

## FACT SHEET 15

# LEASES AND FARM OPERATING ARRANGEMENTS

### Reclamation Reform Act of 1982 (RRA)

This fact sheet details how the acreage limitation provisions, as established by the RRA, are applied to leases and farm operating arrangements. If you are unsure of the information discussed in this fact sheet, contact your district or the appropriate Bureau of Reclamation office, or see the **Sources for more information** section at the end of this fact sheet.

#### How do the RRA and its associated regulations affect leases and farm operating arrangements?

- The RRA and its associated regulations (43 CFR<sup>1</sup> part 426; Regulations) specify that Reclamation irrigation water can be delivered to leased land only if the **lease meets certain criteria**.
- Land leased under a lease document that does not meet the criteria will be **ineligible to receive Reclamation irrigation water** until the lease is terminated or modified to meet the criteria.
- Land leased from a **public entity** counts against both the ownership and nonfull-cost entitlements of the **lessee**. Land subleased from a landholder that leased the land from a public entity counts against the ownership and nonfull-cost entitlements of the **sublessee**.
- **Farm operating arrangements must also meet certain criteria** in order for the farm operating arrangement to be considered exempt from the nonfull-cost entitlement provisions of the RRA.
- The regulations titled “Information Requirements for Certain Farm Operations in Excess of 960 Acres and the Eligibility of Certain Formerly Excess Land” (43 CFR part 428) specify **when a farm operator must submit RRA forms**, and when certain kinds of formerly excess land can receive Reclamation irrigation water.
- **The price for Reclamation irrigation water deliveries can vary** depending on whether land is farmed under a lease or a farm operating arrangement. If Reclamation irrigation water was delivered to land **leased** in excess of the applicable nonfull-cost entitlement, Reclamation will issue a bill for, or collect, the monetary difference between the contract rate and the full-cost rate for the Reclamation irrigation water that was delivered.

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<sup>1</sup> Code of Federal Regulations

## What are the criteria for a lease?

In order for districts to be able to deliver Reclamation irrigation water to leased land, **the lease document must meet all of the following criteria** specified in the RRA and the Regulations:

- The lease must be **in writing**.
- The lease **includes the effective date and term (length) of the lease**, the length of which must be **10 years or less** (including any exercisable options).
  - However, the lease term for perennial crops with an average life longer than 10 years may be equal to 10 years or the average life of the crop as determined by Reclamation, whichever is greater, and in no case may the lease term exceed 25 years, including any exercisable options.
- The lease includes a **legal description of the leased land** that is at least as detailed as what is required on the RRA forms.
- **Signatures of all parties to the lease** are included on the lease.
- The lease **includes the date(s) or conditions when lease payments are due and the payment amounts** or the method of computing the payments due.
- The lease is **available for Reclamation's inspection** (Reclamation reviews and approves all leases having terms longer than 10 years).
- If either the lessor or the lessee is subject to the discretionary provisions, the lease provides for **agreed upon payments that reflect the reasonable value of the irrigation water to the productivity of the land**.

## What happens if a lease does not meet the lease criteria?

- Land under a lease that does not meet all of the above criteria will be ineligible to receive Reclamation irrigation water until the lease is terminated or modified within 60 calendar days of written notification to satisfy the criteria.
- If an approvable lease is not submitted for Reclamation's review and approval, or the lease is not terminated at the end of the 60-day period, the land in question will be ineligible to receive Reclamation irrigation water.
  - Furthermore, previous deliveries of Reclamation irrigation water may be assessed the compensation (full-cost) rate.
- If the lease is terminated or modified within the allowed 60 calendar days, Reclamation will review the matter to determine if the term of the lease was acceptable during the time period it was in effect.

## What is an acceptable term of a lease for acreage limitation purposes?

- The RRA requires the term of a lease for growing **annual crops to be 10 years or less**, including any options to extend the lease.
  - For example, a new lease to grow annual crops having a term of 5 years and an option to extend for an additional 5 years is acceptable. The 5-year initial term plus the 5-year extension total no more than the 10 years allowed for an annual crop lease.

- A lease to grow **perennial crops can have a term of up to 25 years**, depending on the type of perennial crop being grown.
  - Reclamation has worked with the United States Department of Agriculture to produce a list of perennial crops grown in the 17 Reclamation states, including the lifespan associated with each perennial crop. Contact your district or the appropriate Reclamation office for more information.
- If more than one type of crop is being grown on the leased land, **the lease term associated with the predominant crop will apply.**
  - For example, an annual crop is being grown on 51 percent of the land, and a perennial crop with a life span of 15 years is being grown on 49 percent of the land. The annual crop is the predominant crop; therefore, a lease document having a 10-year lease term (not a 15-year lease term) is acceptable.

### **How does Reclamation treat annual leases, lease extensions, and lease renewals?**

- **Annual lease:** A lease having an effective term of 1 year or less that also includes a clause requiring **annual** action to either renew the lease for another year, or withdraw from the lease.
- **Lease extension:** A continuation of the original lease, the term of which, except for annual leases, must be added to the term of the original lease for purposes of determining the total term of the lease.
  - A lease extension is typically accomplished via an exercisable option included in the original lease. If the lease is extended with no exercisable option in the original lease, the extension must be in writing and amend the original lease.
- **Lease renewal:** A lease renewal is generally viewed as entering into a new lease, provided a new lease document is created to renew the lease.
  - A lease renewal that is accomplished through either an exercisable option in the original lease, or without the creation of a new lease document, is treated as a lease extension for acreage limitation purposes.

