

Braeside Farm: Financial Analysis of a Startup Service Business

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Braeside Farm, founded in October 2008, provides the West Michigan area with a premiere hunter/jumper, dressage training and horse boarding facility designed to meet the needs of beginner through advanced riders. Its mission is to provide a full-service riding and boarding facility, focusing on excellent care of the horse and enjoyment for the rider in a competitive arena. In addition, Braeside hopes to offer horse training and sales programs that help match horses to riders within and beyond its stables. Group adventures for all ages, including organized trail rides and overnight experiences accommodating both horse and rider, are under consideration. The farm's current and prospective services are shown in Table 1.

INTRODUCTION

The West Michigan equine facility market currently caters to two classes of riders: 1) the highly competitive, upper socio-economic class; and 2) the casually competitive, lower socio-economic class. Braeside Farm markets toward the middle to upper middle class riders who have the desire and financial means to compete at all levels, but who would largely focus on regional events. Its services are more comprehensive than the majority of barns in the area, but Braeside Farm sacrifices some of the personalization available at the more elite barns in the area. Braeside is extremely proud of its trainers, who are as qualified as their counterparts at the elite barns and far better known than the trainers at the smaller barns are. It has had the ability to attract top-level junior trainers and the youth who aspire to be serious riders. Simply put, Braeside Farm is the only B level barn in a field of few A and many C level barns.

While other barns tend to focus on one aspect of the horse world, such as showing and competing, Braeside Farm also concentrates on clients who wish to support their primary riders. For example, a child who is interested in competing in weekly horse shows, an adult who would like to learn to ride and/or those who are interested in simply furthering their relationship with their horse.

Braeside Farm's goal is to maintain its current clientele, while capturing the equestrian market that is without a premiere barn in the area. The facility is located directly off a major highway in the Grand Rapids, Michigan metropolitan area with close access to the areas of Rockford, Comstock Park, Wyoming, Sparta and Walker, Cadillac, Kent City, and Muskegon. This area was chosen not only because of its easy-to-access location, but also because it was offering a very healthy value per acre of land and a comparatively low property tax rate.

COMPANY BACKGROUND

The enterprise consists of two limited liability corporations (LLC): Braeside Property LLC and Braeside Farm LLC. The first entity owns the fourteen-acre property, which consists

of a twenty-four stall boarding facility, a covered indoor riding facility, five outdoor paddocks, two outdoor riding arenas, a hay barn and a residence. The residence provides an additional benefit to the business of providing a means for around the clock onsite security for the property. Additionally, since living on the grounds is a requirement of the barn manager position, the market value of the monthly rent is deducted from the manager's salary.

Braeside Farm LLC is the operating side of the business, which pays a monthly rental expense to Braeside Property LLC. Braeside Farm LLC collects the monthly boarding fees, pays operating expenses and maintains the assets. Table 2 presents the original organizational structure for the business. For the first year of operations, the enterprise was owned by two married couples, but as the first year ended, a lack of financial responsibility in meeting partnership obligations led to a legal dissolution of the two LLCs on January 31, 2010. A concern of the partnership breakup decision was that the remaining owners could face immediate repayment on existing loans, according to the business attorney. The lender's justification, due to the fact the original business plan and structure were not in place, would support the right to call the mortgage and line of credit.

PRO FORMA AND ACTUAL FINANCIAL STATEMENTS

Table 3 contains the forecasted profit and loss for the first year of operations. Based on these projections, along with the business plan, a local lender approved a \$140,000 mortgage secured by an interest in the property and a \$25,000 commercial line of credit to the Property LLC. One of the two couples (Owner 1) provided the remaining financing of \$215,000. Actual results for the first year of operations are contained in Tables 4, 5 and 6. Your task is advise the lender to extend or end the bank's loan exposure to Braeside Property. Use the following questions to guide your recommendation.

1. Repayment of the mortgage was based on monthly payments with an annual interest rate of 7.25%, a maturity of twenty years (240 months) and maturity date of five years (60 months). Given the terms, what is the monthly principal and interest (PI) payments?
2. Based on your findings for the first question and what you know about expected income and expenses, what is an appropriate monthly rental payment from Braeside Farm to Braeside Property?
3. Assuming a monthly rental payment of \$2,700, evaluate Braeside Farm's performance to budget for the first twelve months of operations.
4. A major monthly outflow for Braeside Farm is the labor required to feed, water, clean and take to pasture the boarded horses. Based on advice from the CPA, the farm meets the three conditions to deduct the monthly housing rent from the barn manager's wages. Comment on this decision relative to other options the business may have with the residence.
5. As of the end of the first year of operations, the lender could call the loans since the ownership of the LLC had changed. Given this right from a legal perspective, should the bank terminate the lending relationship with the entity? From the owner's perspective, should the business be sold, liquidated or continue in operations?

