



United States Department of the Interior

BUREAU OF RECLAMATION
PO Box 25007
Denver, Colorado 80225-0007

IN REPLY REFER TO:

D-5200
LND-9.00

JUN 13 2003

Subject: Application of the Acreage Limitation Provisions to Multi-Ownership Arrangements; Reclamation Reform Act of 1982.

Dear Ladies and Gentlemen:

The purpose of this letter is to provide additional guidance for applying the acreage limitation provisions to certain multi-ownership arrangements that are not specifically addressed by the Reclamation Reform Act of 1982 (RRA) or the Acreage Limitation Rules and Regulations (Regulations; 43 CFR part 426). The information provided in this letter supplements the August 22, 1996, letter (subject: "Application of the Acreage Limitation Provisions to 'Joint Ventures' and 'Holding Partnerships'") that was sent to all districts subject to the acreage limitation provisions.

Entity Classification

What types of multi-ownership arrangements are specifically addressed in the RRA and Regulations?

The RRA and the Regulations address, to varying extents, the following types of multi-ownership arrangements:

- Corporations
- Partnerships
- Tenancies
- Trusts
- Religious organizations
- Charitable organizations
- Public entities
- Indian tribes

How can the classification of a multi-ownership arrangement (hereafter referred to as entity) be determined?

Generally, it can be readily determined if an entity is a tenancy, trust, religious or charitable organization, public entity, etc., by scrutinizing the entity's name. For example, Jones Sisters Partnership would be presumed to be a partnership, while Jones, Inc., would be presumed to be a corporation. Of particular concern however, is how difficult it can sometimes be to determine whether a legal entity should be classified as a corporation or partnership. For example, is a "limited liability company" a corporation or a partnership? This question is answered at the end of this letter.

Why is it important for districts to be able to classify an entity as a corporation or a partnership?

An entity's classification as a corporation versus a partnership can affect the entity's acreage limitation entitlements and the entity's signature requirements when completing RRA forms and irrevocable elections. Details are provided in the "Entity Classification and General Administration of the Acreage Limitation Provisions" section on page 3 of this letter.

What should be done in cases where district staff cannot readily discern whether an entity should be treated like a corporation or a partnership based simply on its name or its ownership arrangement?

In such cases, district staff should contact the appropriate Bureau of Reclamation (Reclamation) office for further guidance.

How will Reclamation apply the acreage limitation provisions to such entities that do not have a clearly defined classification?

For acreage limitation purposes, the entity's classification will be the same classification that is used by the Internal Revenue Service (IRS). For tax purposes, the IRS generally classifies legal entities as either corporations or partnerships. Therefore, if the IRS taxes an entity as a corporation, that entity will be treated as a corporation for acreage limitation purposes. If the IRS taxes an entity as a partnership, that entity will be treated as a partnership for acreage limitation purposes.

Since Reclamation will defer to the IRS when Reclamation cannot identify an entity's classification, how does the IRS determine an entity's classification?

Pursuant to IRS regulations, certain entities are required to be taxed as corporations. Consequently, an entity that is **not** required to be classified as a corporation is generally taxed as a partnership unless the entity makes an election to be taxed as a corporation. An entity that chooses to make such an election does so by submitting a specific IRS form to the IRS and will receive written notification if the election is approved. Once an entity has made such an election, it cannot change its classification for 5 years without IRS approval.

What information will Reclamation use to determine an entity's classification?

Some examples of documents Reclamation will use to determine an entity's classification are:

- Evidence of incorporation (i.e., "articles of incorporation")
- Copies of IRS election approval letters (as described in the previous question-and-answer)
- Copies of IRS tax forms

What happens if an entity disagrees with a classification determination that is made for acreage limitation purposes?

The entity must provide sufficient evidence to demonstrate that it should be classified otherwise. Generally speaking, Reclamation will treat an entity that does not have a clearly defined classification as a partnership for acreage limitation purposes, until such proof is provided.

Can an entity change its classification?

Yes. As explained previously, an entity that the IRS does not require to be taxed as a corporation may choose to be taxed as either a partnership (which is the default tax status) or a corporation (by making an election and having it approved by the IRS). If an entity's classification changes for IRS purposes, it will also change for acreage limitation purposes. For example, if a partnership elects to be taxed as a corporation, at that point Reclamation will treat the entity as a corporation. If 5 years later the entity elects to be treated as a partnership again, at that point the entity will revert to being treated as a partnership for acreage limitation purposes.

Entity Classification and General Administration of the Acreage Limitation Provisions

How is land attributed to a corporation or to a partnership?

If an entity is classified as a corporation, land held by the corporation will be attributed to the corporation and to each of its part owners (usually shareholders) in proportion to the percent of interest each part owner holds in the corporation. Similarly, if an entity is classified as a partnership, land held by the partnership will be attributed to the partnership and each of its part owners (usually partners) based on the percent of interest each part owner holds in the partnership. Some partnerships are comprised of only general partners, while other partnerships have both general partners and limited partners. Land is attributed to all partners, regardless of whether they are classified as general or limited.

