultural production require a skilled and knowledgeable workforce, growers place a high value on employee retention. That is particularly true on highly diversified farms, where it can take a long time for farmworkers to become familiar with the production requirements of dozens of different crops.
Some farmers may ask which conditions and benefits have the greatest impact on worker satisfaction, motivation, retention and loyalty. In our research, respectful treatment, year-round employment and profit-sharing emerged as most important. As a farmworker explained, “we come back here because of the way people are treated, even though the money is a little less.” To the extent that keeping good workers is a goal, year-round employment is perhaps the single most important retention strategy. As a farmer explained, “year-round workers who have been here for a long time see the impacts of their work, they see the benefits, and that makes them motivated to work harder.” In order to build and maintain that loyalty and motivation, workers also need to feel rewarded for these contributions.

While verbal expressions of appreciation are important, a monetary reward at the end of a hard season is key. Profit-sharing was cited by most farmers as a tremendous motivating force, “We do it because it is the right thing to do. They work hard and they deserve it. I also think it has a huge impact on morale, productivity and retention. I don’t think they would want to work here if they didn’t get their bonus.” The beauty of profit-sharing is that it enables farmers to supplement wages in good years while keeping labor costs down during bad years, a virtual risk free strategy that is a win win for farmers and workers.

Many farmers, including the more successful ones, expressed how difficult it is to increase wages and other benefits given extremely low or non existent profit margins. Without ignoring the importance of improving compensation policies, farmers should keep in mind that there are many low cost, simple, yet highly effective ways of increasing worker satisfaction.

### Social Certification and Domestic Fair Trade: New Market Opportunities for Farmers

With Fair Trade leading the way, more and more market based opportunities are emerging for farmers who meet social as well as environmental standards. Given the economic challenges reported by farmers for improving compensation and benefits, market opportunities created by these programs could provide needed incentives and rewards for producers to improve conditions for their workers.

Social certification has been growing most rapidly internationally and in Europe over the past several years. IFOAM’s initiative to integrate social standards into organic standards and SASA’s effort to develop guidelines and increase cooperation among different certification initiatives in sustainable agriculture are two critical international efforts in this area. Domestically, the Food Alliance is the principal program certifying adherence to both social and environmental standards among growers. Unlike Fair Trade, none of these certification schemes explicitly mandate fair prices for farmers. Participation in these schemes has, however, helped farmers access new market opportunities.

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**Low, Medium and High Cost Practices**

**Low Cost Practices:**
- Respectful treatment
- Regular acknowledgement and appreciation
- Free food from the farm
- Personal loans
- Policies and mechanisms for communication and information sharing
- Clear grievance procedures
- Flexible work schedules
- Safe and healthy work environment
- Diverse tasks
- Opportunities for training, skill acquisition and professional advancement
- Surveys and other feedback mechanisms
- Assistance with social services
- Celebrations, team-building and appreciation parties

**Medium Cost Practices:**
- Bonuses and profit-sharing
- Year-round employment
- Paid time off
- Retirement plans
- Educational assistance

**High Cost Practices:**
- Higher wages
- Health insurance
In California, new market opportunities are emerging for farmers that meet higher levels of social and environmental responsibility among institutional markets such as universities, hospitals, and business campuses. In order to meet this growing demand, Food Alliance has plans to enter the California market in the next year. While new markets for producers are an important benefit, the key challenge with all these programs will be to secure higher prices for producers as a means of helping to pay the costs associated with the transition to better environmental and social management practices on the farm.

Fair Trade is one of the few established certification programs that addresses the issue of fair prices for producers and transparency and equity all along the supply chain. With urgency to address the need for higher producer prices domestically, many groups around the world are actively working to develop domestic Fair Trade certification schemes. In the US, several initiatives are underway. A multiyear process led by the Rural Advancement Foundation International (RAFI) and Committee to Support Workers (CATA) to develop North American social justice standards for agriculture is one of the more comprehensive US efforts to date. At least half a dozen other schemes are in process, including the Minnesota Local Fair Trade group, Ag in the Middle, and Wisconsin Fair Trade cheese initiative. These, and other incipient efforts and interested organizations are coming together under the banner of a Domestic Fair Trade Working group that is bringing organized by Organic Valley, a farmer owned cooperative dairy company that has been applying fair trade principles in its business practices since its inception in 1988.

