

# Unrelated Business Income Tax (UBIT) Fundamentals

Presented by: The Financial Services Office, Tax Services



# TAX EXEMPT OR NOT?

Isn't the University exempt from Federal  
Income Tax?



Yes and No



# EXEMPT ACTIVITY

Why is UA partially income tax exempt?

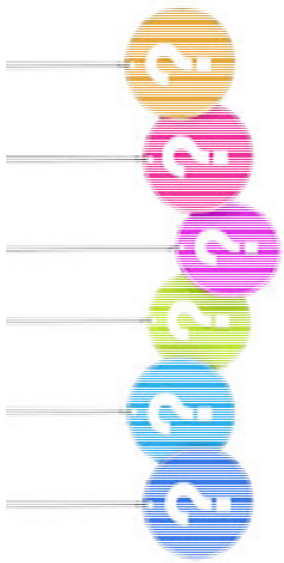
- UA is a political subdivision of the State of Arizona
- UA is income tax exempt as an instrumentality of the State of Arizona under §115 of Internal Revenue Code

Which activities are tax exempt?

- Those that support the exempt purposes of colleges and universities:
  - Research and Discovery (with restrictions)
  - Teaching and Learning
  - Outreach and Public Service
  - Fostering national or international amateur sports competition



BUT...



# TAXABLE ACTIVITY

UA is not tax exempt under § 513 of the Internal Revenue Code for activities which are:



- Substantially unrelated to the exempt purposes of colleges and universities, even if the funds produced are used to support the University's exempt functions



# UBIT DEFINED: 3 PRONG TEST

In order to be subject to UBIT, an activity must meet all three designations:



- Conducted like a trade or business, AND



- Regularly carried on, AND



- Not substantially related to UA's tax exempt purpose



# TRADE OR BUSINESS

- In general, a trade or business is an activity conducted for the production of income from:
  - The sale of goods, or
  - The performance of services
- In order to be a trade or business, an activity must be:
  - Conducted with an intent to profit
  - Not resulting in profit in the short term does not exclude the activity from being a trade or business
  - Prolonged losses could signify a lack of intent to profit and disqualify the activity as UBIT



# REGULARY CARRIED ON

- In general, an activity is regularly carried on if:
  - It shows frequency and continuity
  - Is conducted in a manner similar to a non-exempt organization running a similar business
- An activity should not be considered regularly carried on if it is:
  - Conducted only on an infrequent basis
  - Conducted without competitive or promotional effort
- More to know:
  - Year round activities are regular even if they are conducted only one day a week
  - Seasonal activities may be considered regularly carried on even though they are conducted only for a short period annually



# SUBSTANTIALLY UNRELATED TO EXEMPT PURPOSE

- In general, an activity is unrelated if:
  - It does not contribute importantly to the exempt purposes of the University other than through the production of income
  - Is conducted to a size or extent larger than necessary for the exempt function





# EXCEPTIONS



- Volunteer workforce
  - 85% or more of the activity is conducted by volunteers
- Convenience of members
  - Trade or business provided for the convenience of members
  - UA members include students, faculty, employees, officers and patients
  - Alumni and members of the general public are not members for UBIT purposes
- Sale of donated merchandise
- Qualified sponsorship
  - Payment to UA by a corporation or business for which the company receives no substantial return of benefit other than the use or acknowledgement of its products or services



# SUBSTANTIAL RETURN OF BENEFITS: EXAMPLES

- Non-qualified Sponsorships are potentially subject to UBIT and might include such return of benefits as:
  - Advertising
    - Contains comparative or qualitative language
    - Contains price or savings information
    - Includes a call to action
    - Includes an endorsement or inducement to purchase sponsor's product or service
  - Exclusive provider arrangements
  - Goods, facilities, services or other privileges
  - Exclusive or non-exclusive right to use the University's intangible assets
    - Trademark
    - Logo



# EXCLUSIONS



- Investment income, such as:
  - Interest
  - Annuities
- Royalty income
- Gains or losses from the sale of property (other than inventory or property held primarily for sales)
- Rents from real property, if:
  - Does not include personal property rental
    - Graduated taxability based on inclusion of personal property of <10%, 11-50%, or 51%
  - Rents are not based on net profit
  - Personal services are not provided
  - Property is not debt financed
    - If used 85% or more for exempt purposes, property is not considered debt financed
- Research, except...





# TAX CUTS & JOBS ACT: SOME UBIT IMPACTS

	BEFORE	AFTER
Tax Rate(s)	Graduated; up to 39%	Flat 21%
Qualified Transportation Fringes	Costs not included in UBTI	Costs included in UBTI if not included in employee taxable wages
Activity Bucketing	Gains and losses of all UBI activity consolidated	Gain and losses bucketed by activity, no longer consolidated



# UBIT ESTIMATED PAYMENT AND RETURN

- FSO annually makes an estimate of UBIT liability
  - Estimated payment is due October 15<sup>th</sup>
- FSO annually files IRS Form 990-T
  - Return is due November 15<sup>th</sup> and covers the FY ending June 30<sup>th</sup>

**Form 990-T** Exempt Organization Business Income Tax Return (and proxy tax under section 6033(e)) OMB No. 1545-0087

For calendar year 2016 or other tax year beginning \_\_\_\_\_, 2016, and ending \_\_\_\_\_, 2016

Department of the Treasury Internal Revenue Service

Information about Form 990-T and its instructions is available at [www.irs.gov/form990](http://www.irs.gov/form990). Do not enter SSN numbers on this form as it may be made public if your organization is a 501(c)(3).