What are the impacts of being considered a corporation as compared to a partnership?

For acreage limitation purposes, an entity's classification as a corporation or a partnership mainly impacts (1) ownership and nonfull-cost entitlements, and (2) the signature requirements on RRA forms and irrevocable elections. Details are as follows:

1. Acreage Limitation Entitlements –

- Discretionary provisions – The ownership and nonfull-cost entitlements are the same for both corporations and partnerships, regardless of whether the entity is a qualified recipient, a limited recipient that received water on or before October 1, 1981, or a limited recipient that did not receive water by that date.
- Prior law provisions – The ownership and nonfull-cost entitlements for corporations and partnerships generally are the same (160 acres). However, if a partnership has alienable and separable interests, the entitlements are 160 acres per part owner.

Enclosed is a table that summarizes the ownership and nonfull-cost entitlements for corporations and partnerships.

2. Signature Requirements –

- RRA forms – The signature requirements that apply to a corporation also apply to an **unincorporated** entity (e.g., a partnership) that has elected to be taxed as a corporation and is treated as a corporation for acreage limitation purposes. That is, the forms for such an entity are to be signed by an officer or an authorized agent, and such an entity may not use a signature authorization form.
- Irrevocable election forms – The signature requirements that apply to a corporation also apply to an **unincorporated** entity that has elected to be taxed as a corporation and is treated as a corporation for acreage limitation purposes. That is, the irrevocable election must be signed by an officer or authorized agent in Signature Block 2 on the irrevocable election form. The signature does not need to be notarized. A copy of the entity's corporate resolution must be attached to the election. As is the case with all entities, a signature authorization form cannot be used when making an irrevocable election. Recently, Signature Block 2 on the irrevocable election form was revised so that it will better accommodate unincorporated entities that are being treated as corporations for acreage limitation purposes.

How will a change in entity classification affect the entity's current ownership and nonfull-cost entitlements?

When an entity changes its classification, for acreage limitation purposes it will be considered to be a "new entity" as a result of the classification change. This will affect the following types of Reclamation irrigation water recipients:

- **Limited recipient that received Reclamation irrigation water on or before October 1, 1981:** A new entity classification will reduce the entity's 320-acre nonfull-cost entitlement to zero acres.

Example: Partnership A is a limited recipient that received Reclamation irrigation water before October 1, 1981. Accordingly, its nonfull-cost entitlement is 320 acres rather than zero acres. In the year 2003, Partnership A elects to be taxed as a corporation for IRS purposes. Because of this election, Reclamation treats Partnership A as a corporation for acreage limitation purposes. In addition, the entity is considered a “new entity” as of the date the classification change became effective. Since the “new entity” did not receive Reclamation irrigation water prior to October 1, 1981, its nonfull-cost entitlement becomes zero acres as a result of the classification change.

- **Prior law entity:** A classification change will affect the way the ownership entitlements are applied to the entity. Since an entity is considered a “new entity” when its classification changes, the ownership entitlements will be applied on a westwide basis when the new classification becomes effective, even if the entity owns land in one or more districts and the land was purchased on or before December 6, 1979.

Is an entity’s change to its classification considered to be a landholding change?

Yes. If an entity elects to change its entity classification from a partnership to a corporation or vice versa, Reclamation will consider this to be a landholding change. Accordingly, the entity must:

- Give verbal or written notification of the classification change to all districts in which the entity directly or indirectly owns or leases land *within 30 calendar days of the change*; and
- Submit new standard RRA forms to all such districts *within 60 calendar days of the change*.

For more information regarding landholding changes, see Fact Sheet 11, “What Constitutes a Landholding Change,” which is available at Reclamation’s RRA website www.usbr.gov/rra or from the appropriate Reclamation office.

Entity Classification and Administration of the Acreage Limitation Provisions to Specific Types of Landholders

How should certain religious or charitable organizations enter their entity classification on the RRA forms?

Specifically, this question pertains to religious or charitable organizations that (1) are exempt from taxation under section 501 of the Internal Revenue Code and (2) do not meet the additional criteria in section 219 of the RRA. Pursuant to section 426.9 of the Regulations, this type of religious or charitable organization will be treated as a legal entity for acreage limitation purposes and must therefore complete the RRA form for entities (“Certification of Entity’s Landholdings” [Form 7-2181] or “Report of Entity’s Landholdings” [Form 7-2191], as applicable) rather than the RRA form for religious or charitable organizations (“Certification of Religious or Charitable Organization’s Landholdings” [Form 7-2184] or “Report of Religious or Charitable Organization’s Landholdings” [Form 7-2194], as applicable).