Over the past several years, some organic farmers and advocate groups have expressed interest in developing beyond organic certification schemes to enable truly sustainable farmers to further differentiate themselves in the marketplace. While the US organic community has mostly rejected the idea of integrating social issues into organic certification, it is just a matter of time before a program is developed specifically to certify social, as well as other sustainability criteria among organic farmers and farmers in transition.

**Conclusion**

The findings from this research provide a window into the different ways that sustainable growers in California are currently working to provide socially sustainable farm labor conditions. The findings are hopeful, in that they demonstrate that it is possible to offer good labor conditions, while maintaining an economically viable farm operation. At the same time, they are sobering, in that there is considerable room for improvement, even on the most progressive farms. Tellingly, while the farmworkers we met with were generally happy with the conditions on these farms, virtually none hoped their children would themselves become farmworkers.

While the high cost of benefits, such as health insurance, may make those practices prohibitive for some growers, the research identifies numerous no- and low-cost means of offering positive farm labor conditions. By documenting those conditions, and the value placed on them by farmworkers, we hope to encourage more growers to adopt similar practices.

In addition to being “the right thing to do,” the practices identified by this research have resulted in numerous benefits for growers, who are “doing well by doing good.” With growing interest in domestic fair trade and an increase in certification schemes stressing social and environmental standards, the adoption of positive labor practices offers growers the opportunity access to niche markets offering price premiums. It is essential that sustainable growers be provided with access to the tools and information that will allow them to meet these emerging market demands.

More active engagement is therefore needed by grower, extension and other technical assistance organizations to provide this kind of support to growers. More resources must also be forthcoming from sustainable agriculture funders and others concerned with long term stability, health and well being of agricultural communities.

Other strategies are needed to improve labor practices, including the formalization of these “best practices” – through employee manuals or other mechanisms – to make them less dependent on the goodwill of individual growers. While
immigration reform and the role of farm labor contractors were beyond the scope of this work, these are critical issues that must be addressed as well.

At the same time, attempts to encourage improved labor practices must be accompanied by public policy and market-based mechanisms ensuring greater price equity for growers. As Paul Muller, co-founder of Full Belly Farm notes, ‘Everyone in the food chain needs to adopt a sense of fairness and responsibility for the well being of farm laborers. It needs to be a partnership through the whole agriculture system, with wholesalers and consumers paying fair prices that then assure that farm workers are adequately compensated in an equitable way. The equation of greater social responsibility needs to be integrated though the whole food system (cited in Kapfer 2004). More work is needed to educate and mobilize all levels of the supply chain to increase their willingness to pay a price that reflects the true costs of socially just production. Ultimately, we must seek creative mechanisms to promote a food system that is socially equitable for growers, farmworkers and consumers.’

1 While the social dimensions of sustainable agriculture affect growers, farmworkers and consumers, this research focuses on farmworkers, who with low wages, harsh working conditions, precarious housing and tenuous legal status, have fared particularly poorly within the context of the U.S. food system.

2 Nine of the farms are certified organic, two are mixed conventional and organic, and one uses low-input sustainable agriculture practices. Of these, four are medium sized diversified farms, producing a large range of fruits and vegetables, two are vineyards (including a vineyard management company); and six produce a smaller range of crops, including berries, stone fruits, nuts, herbs, and salad greens. Eight are family run medium-sized operations, with fewer than 70 employees and annual revenues between $600,000 and $2.5 million. Four are larger, with a more corporate structure, and labor forces ranging from 80 to 4,000 employees, with revenues from $10 million upwards.

3 Definition of living wage adopted by Living Wage Summit, July 1998, Berkeley, CA: “A living wage is the net wage earned during a country’s legal maximum work week, but not more than 48 hours, that provides for the needs of an average family unit (nutrition, clothing, health care, education, potable water, child care, transportation, housing, and energy) plus savings (10 percent of income).”

4 At the same time, a number of farms recognized the importance of employee manuals and some were in the process developing them. Others cited a strong interest in doing so but indicated a lack of time and resources.

5 That practice is, however, somewhat controversial, as it effectively penalizes workers injured through no fault of their own.

