Association of American Universities
Inquiry · Innovation · Impact

Unrelated Business Income Tax (UBIT)

Internal Revenue Code Sections 511-514

What is Unrelated Business Income Tax?

The Unrelated Business Income Tax (UBIT) was enacted in 1950 to ensure that tax-exempt entities do not unfairly compete with taxable companies in profit-generating activities.

UBIT is income from a trade or business that is regularly carried on by a tax-exempt organization and is not substantially related to the organization's exempt purpose.

UBIT does not include the following income:

- dividends;
- interest;
- certain research income;
- royalties; and
- certain rents (unless derived from debt-financed property or, in some cases, from 50 percent controlled subsidiaries).

Other exemptions are provided for:

- activities in which substantially all the work is performed by volunteers;
- income from the sale of donated goods; and
- certain activities carried on for the convenience of members, students, patients, officers, or employees of a charitable organization.

Tax-exempt entities that are subject to the unrelated business income tax and that have $1,000 or more of gross unrelated business taxable income are required to report that income to the IRS on Form 990-T. Tax-exempt entities with UBIT liability may also be liable for alternative minimum tax.

Part I	Unrelated Trade or Business Income
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), (9), 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	**Total.** Combine lines 3 through 12

Examples of How UBIT Applies in Specific Income-Generating Activities of Tax-Exempt Entities

Debt-financed property

In general, income that is produced by debt-financed property is treated as unrelated business income in proportion to the acquisition indebtedness on the income-producing property. Special rules apply for acquisition indebtedness incurred in the performance or exercise of a purpose or function constituting the basis of the organization's exemption. Special rules also apply in the case of an exempt organization that owns a partnership interest in a partnership that holds debt-financed income-producing property. An exempt organization's share of partnership income that is derived from such debt-financed property generally is taxed as debt-financed income unless an exception provides otherwise.

Unrelated Income Business Tax (UBIT)

continued

Treatment of income from controlled entities

Section 512(b)(13) provides special rules regarding income derived by an exempt organization from a controlled subsidiary. The general rule treats otherwise excluded rent, royalty, annuity, and interest income as unrelated business income if such income is received from a taxable or tax-exempt subsidiary that is more than 50 percent controlled by the parent tax-exempt organization (to the extent the payment reduces the net unrelated income or increases any net unrelated loss of the controlled entity determined as if the entity were tax-exempt).

Corporate sponsorship

Section 513(i) distinguishes sponsorship payments for which the donor receives no substantial return benefit other than the use or acknowledgment of the donor's name or logo as part of a sponsored event from payments made in exchange for advertising provided by the recipient organization. The latter, but not the former, are subject to UBIT.

UBIT and Universities and Colleges

Although universities and colleges are tax-exempt entities, they are subject to tax on any unrelated business taxable income they may generate.

Recurring UBIT issues for universities include:

1. determining whether a particular activity is educational in nature, and therefore, qualifies for tax-exempt treatment; and
2. determining whether a non-educational activity is exempt from the unrelated business income tax because income from the activity fits within a statutory exemption.

Two examples of university income-generating activities that are subject to UBIT are: 1) income from sales of non-educational materials such as clothing and gift items by a campus bookstore; and 2) industry sponsored research if the results are not made available to the public or directed toward benefiting the public.

2017 Tax Law Implications

The Tax Cuts and Jobs Act (TCJA) increased an institution's UBIT for certain fringe benefit expenses including taxing transportation and parking benefits to 21 percent. It also imposed new UBIT "basketing" provisions that requires institutions to separately compute UBIT for each "trade or business" conducted. The basketing rules require that all losses and gains be calculated by activity rather than in the aggregate for determining UBIT. Universities should pay taxes on business activities *unrelated* to their charitable missions, but the basketing requirement imposes cumbersome tax accounting rules that do not apply to any other sector or industry.

Additional Information

IRS Publication 598

"Tax on Unrelated Business Income of Exempt Organizations"

http://www.irs.gov/pub/irs-pdf/p598.pdf