Both RRA Form 7-2181 and Form 7-2191 require that the person completing the form for the entity indicate the entity's "type." The forms provide the following "entity-type" choices: corporation, partnership, joint tenancy or tenancy-in-common, or other. When indicating the "entity type" on Form 7-2181 or Form 7-2191, an organization that has a section 501 tax exemption but does not meet the other RRA section 219 criteria must check the "Other" box and write "religious organization" or "charitable organization" (as applicable) on the line after the box. This particular instruction is made clear in the 2004 RRA forms that are currently in the approval process required by the Paperwork Reduction Act of 1995. Please note that the "Other" box on Form 7-2181 and Form 7-2191 is not to be used by an entity that does not have a section 501 tax exemption. Such an entity must be classified as a corporation, partnership, or a tenancy, and the appropriate entity-type box must be checked on the entity's Form 7-2181 or 7-2191.

How will Reclamation treat farmers' cooperatives?

Reclamation will treat a farmer's cooperative (cooperative) as a corporation for acreage limitation purposes because:

- Cooperatives are a type of corporation. They are usually incorporated under State law by filing articles of incorporation.
- Pursuant to the Internal Revenue Code, cooperatives generally are exempt from taxation because they do not have taxable income. However, some cooperatives may have taxable income. In that case, the income is taxed in much the same way as corporations are taxed.

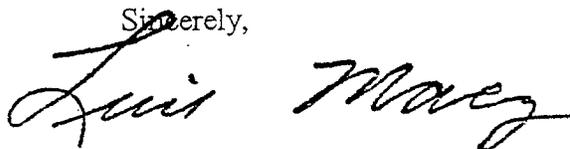
How will Reclamation treat limited liability companies (LLC's)?

The IRS taxes an LLC as a partnership unless the LLC has submitted the appropriate IRS form to elect to be treated as a corporation, and the IRS has approved the election. Therefore, an LLC will be treated as a partnership for acreage limitation purposes, unless the LLC submits a copy of the letter in which the IRS approved its election to be classified as a corporation. When checking the entity type of Form 7-2181 or Form 7-2191, an LLC must identify itself as either a partnership or a corporation. The LLC cannot check the "Other" box on its RRA form.

SEE CLARIFICATION NOTE

If you have questions regarding the information in this letter, please contact the appropriate Reclamation office.

Sincerely,



Luis Maez, Manager
Reclamation Law and Revenues Management Office

Enclosure

**COMPARISON OF OWNERSHIP AND NONFULL-COST ENTITLEMENTS
FOR CORPORATIONS AND PARTNERSHIPS
ESTABLISHED UNDER STATE OR FEDERAL LAW**

ACREAGE LIMITATION STATUS	OWNERSHIP ENTITLEMENTS for Corporations Vs. Partnerships			NONFULL-COST ENTITLEMENTS for Corporations Vs. Partnerships		
	Corporation	Partnership That Does Not Have Alienable and Separable Interests	Partnership With Alienable, Equal, and Separable Interests	Corporation	Partnership That Does Not Have Separable and Alienable Interests	Partnership With Separable, Alienable, and Equal, and Interests
Qualified recipient <i>(See Note 1 below.)</i>	960 acres	960 acres	960 acres	960 acres	960 acres	960 acres
Limited recipient that received Reclamation irrigation water on or before 10/1/81. <i>(See Note 1 below.)</i>	640 acres	640 acres	640 acres	320 acres	320 acres	320 acres
Limited recipient that did not receive Reclamation irrigation water on or before 10/1/81. <i>(See Note 1 below.)</i>	640 acres	640 acres	640 acres	0 acres	0 acres	0 acres
Prior law recipient <i>(See Note 2 below.)</i>	160 acres	160 acres	160 acres per partner	160 acres	160 acres	160 acres per partner

Note 1: Ownership and nonfull-cost entitlements for qualified and limited recipients apply on a westwide basis. See section 426.8 of the Acreage Limitation Rules and Regulations regarding ownership and nonfull-cost entitlements for foreign entities.

Note 2: Ownership entitlements for prior law recipients apply on a westwide basis unless the land was acquired by the current landowner on or before December 6, 1979. For land acquired before that date, the ownership entitlements apply on a district-by-district basis.

The nonfull-cost entitlement for prior law recipients is equal to the recipient's ownership entitlement. However, when computing a prior law recipient's acreage subject to full-cost, all owned and leased irrigation land westwide must be included in the computation.

See section 426.8 of the Acreage Limitation Rules and Regulations regarding ownership and nonfull-cost entitlements for foreign entities.

Clarification Note to June 13, 2003, letter

Effective January 2006, a limited liability company can check the "Other" box in entity type and enter "LLC" as the type of entity. Since the entity checked the "Other" box, the entity will be required to answer the question of how the entity is taxed by the Internal Revenue Service - as a corporation or as a partnership.