6 In the US Fair Trade Certified coffee grew by an astounding 93 percent in 2003 and 76 percent in 2004.


8 One of the more advanced domestic fair trade schemes is the British Soil Associations’ Ethical Trade Initiative which was launched as a pilot certification scheme for UK produced organic products in 2001. Implementation of a full (voluntary) domestic ethical trading certification program is planned for 2006.

We are grateful for the support of the many individuals and organizations that helped us in this effort, including the Columbia Foundation and the Ramsay-Merriam Fund, which provided generous support for this project; the growers that invited us to their farms and shared information on their labor practices; the farmworkers who agreed to meet with us and share their experiences working on these farms; the many individuals who contributed invaluable advice and information that helped shape and inform this work; and the many colleagues that provided important insights and information through key informant interviews. Thank you all! A more detailed version of this study is available at www.cirsinc.org

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12 — California Institute for Rural Studies
Lesson 3.8: Food Safety for Producers in Direct Marketing Venues

Estimated time: One hour.

Overview

Lesson 3.8 is a short course on food safety responsibilities in direct marketing to consumers. The focus is strengthening your understanding of risk minimizing principles and practices. At the end of this lesson, you will know sources of contamination and preventative practices.

Objectives

1. Identify control points for producers’ food safety issues.
2. Introduce preventative and combative measures of minimizing microbial contamination risk.
3. Learn benefits and limitations of food safety control measures.

Assessment

Throughout the lesson, handouts relevant to subject matter will be introduced and studied. Although there are no homework assignments, suggested further reading sources are provided as continued instruction outside of the period.

Equipment, Supplies, and Materials

1. Power Point presentation Lesson 3.8
2. Handout “Reduce microbial contamination with good agricultural practices”
3. Handout “Handwashing and Drying Procedures”
4. Handout “Bacteria Control Chart”

References

2. Electronic Code of Federal Regulations: Title 7 Agriculture: Part 205 National Organic Program. Accessed on Sept. 2, 2009. http://ecfr.gpoaccess.gov/cgi/t/text/text-idx?type=simple;c=ecfr;cc=ecfr;sid=4163ddc3518c1ffdc539675aed8efe33;region=DIV1;q1=national%20organic%20program;rgn=div5;view=text;idno=7;node=7%3A3.1.1.9.31
References Continued


Classroom Procedures

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| Lead discussion to assess previous knowledge, and then begin power point presentation. | • What preventative food safety measures do you have in place?  
• What are some hazards at your farm/ packing facility? |
| Slide 5: GAPs and GHPs. The GAP guidelines are extensive and could cover a whole hour period or longer. They are important to all producers and required by some outlets. Direct the students to further reading documents about guidelines and self-auditing before an FSIS audit. | • GAP guidelines – “Guide to minimize microbial food safety hazards for fresh fruits and vegetables.”  
• GAP certification is achieved through an FSIS audit  
• Self-audit before FSIS – “Good agricultural practices: A self-audit for growers and handlers.” |
| Slide 6: Have students contemplate their operations and what they think are their riskiest areas. | • What are your areas of most concern in your operation?  
• What preventative measures can you take to minimize risk? |
## Classroom Procedures Continued

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<td>Slide 7: Water testing</td>
<td>• In Arkansas, ____ will test your water. Contact info.</td>
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| Slide 8: Combating contamination with mechanical methods post-harvest | • Variation between physical characteristics of produce may affect the methods of cleaning them, and may also affect how effective practices are in reducing contamination.  
• For example, practices for washing watermelons (smooth surface) will be different from those of cantaloupes (rough surface), and the ability to reduce contamination on the watermelon may be greater. |
| Slide 10: Source of additional information on chlorination | • Chlorine's role in the packing facility’s water is the source –“Chlorination in the production and postharvest handling of fresh fruits and vegetables.”  
• Chlorinated water is only allowed in organic production at levels allowed by the “Safe Drinking Water Act.” |
| Slide 11: Compost vs. Manure | • First choice is compost – minimal contamination risk  
• If raw manure must be used, maximize time between application an harvest – this means months to years  
• Unavoidable manure contamination from wildlife – principles are still important if you don’t intentionally incorporate manure |
| Slide 12: Why? | • Some pathogens can live in the soil for months to years. Raw manure is especially risky for produce that is consumed fresh or organic produce that is treated with minimal chemicals. |
| Slide 13: End of soil, water and manure section – introduce handout “Reduce microbial contamination with good agricultural practices” and then direct students to sources of additional information | • Further reading – “Microbial food safety is your responsibility” details some of the most common pathogens associated with produce production, including their sources and effects on humans.  
• Further reading – “Key points of control and management of microbial food safety: Information for growers, packers, and handlers of fresh-consumed horticultural products” |
Classroom Procedures Continued