Table 1
Braeside Farm's Services Provided

<i>Horse Care:</i>
Regulating each horse's feeding needs, supplements, requirements and daily turnout.
Maintaining a routine schedule for each horse's farrier needs, dental and veterinary care.
Maintaining a bi-monthly dewormer program for each horse.
Administering any medications, bandages, or recovery care for each horse as needed.
Handling horses for veterinary, farrier, chiropractic, dentistry or other care.
<i>Boarder Care:</i>
Setting up regular lesson schedules for each boarder and training rides for boarded horses.
Maintaining a regular exercise regiment for each client's horse.
Aid in the purchase and/or selling of a client's horse.
<i>Schooling Horses Program:</i>
Choosing the appropriate horses for the program and maintaining training on the horses.
Maintaining the equipment required for the program.
Arranging lessons accordingly with each trainer.
Maintain any leasing arrangements with any school horse to a client.
<i>On-site Horse Shows:</i>
Setting dates for monthly schooling shows at the facility.
Preparing a class list for each schooling show.
Organizing the boarders and riding school clients for each show.
Prepare arena for each event at the schooling shows.
Hire an appropriate judge for each schooling show.
Inform other trainers of the show dates and supply them with a show bill.

Table 2: Organization Structure

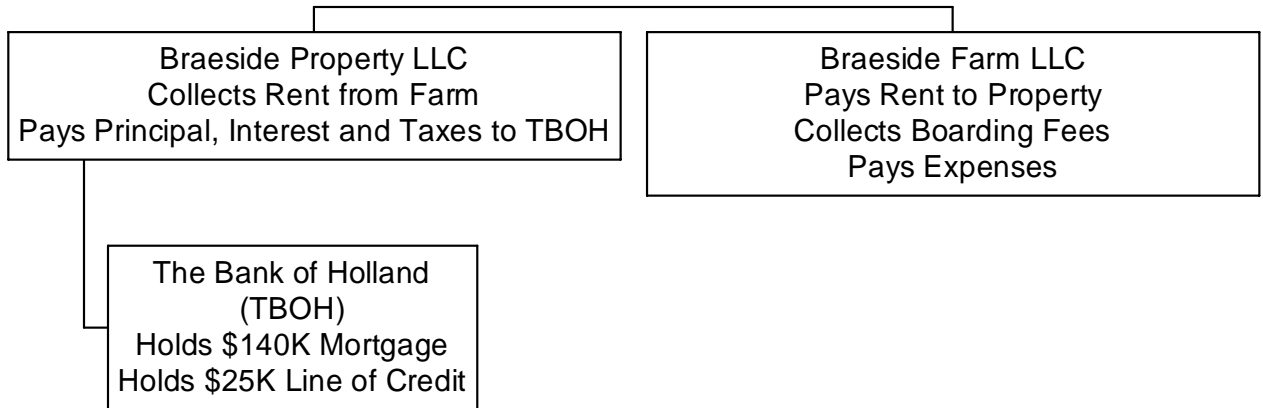


Table 3
Braeside Farm LLC
Budgeted Income v. Expenses
For the Period Ending December 31, 2009

	Q1	Q2	Q3	Q4	2009
<i>Income:</i>					
BF Show	0	1,500	1,500	0	3,000
School Horse Lease	2,640	2,640	2,640	2,640	10,560
Boarding Income	10,680	10,680	13,570	17,205	52,135
Trainer Arena Fees Income	90	90	90	90	360
Camp Income	0	650	1,300	0	1,950
Other Income	400	450	450	450	1,750
Total Income	13,810	16,010	19,550	20,385	69,755
<i>Expense:</i>					
Vehicle Expense	0	0	0	0	0
Advertising and Promotion	0	0	0	0	0
Miscellaneous	0	0	0	0	0
Bank Service Charges	0	0	0	0	0
Contract Labor	1,701	1,701	1,701	1,701	6,804
Farrier	375	375	375	375	1,500
Gasoline, Fuel and Oil	1,050	1,050	1,050	1,050	4,200
Hay & Grain	5,208	5,208	5,968	6,837	23,221
Insurance Expense	750	750	750	750	3,000
Professional Fees	0	0	0	0	0
Rent Expense	8,100	8,100	8,100	8,100	32,400
Repairs and Maintenance	0	0	0	0	0
Shavings	1,500	1,500	1,500	1,500	6,000
Supplies	0	0	0	0	0
Utilities	1,500	1,500	1,500	1,500	6,000
Vet Fees	510	510	510	510	2,040
Total Expense	20,694	20,694	21,454	22,323	85,165
Income less Expenses	(6,884)	(4,684)	(1,904)	(1,938)	(15,410)