### **How is the RRA generally administered to a sublease?**

- Land that is subleased from a lessee to a sublessee does not need to be factored into the original lessee's total landholdings for purposes of calculating total landholdings or for application against the RRA forms submittal threshold.
- Sublessees must factor in the subleased land for purposes of calculating total landholdings and for application against the RRA forms submittal threshold.
- The original lessee and the sublessee are required to include information where requested on their respective RRA forms concerning the subleased land and the parties involved.

### **How is the RRA generally administered to a sharecropping arrangement?**

- The main difference between a lease and a sharecropping arrangement is the method and timing of payment to the landowner for the use of the landowner's land.
- A typical lease involves payment to the landowner **prior to** the lessee's use of the land.
- A typical sharecropping arrangement involves the landowner's receipt of a portion of the crop as payment, **after** the land is used (that is, after harvest).

- A sharecropping arrangement is generally treated as a lease for acreage limitation purposes except in very specific circumstances. Contact your district or the appropriate Reclamation office for more information.

### **What is a farm operating arrangement?**

- A farm operating arrangement involves an individual or legal entity other than the landowner, lessee, or sublessee, that performs any portion of the farming operation.
- Farm operators can include farm managers, but do not include spouses, minor children, employees for whom the employer pays social security taxes, or custom service providers (for example, crop dusters, custom harvesters, etc.).

### **When is a farm operating arrangement considered to be a lease for acreage limitation purposes?**

If **both** of the following criteria are met, the farm operating arrangement will **not** be considered to be a lease for acreage limitation purposes.

- The **landholder** assumes all of the economic risk. For example, the farm operator, manager, or consultant receives a fee for service(s) and that fee is not based on the productivity of the land, the results of the services provided, how well the market is doing, etc.
- The **landholder** retains the right to the use and possession of the land.

If the first criterion is not met and the farm operator has either use or possession of the land, it may result in Reclamation's determination that the farm operating arrangement is a lease for acreage limitation purposes. If a farm operating arrangement is determined to be a lease, the arrangement must then meet all of the required lease criteria in order to be considered a valid lease for acreage limitation purposes.

### **Who must submit a "Declaration of Farm Operator Information" (Form 7-21FARMOP)?**

- A farm operator that provide services to more than 960 nonexempt acres westwide (in the 17 Western States where Reclamation has projects) held (directly or indirectly owned or leased) by a single trust (not an estate) or legal entity (including 100-percent owned entities) or any combination of trusts and/or legal entities.
- A part owner of a farm operator entity that must submit RRA forms if that farm operator is providing services to land that the part owner formerly owned as excess and sold or transferred at a price approved by Reclamation.
- A "Verification of Landholdings" (Form 7-21VERIFY) cannot be used to satisfy the annual requirement to submit a Form 7-21FARMOP.
- The landholding change requirements with regard to RRA form submittal do not apply to the submittal of Form 7-21FARMOP. See Fact Sheet 11 (Landholding Changes) for more information.

## How does 43 CFR part 428 apply to farm operating arrangements?

- An estate is not treated in the same manner as a trust in a farm operating arrangement.
- Public entities will not be considered to be farm operators.
- Certain farm services are exempted from application of 43 CFR part 428, and certain farm services have been grouped together to form one farm service for the purpose of applying 43 CFR part 428.
  - Contact your district or the appropriate Reclamation office for more information.
- Reclamation is required to audit at least once every 5 years all farming operations that provide services to more than 960 acres, including land held by individuals.

## When is a farm operator not allowed to receive Reclamation irrigation water?

- Former owners of excess land who (1) sold or transferred such land at a price approved by Reclamation, **and** (2) became farm operators of that land.
  - The exceptions are when the full-cost rate is paid for all Reclamation irrigation water deliveries, **or** the land in question becomes exempt from the acreage limitation provisions.

## Sources for more information

More information for your landholding situation and the corresponding acreage limitation entitlements can be found in the following documents. Contact your district or the appropriate Reclamation office for further guidance.

<b>Form 7-21INFO</b>	General Information About the RRA Forms	The RRA Fact Sheets and the current water year's RRA forms and instructions are available online and at your district or the appropriate Reclamation office.
Separate instructions to each RRA form applicable to your landholding situation		
<b>RRA Fact Sheet 1</b>	RRA Forms	
<b>RRA Fact Sheet 2</b>	Acreage Limitation Status	
<b>RRA Fact Sheet 4</b>	Qualified Recipient Entitlements	
<b>RRA Fact Sheet 6</b>	Limited Recipient Entitlements	
<b>RRA Fact Sheet 8</b>	Prior Law Recipient Entitlements	
<b>RRA Fact Sheet 11</b>	Landholding Changes	
<b>RRA website</b> (including the RRA forms, District Reference Sources, and the text of the RRA and its associated Regulations)		<a href="http://www.usbr.gov/rra">www.usbr.gov/rra</a>