<table>
<thead>
<tr>
<th>Teaching Procedures</th>
<th>Content</th>
</tr>
</thead>
<tbody>
<tr>
<td>Handout “Reduce microbial contamination with good agricultural practices”</td>
<td>• Give students a few moments to review the checklist</td>
</tr>
<tr>
<td></td>
<td>• Answer questions</td>
</tr>
<tr>
<td>Slide 15: Handout “Handwashing and Drying Procedures”</td>
<td>• Handout supplements slide.</td>
</tr>
<tr>
<td>Slide 18: Handout “Bacteria Control Chart”</td>
<td>• Note thermometer areas “room temperature” and “refrigeration” as well as the maximum time it should take to cool products down.</td>
</tr>
<tr>
<td>Slide 21: Refer again to handout “Bacteria Control Chart”</td>
<td>• Note thermometer areas at boiling (212°F) – botulism toxin inactivated but staphylococcus toxin is not</td>
</tr>
<tr>
<td>Slide 22: Refer again to handout “Bacteria Control Chart” and direct students to additional sources of information</td>
<td>• Note thermometer areas for both refrigeration and freezing for safe food transport to, from, and during the farmers’ market</td>
</tr>
<tr>
<td></td>
<td>• Further reading – “Storing fresh fruits and vegetables”</td>
</tr>
<tr>
<td>End of lesson: Remember to ask for questions.</td>
<td>• Discuss any questions.</td>
</tr>
<tr>
<td></td>
<td>• Remind students of sources of additional information.</td>
</tr>
</tbody>
</table>

Sources of Additional Information

Sources of Additional Information Continued


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Overview

- Lesson 3.8 is a short course on your food safety responsibilities as a producer participating in direct marketing to consumers
- Its focus is strengthening your understanding of risk minimizing principles and practices
- At the end of this lesson, you will know sources of contamination, preventative practices, and why minimizing your risk is important to both your business and your customers

Objectives

1. Identify control points for producers’ food safety issues
2. Introduce preventative and combative measures of minimizing microbial contamination risk
3. Learn benefits and limitations of food safety control measures
Preventative Measures in Direct Markets

- Preventative practices are both more effective and less expensive to implement than fixing a contamination issue
- Some contamination issues are irreversible
- Safe handling practices will keep your customers coming back and recommending you to others
- Direct marketing eliminates many distribution steps that can increase the risk of contamination along the chain of handling products
- Direct marketing results in a greater burden on the farmer to adequately protect their consumers from food borne illnesses

GAPs and GHPs

- Good agricultural practices and good handling practices
  - Suggested guidelines set forth by the FDA to minimize microbial contamination of food from farm and transportation.
  - Minimize the risk of pathogenic contamination of your products
  - Protect your consumers
  - Promote your business
- Although not legally binding, some outlets require suppliers to have GAP certification through FSIS.

Potential Sources of On-Farm Contamination

- Soil
- Irrigation water
- Animal manure
- Inadequately composted manure
- Wild and domestic animals
- Inadequate field worker hygiene
- Harvesting equipment
- Transport containers
- Wash and rinse water
- Unsanitary handling of produce
- Soaking, packing, or cutting equipment
- Ice
- Cooling units (hydrocoolers)
- Transport vehicles
- Improper storage temperatures
- Improper packaging
- Cross contamination
Pre-Planting Study

- Ensure that the land is suitable for cultivation and will not be subject to runoff contamination from:
  - Agriculture
  - Industry
  - Other sources
- Conduct regular intervals of water testing

Treat All Products As If They Will Be Consumed Raw

- Be aware of potential risks: identify and establish management practices to minimize the chance of external and internal contamination at every step
- Natural barriers (inedible skins) guard against microbial contamination
  - Further contamination reduction can be achieved with light to vigorous brushing upon harvest.
- Only harvest good quality produce
  - Wounds or decaying areas are highly likely to be contaminated with bacteria or fungi internally

Remember!

