Non-Profit Unrelated Business Income Tax

US Youth Soccer Workshop
February 25, 2011
Introduction & learning objectives

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- Learning objectives:
  - To understand whether your organization may be subject to UBIT
  - To identify unrelated trade or business activity
  - To capture and report UBIT
  - To prepare tax filings for UBIT
Disclaimer

Brad is not a practicing tax specialist. This presentation is intended to be a basic introduction to non-profit UBIT and should not be construed, used or referred to as tax advice from Brad or Grant Thornton LLP. Your specific tax situation should be discussed with your own qualified tax professional.
Failure to heed disclaimer
Agenda

- Define UBIT
- Unrelated trade or business activities
- Organizations subject to UBIT
- Unrelated business taxable income
- Tax and filing requirements
What is UBIT?

- Income from a trade or business:
  - *Regularly carried on* by an exempt organization
  - *Not substantially related* to the performance of the exempt purpose/function
  - Organization *uses the profits*
What is a trade or business?

- Any activity:
  - For the *production of income*
  - *Sale* of goods or services
- Can't bury in another exempt activity
What is "regularly carried on"?

- Frequency & continuity
- Pursued *similar to non-exempt* commercial activities:
  - Sandwich stand 2 weeks at state fair = OK
  - Year-round parking lot = UBIT
When is it "not substantially related" to exempt purpose?

- Does not *contribute importantly* to accomplishing the exempt purpose/function
  - Facts and circumstances driven
- Consider *size & extent* of activities
  - Sales of products from performance of exempt functions in same state
  - Dual use of assets or facilities
  - Exploitation of exempt functions
Examples: "not substantially related"

- Artist facilities
- Member list sales
- School handicrafts
- Halfway house workshop
- Directory of members
- Sales of advertising space
Excluded activities

- Volunteer workforce
- Convenience of members
- Qualified sponsorship payments
  - Sponsor receives no substantial benefit
  - May use name or logo in acknowledgement/activities
    - NOT advertising (discussed later)
    - NOT used in organization's regularly published periodicals
- Selling donated merchandise
- Some instances...bingo
- Distribution of low cost articles
  - Giveaways
- Exchange or rental of member lists
- Public entertainment activities
- Convention or trade show activity
Organizations subject to UBIT

- Most organizations exempt under IRC §501(a), including 501(c)(3)s:
  
  • "To be tax-exempt under section 501(c)(3)…, an organization must be organized and operated exclusively for exempt purposes…, and none of its earnings may inure to any private shareholder or individual. In addition, it may not…attempt to influence legislation as a substantial part of its activities and it may not participate in any campaign activity for or against political candidates."
  
  • "Organizations described in section 501(c)(3) are commonly referred to as charitable organizations. Organizations described in section 501(c)(3), other than testing for public safety organizations, are eligible to receive tax-deductible contributions in accordance with Code section 170."
UBIT: taxable income

- Gross income from UB
- Less: Deductions directly connected

<table>
<thead>
<tr>
<th>Gross income</th>
<th>$1,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less: Costs to sell</td>
<td>500</td>
</tr>
<tr>
<td>UBITaxable income</td>
<td>$ 500</td>
</tr>
</tbody>
</table>
General exclusions from gross UBI

- Dividends, interest annuities and other investment income
- Royalties
- Rents from real property
- Income from research
- Gains and losses from disposition of assets
Deductions from UBI

- Proximate and primary relationship to UBI
- Expenses, depreciation and similar items
Advertising examples
Advertising in periodicals

- Considered an "exploitation" of exempt activity

<table>
<thead>
<tr>
<th>IF gross advertising income is...</th>
<th>THEN UBTI is...</th>
</tr>
</thead>
<tbody>
<tr>
<td>More than direct advertising costs</td>
<td>The excess advertising income, reduced (but not below zero) by the excess, if any, of readership costs over circulation income</td>
</tr>
</tbody>
</table>
| Equal to or less than direct advertising costs | Zero.  
  • Circulation income and readership costs are not taken into account  
  • Any excess advertising costs reduce (but not below zero) UBTI from any other UB activity. |
Periodical income

- *Gross advertising income* = all income from the unrelated advertising activities
- *Circulation income* = all income from production, distribution, or circulation
  - Includes *allocable membership receipts* if periodical comes with membership
Allocable membership receipts

- Part of membership receipts (dues, fees, charges) equal to the amount that would have been charged and paid for periodical if it had been published:
  - By a taxable entity
  - For profit
  - At arm's length
## Allocable membership receipts

<table>
<thead>
<tr>
<th>IF...</th>
<th>THEN the amount used to allocate membership receipts is...</th>
</tr>
</thead>
<tbody>
<tr>
<td>20% or more of the total circulation consists of sales to non-members</td>
<td>The subscription price charged to non-members.</td>
</tr>
<tr>
<td>The above condition does not apply, <strong>and</strong> 20% or more of the members pay reduced dues because they do not receive the periodical</td>
<td>The reduction in dues for a member not receiving the periodical.</td>
</tr>
<tr>
<td>Neither of the above conditions applies</td>
<td>The membership receipts multiplied by this fraction:</td>
</tr>
<tr>
<td></td>
<td><strong>Total periodical costs</strong></td>
</tr>
<tr>
<td></td>
<td><strong>Total periodical costs plus</strong></td>
</tr>
<tr>
<td></td>
<td><strong>Cost of other exempt activities</strong></td>
</tr>
</tbody>
</table>
UBIT tax reporting

- Form 990-T
- UB gross receipts over $1,000
- Generally, filed 15\textsuperscript{th} day of the 5\textsuperscript{th} month after end of tax year
  - 3 month extension available
- Must be available for public inspection
- See \url{www.irs.gov} for resources
UBIT violations
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