

# Audit Technique Guide - Corporations Organized To Finance Crop Operations – IRC Section 501(c)(16)

## Introduction

This discussion contains audit guidelines for IRC Section 501(c)(16) organizations. It gives audit methods that are useful in finding and developing issues in these types of audits.

These guidelines give specific aid for IRC Section 501(c)(16) organization audits and aren't all-inclusive. Its purpose is to add to the information in:

- [IRM 4.75.10, Exempt Organization Pre-Audit Procedures](#)
- [IRM 4.75.11, On Site Examination Guidelines](#)
- [IRM 4.75.12, Required Filing Checks](#)
- [IRM 4.75.13, Issue Development](#)

The intent isn't to restrict identifying issues or using audit techniques not included here. This discussion doesn't contain detailed technical information on IRC Section 501(c)(16) organizations. Review [IRM 7.25.16, Corporations Organized to Finance Crop Operations](#) .

## Background Information

IRC Section 501(c)(16) exempts from federal income tax corporations organized by an IRC Section 521 farmers' cooperative marketing or purchasing association or members for financing the members' or other producers' crop operations.

The financing corporation must operate in conjunction with the marketing or purchasing association.

## Audit Guidelines

Determine whether the organizing farmers' cooperative is an IRC Section 521 association or IRC Section 521 corporation. If the cooperative is exempt under IRC Section 521:

- Get a copy of its determination letter.
- Inspect the cooperative's annual tax return.

Inspect the governing instruments. Evaluate the organization's operations. Determine whether:

- The organizing IRC Section 521 organizations, or members, hold substantially all of the voting stock.
- Nonvoting preferred stock, if issued, can't participate in the organization's profits beyond the fixed dividend rate.

Verify that the dividend rate on all capital stock doesn't exceed the greater of:

- The legal rate of interest in the state where incorporated.
- Eight percent per year on the cost of the stock when issued.

Determine if there is a reserve and the purpose, the need, and the reasonableness of the reserve(s). Find out if state law requires a reserve. (For example: A reasonable reserve for erecting buildings required in the business operation).

If you have any problems or concerns about the farmers' cooperative, contact Small Business/Self Employed (SB/SE) or Large Business and International (LB&I).