- Clean soil
- Clean water
- Clean hands
- Clean surfaces

- Attention to these components of production will assist in minimizing the risk of the spread of foodborne illness.
- Good record keeping demonstrates your commitment to good agricultural practices and safe food products.
Water Contamination

- Water can be a pathogen vector through irrigation or washing
- Sedimentary or pathogenic contamination of water
  - Surface run-off from irrigation
  - Heavy rains
- Use potable water
  - For foliar applications within two weeks of harvest
  - For all post harvest washing
  - When making ice
- Chlorination of water used during cleaning and packing is very effective in reducing microbial contamination.

Manure and Municipal Biosolids Risk

- Improperly composted or treated manure can contaminate fresh produce
  - Direct contact or splashing on low-growing products
  - Some pathogenic bacteria can survive in soil for months to a year or more
- Safest for application after proper composting
  - The time between application and harvest should still be maximized to minimize risk
- Introduction of manure in your operation can be both intentional and/or unavoidable

Best Management Practices of Applying Compost/Manure Products

- Never apply directly to plants
- Apply either at the end of the season or fall
- Incorporation into the soil is beneficial
- If you must apply in the spring, spread at least two weeks before planting and wait at least 120 days between application and harvest of fresh produce
  - If 120 days is not feasible, such as in short season crops, only apply properly composted manure
- Do not plant root crops or leafy produce in the same year as manure is applied to a field
Wild and Domestic Animals

- Both wild and domestic animals can be a source of fecal contamination in production areas.
  - Do not allow domestic animals entry
  - Deter wildlife
    - Minimize attractants such as cull piles
    - Create physical buffers or barriers

Farm Employees’ Health and Hygiene

- Any worker with illness or injury should be assigned to jobs without produce contact
- Awareness, training, and reinforcement are key
- OSHA regulates requirements for sanitary facilities
- Plans to contain waste spills should be in place to prevent contamination of the field
- Regular proper hand washing, adequate restroom access, and communication/remedy of illness or injury can greatly reduce risk of contamination from field workers

Handwashing Procedures

- The most important risk-minimizing practice
  1. Wet hands with clean, warm water, apply soap, and work up a lather.
  2. Rub hands together for at least 20 seconds (sing the ABC song one time).
  3. Clean under the nails and between the fingers. Rub fingertips of each hand in suds on palm of opposite hand.
  4. Rinse under clean, running water.
  5. Dry hands with a single-use towel.
Pick-Your-Own Considerations

- Provide handwashing facilities to visitors
- Pets at PYO operations
  - Pets should generally not be allowed
  - Some sources argue that pets present a similar risk as humans, and visitors may prefer to bring their pets
  - If you allow pets, insist owners collect waste
- Wash and sanitize containers for produce regularly
- Do not offer produce harvested by customers for resale
- Remind customers of your policies with posted signs
- Customers will appreciate your concern for their safety

Food Contact Surfaces

- No practice can completely eliminate contamination
- Wash and disinfect all surfaces
  - Harvest
  - Packing
  - Transport
- Surfaces should be designed so that injury to produce is minimized and ability to clean and sanitize is maximized
- Educating workers is key to minimizing risk
- Surfaces should be cleaned before and after using them
- A cleaning and sanitizing system should be in place, as well as a documentation procedure for the practices

Post-Harvest Considerations

- Temperature control is very important
  - Refrigeration retards bacterial growth
  - Produce in very high temperatures may spoil much more quickly than under moderate conditions
- The chain of transport from farm to plate should be linear
  - Do not allow washed produce to come into contact with produce or surfaces that have not been washed
  - Do not allow workers to move from “dirty” to “clean” areas
  - If possible, use different physical areas, rooms, etc.
- Separate and label products in transport to establish origin and ensure delivery to various destinations
Farmers' Markets Considerations

- Many types of food available
  - Raw, uncooked, uncleaned foods (corn, potatoes) that need further preparation
  - Ready-to-eat foods (berries, salads, cheese, nuts without shells)
  - Home-canned products (jams, sauces, pickles)
- Home-canned and ready-to-eat products present a greater risk to the consumer than foods that need further preparation