**2016**

**Open to Public Inspection for 30 Days**

**A** Check box if address changed

**B** Exempt under section:  501(c)(1)  408(a)  408A  505(a)

**C** Book value of all assets at end of year

**D** Employer identification number (Employer/ trust, see instructions.)

**E** Unrelated business activity codes (See instructions.)

**F** Group exemption number (See instructions.)

**G** Check organization type:  501(c) corporation  501(c) trust  401(a) trust  Other trust

**H** Describe the organization's primary unrelated business activity.

**I** During the tax year, was the corporation a subsidiary in an affiliated group or a parent-subsidiary controlled group?  Yes  No. If "Yes," enter the name and identifying number of the parent corporation.

**J** The books are in care of \_\_\_\_\_ Telephone number \_\_\_\_\_

Part I Unrelated Trade or Business Income		(A) Income	(B) Expenses	(C) Net
1a	Gross receipts or sales			
b	Less returns and allowances			
c	Balance			
2	Cost of goods sold (Schedule A, line 7)			
3	Gross profit. Subtract line 2 from line 1c			
4a	Capital gain net income (attach Schedule D)			
b	Net gain (loss) (Form 4797, Part II, line 17) (attach Form 4797)			
c	Capital loss deduction for trusts			
5	Income (loss) from partnerships and S corporations (attach statement)			
6	Rent income (Schedule C)			
7	Unrelated debt-financed income (Schedule E)			
8	Interest, annuities, royalties, and rents from controlled organizations (Schedule F)			
9	Investment income of a section 501(c)(7), (8), or (17) organization (Schedule G)			
10	Exploited exempt activity income (Schedule I)			
11	Advertising income (Schedule J)			
12	Other income (See instructions; attach schedule)			
13	<b>Total.</b> Combine lines 3 through 12			
<b>Part II Deductions Not Taken Elsewhere</b> (See instructions for limitations on deductions.) (Except for contributions, deductions must be directly connected with the unrelated business income.)				
14	Compensation of officers, directors, and trustees (Schedule K)			
15	Salaries and wages			
16	Repairs and maintenance			
17	Bad debts			
18	Interest (attach schedule)			
19	Taxes and licenses			
20	Charitable contributions (See instructions for limitation rules)			
21	Depreciation (attach Form 4562)			
22	Less depreciation claimed on Schedule A and elsewhere on return			
23	Depletion			
24	Contributions to deferred compensation plans			
25	Employee benefit programs			
26	Excess exempt expenses (Schedule I)			
27	Excess readership costs (Schedule J)			
28	Other deductions (attach schedule)			
29	<b>Total deductions.</b> Add lines 14 through 28			
30	Unrelated business taxable income before net operating loss deduction. Subtract line 29 from line 13			
31	Net operating loss deduction (limited to the amount on line 30)			
32	Unrelated business taxable income before specific deduction. Subtract line 31 from line 30			
33	Specific deduction (Generally \$1,000, but see line 33 instructions for exceptions)			
34	<b>Unrelated business taxable income.</b> Subtract line 33 from line 32. If line 33 is greater than line 32, enter the smaller of zero or line 32			

For Paperwork Reduction Act Notice, see instructions. Cat. No. 11201J Form 990-T (2016)



# UBIT CASE STUDIES

- PLR 201630009:
  - Tax Exempt Organization rented real property with personal property equaling 5% of FMV of the rental price. Rental price was not based on net income or profits of the activity.
  - Rent from real property held nontaxable; rental from personal property held incidental and nontaxable
- PLR 201710002:
  - Tax Exempt Organization specialized in data analysis on community issues, the results of which were made freely available to the general public. The organization offered the same technical assistance services to other organizations and provided them based on a sliding scale.
  - Income from the sale of the services was held to be substantially related to the organizations tax exempt purposes



# UBIT CASE STUDIES

- PLR 201645017:
  - Tax Exempt Organization operated a coffee shop in connection to their facilities. The shop was advertised widely and operated in a commercial manner. The profits were used to support the organizations exempt functions.
  - The coffee shop was deemed substantially unrelated to the organization's exempt purposes and held subject to UBIT.
- PLR 201710005:
  - Tax Exempt Organization (Cultural Center) operated coffee shop housed inside the center. There were no exterior doors to the coffee shop nor any external advertising of any kind.
  - As there was no call to non-visitors of the Cultural Center to purchase coffee in any other circumstance than while they happened to be visiting the Center, the activity was held not unrelated to the organizations exempt purpose.





# RESOURCES AND CONTACT INFORMATION

- Tax Services webpage: <http://www.fso.arizona.edu/tax-services>
- Contact information:  
Email: [taxservices@fso.arizona.edu](mailto:taxservices@fso.arizona.edu)  
Direct Line: 520-621-1957
- FSM 20.10: <https://policy.fso.arizona.edu/fsm/2000/2010>
- Research Gateway: <https://rgw.arizona.edu/resources/forms-and-templates>
- Internal Revenue Code including but not limited to §§ 511, 512, 513: <https://www.irs.gov/privacy-disclosure/tax-code-regulations-and-official-guidance>
- Title 26 of the Code of Federal Regulations including but not limited to §§ 1.511, 1.512, and 1.513: <https://www.law.cornell.edu/cfr/text>
- Internal Revenue Service Publication 598: <https://www.irs.gov/forms-instructions>

