

Cooperation Without Incorporation

August 5, 2019



Agenda

- Introduction
- Advantages
 - Legal
 - Tax
- Disadvantages
 - Legal
 - Tax
- Alternatives
- Group discussion and Q & A

Introduction



What is an Unincorporated Cooperative Association?

- AKA: Limited Cooperative Association, Cooperative LLC hybrid, etc
- Entity organized under a state's unincorporated cooperative association statutes
- Still have member patrons that are allocated earnings based on business done with and for the cooperative
- However allows for member investors that are allocated earnings based on investment
- Both member types can have voting rights

History

- Need for capital because of more agricultural cooperatives getting into or were specifically created for value-added processing
- 2001 - Wyoming adopted the Wyoming Processing Cooperative Law (limited to ventures that market or process agricultural products)
- 2002 – 2006 Minnesota, Tennessee (limited to Ag), Iowa, Wisconsin
- 2007 – National Conference of Commissioners on Uniform State Laws drafted the Uniformed Limited Cooperative Association Act

A Comparison of Limited Cooperative Association Statutes*
(Updated & adapted from Draft for Approval, Uniform Limited Cooperative Association Act, With Prefatory Note and Comments, NCCUSL, 2007)

CITATION	SCOPE	PATRON VOTES	PATRON ELECTED DIRECTORS	ALLOCATION
"Wyoming Processing Cooperative law [sic]" (enacted 2001). <i>Wyo. Stat. Annot.</i> §17-10-201.	Formed under a cooperative plan to market or process crops, livestock and other agricultural products and other purposes that are related to the business of the cooperative.	Each patron has one vote but may have more; patron members voted collectively based upon the majority of patron members voting on the issue."	At least one-half of the voting power on general matters allocated to 1 or more directors elected by patron members	Based on contributions unless otherwise provided. Patrons, collectively, shall have not less than 15 percent. Same rule for distributions.
"Minnesota Cooperative Associations Act" (2003 session laws). <i>Minn. Stat. Annot.</i> §305B.001.	Based on a cooperative plan for any lawful purpose	Patron vote based on block voting; bylaws may not reduce the collective patron vote to less than 15 percent of the total vote	At least one-half of the voting power on general matters shall be allocated to 1 or more directors elected by patron members	Based on contributions unless otherwise provided. Patrons must have 50 percent of profits allocation and distributions in any fiscal year except articles or bylaws may reduce to 15 percent
"Tennessee Processing Cooperative Law" (effective 2005). <i>Tenn. Code Annot.</i> §43-38-101.	Requires a cooperative plan for ag. processing and marketing	Each patron member has one vote but may have more. "On any matter of the cooperative, the entire patron members voting power shall be voted collectively based upon the vote of the majority of patron members' voting on the issue	At least one director must be elected by patron members; minimum 51 percent of the voting power on general matters must be allocated to directors elected exclusively by patron members.	Based on contributions unless otherwise provided. Patrons must have at least 15 percent of both allocations and distributions.
"Iowa Cooperative Associations Act" (effective 2005) <i>Iowa Code Annot.</i> Ch. 501A.	Any lawful purpose.	Patron members vote on a collective block vote; bylaws may not reduce patron member vote to less than 15 percent of the total vote	A least one-half of the voting power allocated to the board members elected by patron members, except in certain matters.	Based on contributions unless otherwise provided . Patrons must be allocated at least 50 percent of profits and distributions in any fiscal year. Articles, bylaws, or patron member votes may reduce to 15 percent.
"Wisconsin Cooperative Associations Act" (effective 2006) <i>Wis. Stat. Annot.</i> §193.005 (note that the reviser of statutes captions the chapter, "Unincorporated Cooperative Associations").	Any lawful purpose, except utilities	Patron members vote on a collective block vote; the articles or bylaws may not reduce the collective patron member vote to less than 51 percent of the total member vote. Unless the articles or bylaws provide otherwise, the collective vote of the patron members approving an issue must be a majority of all members votes	"[A] majority of the directors shall be elected exclusively by patron members, unless otherwise provided in the articles or bylaws." Also provides for a non-voting financial expert.	Patron members must have 51 percent of both profit allocations and distributions. The patron members, by majority vote, may authorize lower amount but not less than 30 percent
"Uniform Limited Cooperative Association Act", NCCUSL, November 27, 2007.	For "any lawful purpose, whether or not for profit, [except] [designated prohibited purposes]."	Each patron member has at least one vote. Requires majority of voting power be held by patron members. Majority of member votes AND majority of patron member votes required for approval, unless more than a majority from either group required by bylaws.	A majority of the board must be elected exclusively by patron members. At least one-third of directors must be patron members. Each director has one-vote.	Patron members must be allocated at least 50% of profits. Unless bylaws state otherwise, distributions at discretion of board and (implicitly) are not subject to allocation requirements.

*This is a summary only; exceptions may exist in statutory language or through interpretation.

UW Center for
Cooperatives
[https://resources.
uwcc.wisc.edu/Leg
al/LimitedCoopAss
oc.pdf](https://resources.uwcc.wisc.edu/Legal/LimitedCoopAssoc.pdf)



States with these Statutes

Wyoming

Tennessee

Wisconsin

Oklahoma

Kentucky

Vermont

Washington

Minnesota

Iowa

Utah

District of Columbia

Nebraska

Colorado

Advantages - Legal

- Generally, tend to permit more flexibility than traditional coop laws
- Outside directors allowed
- Investors allowed
- Can use cooperative in your name

Advantages - Tax

- Flexibility
 - PLR 200139020 - eligible entity under Reg. §301.7701-3(a) (same as LLC)
 - Partnership
 - Sub chapter T
 - C-Corporation (taxable)
 - Single member (disregarded entity)
- Partnership advantages
 - Most members should not have self employment income from the cooperative
 - All income including nonpatronage receives single level of taxation

Disadvantages - Legal

- May not be well understood by banks, potential members, etc.
- Unclaimed property
- Worker co-op

Disadvantages - Tax

- May lose state tax exemption
- May end up being taxed as the wrong tax entity type
- Uncertainty that even if check in the box election to be taxed as a corporation that the cooperative will meet “operating on a cooperative basis”
- If taxed as a partnership
 - Lose out of 199A(g) benefits (DPAD)
 - K-1s can be discouraging membership of some co-ops and if the operation is multistate, all members must file tax returns in each state
 - Passive losses

Alternatives

- Joint Ventures
 - Traditional cooperative and investors create a new entity
 - Don't have investors involved with 100% of cooperative's business
- LLC
 - A well crafted member agreement can simulate these state statutes

Group Discussion and Q & A



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