Potentially Hazardous Foods at Farmers’ Markets

- Wash, handle, and store ready-to-eat products properly
  - Wash your hands
  - Use gloves and utensils to prepare
  - Clean and sanitize food contact surfaces
  - Food handlers must not show symptoms of diarrhea, nausea, vomiting, jaundice, lesions containing pus, fever or sore throat

Potentially Hazardous Foods at Farmers’ Markets

- Prepare home-canned products properly
  - Higher risk of contamination with *Clostridium botulinum*, the bacterium that causes botulism
  - Must be prepared in an inspected and certified kitchen
- If a product contains two or more ingredients, label with
  - Ingredients in order of descending weight
  - A name and address of the business/producer and the quantity of the good given in weight, volume, or pieces
Potentially Hazardous Foods at Farmers' Markets

- Keep under proper refrigeration during transport to and from the market and also during market hours:
  - Dairy products
  - Meat, poultry, seafood and eggs
  - Sliced fruits or vegetables
  - Raw sprouts
  - Garlic-in-oil mixtures

References

Chlorination in the production and post harvest handling of fresh fruits and vegetables [link]

Electronic code of federal regulations: Title 7 Agriculture: Part 205 National organic program [link]

Food safety begins on the farm: A grower’s guide: Good agricultural practices for fresh fruits and vegetables [link]

Food safety regulations for farmers’ markets [link]

Key points of control and management of microbial food safety for growers, packers, and handlers of fresh-consumed horticultural products [link]

Lesson template adapted from Cornell University’s GAPS Food Safety Investigation program: [link]

New England extension food safety consortium: Good agricultural practices [link]
References

Microbial food safety is your responsibility.
http://ucce.ucdavis.edu/files/filelibrary/5453/6558.PDF

Reduce microbial contamination with good agricultural practices.

Sources of Additional Information


http://www.fda.gov/Food/FoodSafety/Product-SpecificInformation/default.htm


Sources of Additional Information


http://www.iapub.graph.unl.edu/publication?publicationid=529


http://www.gaps.cornell.edu/Educationalmaterials/Samples/FSBFExpMED.pdf

Section 3-209
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Contamination of food through agricultural practices can be reduced by implementing Good Agricultural Practices. This involves minimizing the risk of microbial contamination on the farm, during transportation, and at the packing house. The following are specific recommendations:

1. **Clean Hands**: Before harvesting or packing and at the end of each day, clean all bins and work surfaces. Sanitize hands using recommended chemicals and water. Always make ice with potable water. Make sure that water used for produce cooling, washing, and processing operations is drinkable (potable). Whenever possible, use chlorinated water. Always make ice with potable water. In exceptional cases, when commercially available sanitizers are not available, use hot water, and single-use towels in the field and in some cases within the packing house.

2. **Clean Water**: Aware that there is no way to guarantee that every drop of water is free of harmful microbial contamination. The risk of contamination can be reduced if preventative steps are taken before produce leaves the farm. There is no way to guarantee that every drop of water is free of harmful microbial contamination. The risk of contamination can be reduced if preventative steps are taken before produce leaves the farm. There is no way to guarantee that every drop of water is free of harmful microbial contamination. The risk of contamination can be reduced if preventative steps are taken before produce leaves the farm.

3. **Clean Surfaces**: It is important to consider the recommendation to sanitize surfaces using recommended chemicals and water. Always make ice with potable water. Make sure that water used for produce cooling, washing, and processing operations is drinkable (potable). Whenever possible, use chlorinated water. Always make ice with potable water.

4. **Reduce Microbial Contamination**: The improper use of manure can be a risk factor contributing to foodborne illness. Pathogens such as *E. coli* 0157:H7, *Salmonella*, and *Campylobacter* can be present in manure slurry and soil for up to 3 months or more, depending on temperature and soil conditions. *Listeria* may survive on vegetables growing in the soil, even though it may not survive in the soil itself. *Yersinia* may survive in soil for up to 330 days. Composting manure, incorporating it prior to planting, and avoiding top-dressing with fresh manure are important steps that can reduce the risk of contamination while making use of this important source of nutrients. Excluding domestic and wild animals as much as possible from production fields will help reduce the risk of manure (fecal) contamination.