Table 4
Braeside Farm LLC
Actual Income v. Expenses
For the Period Ending December 31, 2009

	Q1	Q2	Q3	Q4	2009
<i>Income:</i>					
BF Show	0	309	701	0	1,010
School Horse Lease	0	665	30	0	695
Boarding Income	8,912	9,435	10,983	15,683	45,013
Trainer Arena Fees Income	203	160	225	340	928
Camp Income	380	120	0	0	500
Other Income	0	221	0	20	241
Total Income	9,495	10,910	11,939	16,043	48,386
<i>Expense:</i>					
Vehicle Expense	0	658	367	185	1,210
Advertising and Promotion	638	438	0	0	1,076
Miscellaneous	247	907	109	268	1,531
Bank Service Charges	91	279	502	101	974
Contract Labor	2,619	2,343	3,624	3,212	11,798
Farrier	666	140	650	108	1,564
Gasoline, Fuel and Oil	939	1,371	874	246	3,430
Hay & Grain	3,253	4,792	3,891	5,456	17,392
Insurance Expense	865	1,655	0	1,091	3,611
Professional Fees	3,443	2,374	0	1,124	6,940
Rent Expense	9,165	8,027	8,931	8,708	34,831
Repairs and Maintenance	3,792	2,951	753	506	8,002
Shavings	2,042	2,066	740	810	5,658
Supplies	2,219	1,604	819	549	5,190
Utilities	1,422	1,999	1,323	1,560	6,304
Vet Fees	0	3,248	0	104	3,352
Total Expense	31,400	34,852	22,583	24,028	112,863
Income less Expenses	(21,905)	(23,942)	(10,645)	(7,985)	(64,477)

Table 5
Braeside Farm LLC
Balance Sheet
As of December 31, 20XX

	<i>2009</i>	<i>2008</i>
Current Assets		
Cash - Bank of Holland (BOH)	(165.22)	1,764.06
Accounts Receivable	310.00	2,500.00
Total Current Assets	144.78	4,264.06
Fixed Assets		
Equipment	31,900.16	25,868.16
Furniture & Fixtures	100.00	100.00
Horses	4,950.00	5,300.00
Leasehold Improvements	73,354.42	67,054.42
Accumulated Depreciation	(15,063.93)	(1,660.60)
Total Fixed Assets	95,240.65	96,661.98
Total Assets	95,385.43	100,926.04
Current Liabilities		
Total Credit Cards	22,695.69	9,768.57
Other Current Liabilities		
Vehicle Reimbursement - Owner 1	1,210.00	0.00
School Horse Loan - Owner 1	4,200.00	4,200.00
Advance - Braeside Properties	99,966.37	89,921.37
Advance - Owner 1	14,300.00	0.00
Advance - Owner 2	460.00	0.00
Bridge Loan - Owner 1	16,400.00	0.00
Equipment Loan - BOH	13,949.19	0.00
Line of Credit - BOH	24,877.73	22,500.00
Total Other Current Liabilities	175,363.29	116,621.37
Total Current Liabilities	198,058.98	126,389.94
Long-term Liabilities	0.00	0.00
Total Liabilities	198,058.98	126,389.94
Total Equity	(102,673.55)	(25,463.90)
TOTAL LIABILITIES & EQUITY	95,385.43	100,926.04

Table 6
Braeside Farm LLC
Statement of Cash Flows
For the Period Ending December 31, 2009

<i>Cash Flows From Operating Activities</i>	
Net Income	(77,209.65)
Depreciation	13,403.33
Adjusted Net Income	(63,806.32)
Change in Accounts Receivable	2,190.00
Vehicle Reimbursement - Owner 1	1,210.00
Net cash provided by Operating Activities	(60,406.32)
<i>Cash Flow From Investing Activities</i>	
Equipment	(6,032.00)
Horses	350.00
Leasehold Improvements	(6,300.00)
Net cash provided by Investing Activities	(11,982.00)
<i>Cash Flow From Financing Activities</i>	
Change in Credit Card Balances	12,927.12
Change in Advance - Braeside Properties	10,045.00
Advance - Owner 1	14,300.00
Advance - Owner 2	460.00
Bridge Loan - Owner 1	16,400.00
Equipment Loan - BOH	13,949.19
Change in Line of Credit - BOH	2,377.73
Net cash provided by Financing Activities	70,459.04
Net cash increase for period	(1,929.28)
Cash at beginning of period	1,764.06
Cash at end of period	(165.22)