



UNRELATED BUSINESS INCOME TAX



Credit Union Executives Society Background

- ◆ **Annual budget approximately \$14,000,000**
- ◆ **Not-for-profit Wisconsin Corporation**
- ◆ **Tax Exempt under IRC section 501 C (6)**
- ◆ **File 990, 990-T and related WI tax forms**
- ◆ **Income Taxes still apply to the following:**
 - **Unrelated Business Income (UBIT)**

Unrelated Business Income Tax

- ◆ Even though an organization is recognized as tax exempt, it still may be liable for tax on its unrelated business income. Unrelated business income is income from a trade or business, regularly carried on, that is not substantially related to the charitable, educational, or other purpose that is the basis of the organization's exemption. An exempt organization that has \$1,000 or more of gross income from an unrelated business must file Form 990-T. An organization must pay estimated tax if it expects its tax for the year to be \$500 or more.

What is UBIT ?

■ **Unrelated Business Income Tax Defined**

- **For most organizations, an activity is an unrelated business (and subject to UBIT) if it meets the three requirements below:**
 - **1) It is a trade or business**
 - **2) It is regularly carried on**
 - **3) It is not substantially related to furthering the exempt purpose of the organization**

Definition of Trade or Business:

◆ "Trade or Business" Defined

- The term *trade or business* generally includes any activity carried on for the production of income from selling goods or performing services. It is not limited integrated aggregates of assets, activities, and goodwill that comprise businesses for purposes of certain other provisions of the Internal Revenue Code. Activities of producing or distributing goods or performing services from which gross income is derived do not lose their identity as trades or businesses merely because they are carried on within a larger framework of other activities that may, or may not, be related to the organization's exempt purposes.

Definition Of “Regularly Carried On”

◆ “Regularly Carried On” Defined

- Business activities of an exempt organization ordinarily are considered *regularly carried on* if they show a frequency and continuity, and are pursued in a manner similar to, comparable commercial activities of nonexempt organizations.

Definition of “Substantially Related”

◆ "Substantially related" defined

- To determine if a business activity is *substantially related* requires examining the relationship between the activities that generate income and the accomplishment of the organization's exempt purpose. Trade or business is related to exempt purposes, in the statutory sense, only when the conduct of the business activities has causal relationship to achieving exempt purposes (other than through the production of income). The causal relationship must be substantial. The activities that generate the income must contribute importantly to accomplishing the organization's exempt purposes to be substantially related.

Exceptions to UBIT per IRS

- ◆ There are a number of modifications, exceptions and exclusions to the general definition of UBIT.
 - **Volunteer Labor:** Any trade or business is excluded in which substantially all the work is performed for the organization without compensation. Some fundraising activities, such as volunteer operated bake sales, may meet this exception.
 - **Convenience of Members:** Any trade or business is excluded that is carried on by an organization described in section 501(c)(3) or by a governmental college or university primarily for the convenience of its members, students, patients, officers, or employees. A typical example of this is a school cafeteria.
 - **Selling Donated Merchandise:** Any trade or business is excluded that consists of selling merchandise, substantially all of which the organization received as gifts or contributions. Many thrift shop operations of exempt organizations would meet this exception

What Does This Mean To CUES?

- **Example: Advertising Revenue**
 - Revenue for ads in Magazine
 - No relationship to CUES reason for Tax Exempt status
 - Not related to Professional Development
- **Example: Sponsorship Revenue**
 - Avoid key terms
 - Exclusive
 - Support
 - Recommend
 - Remain “middle of the road” and non-committal
- **Contracts with 3rd Parties**
 - Avoid “exclusive” terminology in any arrangements with the context of the contract

The Bottom Line...

- **Up to 25% of Income from UBIT**
 - <25% - OK
 - >25% - Risk loss of tax exemption
 - Tax Rate = 34% ?
- **More scrutiny from IRS**
 - Publication 598
 - <http://www.irs.gov/pub/irs-pdf/p598.pdf>
- **See your own Tax Attorney or Accountant**