**Food Safety Begins On The Farm**

Outbreaks of foodborne illness make news headlines on a regular basis. In the U.S., it is estimated that as many as 76 million people contract some type of foodborne illness each year. As a result, over 325,000 are hospitalized and about 5,000 deaths occur. *Salmonella* on tomatoes and cantaloupes, *E. coli* 0157:H7 on lettuce and in apple juice, hepatitis A on strawberries, and *Cyclospora* on raspberries have shaken consumer confidence in the safety of fruits and vegetables. Since 1987, the number of produce-associated outbreaks has doubled, raising concern among the produce industry, government agencies, and consumers.

From planting to consumption, there are many opportunities for bacteria, viruses, and parasites to contaminate produce. On the farm, soil, manure, water, animals, equipment, and workers may spread harmful organisms. Produce may be harvested on a farm, processed in one plant, repackaged in another, then stored, displayed, or served by an institution or in the home. Each of these steps is an opportunity for harmful microorganisms to enter the food supply.

How much foodborne illness originates on the farm? **No one knows**. Are there reasonable steps that a grower can take to reduce the risk that pathogens will contaminate the food produced on the farm? **Absolutely.**

**Clean Soil**

The improper use of manure can be a risk factor contributing to foodborne illness. Pathogens such as *E. coli* 0157:H7, *Salmonella*, and *Campylobacter* can be present in manure slurry and soil for up to 3 months or more, depending on temperature and soil conditions. *Listeria* may survive on vegetables growing in the soil, even though it may not survive in the soil itself. *Yersinia* may survive in soil for up to 330 days. Composting manure, incorporating it prior to planting, and

**Reduce Microbial Contamination with Good Agricultural Practices**

There is no way to guarantee that everything we grow and consume is free of harmful microbial contamination. The risk can be reduced if preventative steps are taken before produce leaves the farm. This brochure contains detailed suggestions on how you can reduce risks of microbiological contamination on the farm.
Minimize Pathogen Contamination During Production and Harvest of Fresh Produce

Pre-Plant
Select Produce Fields Carefully
- Review land history for prior use and applications of sludge or animal manure.
- Choose fields upstream from animal housings.
- Know upstream uses of surface water and test water quality as needed.
- Prevent runoff or drift from animal operations from entering produce fields.

Store Manure
- Store slurry in continuously loaded systems for 60 days in summer or 90 days in winter prior to field application.
- Consider satellite storage for slurry used on produce fields.
- Compost manure properly to kill pathogens.

Time Applications and Incorporate Manure
- In fall- apply manure to all planned vegetable ground, preferably when soils are warm (>50°F), non-saturated, and cover cropped.
- In spring- incorporate manure two weeks prior to planting.
- Whenever possible, incorporate manure.
- Do NOT harvest produce within 120 days after manure application.
- Keep records of application rates, source, and dates.

Choose Crops Carefully
- Avoid root / leafy crops if manure is applied in spring.
- Plant agronomic or perennials crops where manure is applied in spring.

Production
Do NOT Sidedress with Manure
- ABSOLUTELY DO NOT SIDE-DRESS with fresh or slurry manure or manure ‘tea’ or mulches containing fresh manure.
- OK to side dress with mature composts or compost teas.

Exclude Animals
- NO grazing of livestock near produce fields.
- Minimize wild and domestic animal traffic in produce fields.

Test Irrigation Water Quality
- Identify water source for irrigation.
  - Municipal drinking water—low risk
  - Potable well water- minimal risk if well water is maintained and livestock excluded from active recharge area
  - Surface water-high risk
- Test quarterly or during season (beginning, mid or high draw, and at harvest) if water source passes near livestock or sewage treatment.
- Filter or use settling ponds to improve water quality.
- Use potable water for crop protection sprays.
- Maintain records of water tests.

Select Irrigation Method
- Where feasible, use drip irrigation to reduce crop wetting and minimize risk.
- Apply overhead irrigation early in the day so leaves dry quickly.

Harvest
Clean Harvest Aids
- Check that bins are clean and in good repair.
- High-pressure wash and sanitize bins prior to harvest and clean bins daily during harvest.
- Remove excess soil from bins in field.
- Ensure that packing containers are not overfilled and protect produce adequately from bruising and damage.

