UNRELATED BUSINESS TAXABLE INCOME

Overview
Unrelated Business Taxable Income

• UBTI is the gross income derived by an tax-exempt organization from an unrelated trade or business regularly carried on, less allowable deductions connected with the trade or business.

• An activity is an unrelated trade or business if:
  – Activity constitutes a trade or business;
  – Activity is regularly carried on; and
  – Activity is not substantially related to the organization’s exempt purpose.

• Certain modifications and exclusions apply.
Definition of Trade or Business:

- The definition of the term “trade or business” refers to any activity that is carried on for the production of income, from the sale of goods, or from the performance of services.

- The IRS generally considers a trade or business to be any venture motivated by the desire to earn a profit as any other commercial venture.
Definition of Regularly Carried On

- The term “regularly carried on” refers to the frequency and continuity of the business activity as well as the manner in which it’s conducted.

- Even when the activity is not conducted year round, it may be deemed regularly carried on if for-profits conduct comparable activities with the same frequency and continuity.

- The regular activity can be seasonal or intermittent.
Definition of Substantially Related

The third factor is that the activity not be “substantially related” to the tax-exempt organization’s exempt purpose. To determine whether the activity is substantially related requires examining the relationship between the activities that generate income and the accomplishment of the organization’s exempt purpose.
Common Sources of UBI

- Laboratory Services
- Research Activities
- Rental of real estate when income is based upon net profits
- Rent of tangible personal property
- Income from certain alternative investments
- Private business use of tax-exempt bond financed facilities
- Museum / Hospital Gift Shop
- Child Care
- Catering
- Printing or audio visual sales and services
- Parking
- Retail sales
- Advertising income
- Consulting Services
Examples of Exclusions from UBTI

- Passive income such as dividends, interest, annuities, and royalties where no active business participation and management is involved;
- Rental income from real property
- Income generated from donated services or property;
- Income produced from sales made primarily for the convenience of the organization's members, students, and employees (including faculty and staff); and
- Income from services provided by volunteer labor
- Qualified sponsorship payment
Taxation on UBI

- UBIT is imposed on the net taxable income of the unrelated business activity. (gross income less related expenses)

- Unrelated Business Income is subject to Federal, State and Philadelphia corporate income taxes.
  - The federal tax rate is a graduated rate with a max of 35%
  - Certain states, such as Pennsylvania, do not tax UBI
    - (the rates vary by state)
  - There are two rates for Philadelphia
    - Income tax at 6.39% and gross receipts tax at .1415%

- Purchases of expense items for unrelated business activity are subject to the 8% PA/Phila sales tax.
UBI Activity Losses

- If the unrelated business activity does not generate a profit in three out of five years, it is viewed as a “Hobby Loss” and will not included in the UBIT calculation.

- The year that a hobby loss activity becomes profitable, it will be included in the UBIT calculation.
Reporting Responsibility

• 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.

• UBIT questionnaires and income tax worksheets are emailed to the University/Health System communities during the month of September.

• The questionnaires and worksheets must be completed and emailed to the Tax Office during November.

• Certifications are emailed to the Sr. Business Officer to confirm that the information reported is accurate.