

BakerHostetler



The University of Texas at Austin

Accounting and Financial Management

Technical UBTI Session: Rent, License or Services – What is it Really for Tax Purposes?

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Objectives

- Discuss the many issues that an institution may face when departments submit a purported lease, license, or services agreement with multiple components.
- Is it a related lease?
- Does it qualify for the Rental Exclusion?
- Is it a license, and what are the implications - distinguishing royalties from rents and services income?
- Does it involve personal property or services?
- And what about debt financing?
- Also take a look at book UBI that was brought to life by the Inflation Reduction Act.

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UBIT Background

- Prior to 1950, all income destined for charitable purposes was not subject to federal tax. (Destination of Income Test)
- In 1950, after cries from for-profit businesses about unfair competition Congress enacted new federal income tax regime (i.e. UBIT) for tax-exempt entities. (NYU Macaroni Case)
- Revenue Act of 1951 expanded scope of UBIT to include public colleges and universities. (UT now subject to UBIT)

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What is UBIT?

- Unrelated business income is defined as “gross income derived by any organization from any unrelated trade or business that is regularly carried on”
 - Trade or Business
 - Regularly Carried On
 - Not Substantially Related to Exempt Purpose
 - **ALL THE ABOVE ARE QUESTIONS OF FACT

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Trade or Business

- Trade or business is any activity carried on for the production of income.
- At some point, an activity must produce a profit to be considered a trade or business. (Hobby Loss Rule)

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Regularly Carried On

- To determine if a trade or business is regularly carried on, the IRS generally compares the time span for a comparable commercial activity to that for the activity conducted by a university.
- Activities engaged in only discontinuously or periodically are not regularly carried on so long as no competitive and promotional efforts typical of commercial endeavors.
- Activities lasting only a short period of time on an annual basis would not be considered regularly carried on.
- NCAA Case: it was held that preparatory time not included in determining whether activity was regularly carried on. Length of tournament (3 weeks), despite months of preparatory time, was dispositive of question concerning whether activity was regularly carried on.

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