Handle Produce Carefully During Harvest
- Avoid standing in bins during harvest to reduce pathogen spread by shoes.
- Minimize bruising of produce during harvest.
- Remove excess soil from produce in the field.

Promote Cleanliness at U-Pick
- Provide clean and convenient restrooms.
- Supply soap, clean water, and single-use towels for hand washing and enforce use.
- Reduce pathogen spread by shoes.

Avoid Dropping Cider
- Do not use decayed or wormy fruit.
- Pasteurize cider.

Promote Worker Hygiene (see “Production”)

Keep Produce Cool
- Cool produce quickly to minimize growth of any potential pathogens.
- Use ice made from potable water.
- Store produce at appropriate temperatures to maintain good quality.

Post-Harvest Handling
Promote Worker Hygiene and Health
- Teach workers about microbial risks and the importance of hygiene.
- Provide clean restrooms with soap, clean water, and single-use towels.
- Post signs in restrooms and enforce hand washing.
- Provide non-food contact jobs for sick employees.

Monitor Wash Water Quality
- Use potable water for all washes.
- Maintain clean water in hop tanks by sanitizing and changing water regularly.
- Chlorinate wash water.
- Monitor chlorine levels.
- Maintain 150 ppm for leafy vegetables and up to 500 ppm for other crops.
- Maintain water pH at 6.0-7.0
- Provide final rinse if using >100 ppm chlorine.
- Avoid tank water temperatures more than 10°F cooler than produce temperature.

Sanitize Packing House
- Clean and sanitize loading, staging, and all food contact surfaces at end of each day.
- Exclude all animals, especially rodents and birds from the packing house.
- No smoking or eating in packing area.

Transportation and Refrigeration
- Check and clean trucks prior to loading.
- Sanitize if animals previously hauled.
- Pre-cool vehicles prior to loading.
- Ensure that refrigeration equipment is working properly.
Handwashing and Drying Procedures
For Food Employees As Required By
410 IAC 7-24, Section 128 and 129

When to Wash Hands

- Before placing gloves on hands
- After touching human body parts
- After using the restroom, coughing, sneezing, blowing your nose, eating, using tobacco, or drinking
- Before and during food preparation, when switching between raw food and ready-to-eat foods or as often as necessary to remove contamination and to prevent cross-contamination
- After engaging in other activities that contaminate the hands (taking out the garbage, wiping counters or tables, handling chemicals, picking up dropped items, etc.)
- After caring for or handling animals

Correct Method to Wash Hands

- Use a designated sink for handwashing
- Wet hands and apply soap
- Rub hands vigorously making sure to wash palms, back of hands, between fingers and forearms for at least 20 seconds in water of at least 100°F. (If available, use a brush to clean under and around the fingernails)
- Rinse hands and forearms thoroughly with running hot water
- Turn off water using a paper towel
- Dry hands with a single-use paper towel or hand drying device
- Do not use a common towel

Food Protection Program
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Section 3-214
Bacteria may not be killed when foods are stored at this temperature.

Poultry, stuffed poultry, stuffed meats or pasta. Stuffing containing meats, cooking in a microwave, and reheating of leftovers must be internally cooked to this temperature.

Ground beef, other ground meat products, injected meats, and eggs not prepared for immediate service.

Maintain heated foods at this temperature.

Foods must be rapidly refrigerated through this entire temperature range to minimize bacterial growth.

Refrigerators kept in this range to reduce food spoilage by bacteria.

Bacteria may not be killed when foods are stored at this temperature.

Rapid bacterial growth at ordinary room temperature.

Rapid bacterial growth.

Moderate bacterial growth.

Two hours

Four hours

Botulism toxin inactivated by boiling

Staphylococcus toxin not inactivated

Ground beef, other ground meat products, injected meats, and eggs not prepared for immediate service.

Eggs, fish, beef & pork.
For more information and to download any of these lessons or the entire curriculum, please visit:

**The Center for Agricultural and Rural Sustainability**
[www.ruralprosperity.net](http://www.ruralprosperity.net)

or

**Manage Your Risk**
[www.manageyourrisk.net](http://www.manageyourrisk.net)