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## Recent Developments in College and University Tax Law

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## **RECENT DEVELOPMENTS IN COLLEGE AND UNIVERSITY TAX LAW**

### **I. Overview of College/University-Related Provisions in 2017 Tax Reform Legislation**

A. On December 22, 2017, the President signed the 2017 tax reform legislation, commonly referred to as the Tax Cut and Jobs Act. The TCJA substantially changed the Internal Revenue Code by lowering tax rates on wages, investment, and business income; broadening the tax base; and simplifying many provisions of the tax code. It also contained a number of provisions that impacted tax-exempt organizations generally and colleges and universities more specifically.

B. Attached is a KPMG-prepared summary of those aspects of the tax bill impacting institutions of higher education.

### **II. Unrelated Business Income Tax Developments**

#### **A. Courts Address “Engaged in For Profit” Test**

1. In *Losantiville v. Commissioner*, T.C. Memo. 2017-158, the Tax Court (i) said that the section 183 profit motive factors are not applicable in determining whether a tax-exempt organization engaged in a loss activity with the intent to make a profit, and (ii) citing the Supreme Court’s *Portland Golf* case, seemed to say that the organization had to actually make a profit in order to demonstrate an intent to do so. The taxpayer has appealed this decision to the Sixth Circuit, and a decision in that appeal is currently pending. A copy of this case can be found at <https://www.ustaxcourt.gov/UstcInOp/OpinionViewer.aspx?ID=11364>.
2. In *Wicks v. U.S.*, 121 AFTR 2d 2018-515 (DC OK 2018), a federal district court refused to hold that a couple’s cattle ranching activity was not engaged in for profit after applying the various profit-motive factors set forth in Treas. Reg. § 1.183-2(b). A copy of this decision is not online. If you would like a copy, please send an email to [bharding20@verizon.net](mailto:bharding20@verizon.net) with Wicks Case in the Subject line.
3. In *Ford v. Commissioner*, T.C. Memo. 2018-8, the Tax Court, using the same factors set forth in the regulations as well as certain others, held that the taxpayer did not operate a night club with the intent to earn a profit. A copy of this case can be found at <https://www.ustaxcourt.gov/ustcinop/OpinionViewer.aspx?ID=11564>.
4. In *Welch v. Commissioner*, T.C. Memo. 2017-229, the taxpayer incurred losses for all of the years at issue (2007-2010), but the Court, after applying the section 183 factors profit-motive factors, nevertheless found

that the taxpayer engaged in the activity with the intent to earn a profit. The Court also addressed the question of whether the taxpayer's cattle, hay, and horse operations should be treated as a single trade or business or as multiple business activities, finding that they were one, integrated business. A copy of this case can be found at <https://www.ustaxcourt.gov/ustcinop/OpinionViewer.aspx?ID=11462>.

B. IRS "Snapshot" Guidance on Rental Income Exception and Unrelated Debt-Financed Income

In two "Snapshot" guidance items, the IRS describes and discusses:

1. The section 512(b)(3) rental income exception. See <https://www.irs.gov/charities-non-profits/rents-from-personal-property-mixed-leases-and-the-rental-exclusion-from-ubti> and <https://www.irs.gov/charities-non-profits/exclusion-of-rent-from-real-property-from-unrelated-business-taxable-income>, and
2. The section 513 unrelated debt-financed income provisions. See <https://www.irs.gov/charities-non-profits/unrelated-business-income-from-debt-financed-property-under-irc-section-514>.

C. Tax Court Case Impacting Definition of Royalties and Convenience Exception

The New Jersey Council of Teaching Hospitals is a section 501(c)(3) organization that acts as a supporting organization with respect to its member hospitals and medical schools. It entered into an agreement with certain third-party vendors to provide debt collection, group purchasing, and other services for its members. The Council received fees from the vendors in return for promoting these programs to its members. The IRS said that the fees were unrelated business income but the organization argued that they were exempt from tax either as royalties under section 512(b)(2) or under the convenience exception in section 513(a)(2).

In *New Jersey Council of Teaching Hospitals v. Commissioner*, 149 T.C. No. 22 (2017), the Tax Court rejected both arguments. It said that a royalty is a payment for a valuable intangible property right and that in the Council's "service agreements" with the service providers there were no provisions whereby the Council licensed the use of its intangible property; therefore, the Court was required to assume that the payments by the vendors were in return for services rendered. And the convenience exception, the Court said, was not applicable because that provision only applies when the activity in question benefits the member, student, patient, officer, or employee in their capacity as such. Here, while the services might benefit the hospital and medical school members in their operational capacities, it did not benefit them in their capacity as members of the Council. A copy of this case can be found at <https://www.ustaxcourt.gov/UstcInOp/OpinionViewer.aspx?ID=11521>.

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