

Unrelated Business Income Reporting Guidelines

Each fiscal year, the university is required to file an Exempt Organization Business Income Tax Return (Form 990-T) with the Internal Revenue Service. This filing reports any unrelated business income generated by the activities of the university's academic and support units. The Internal Revenue Code states that a college or university is generally deemed to have unrelated business taxable income (UBI) when it realizes income from any regularly conducted trade or business that is not substantially related to its exempt purposes. It is very important that all unrelated business activities of the university are reported on the federal tax return. The Internal Revenue Service can and will assess costly penalties and interest charges for underpayment of taxes.

Unrelated business income tax analysis can be complex requiring significant review of all specific facts to properly determine whether or not the activity may generate UBI and a tax liability for the university. If you think you have or plan to start an activity that may result in UBI please contact the Barbara Starling, starlibs@vt.edu, or Dave McGarry, mcgarrde@vt.edu at the Controller's Office to discuss the specifics of the planned or on-going activity.

As mentioned above an activity may be considered an unrelated trade or business if its operations meet **all** the criteria listed below.

- Trade or Business

The term "trade or business" generally includes any activity carried on for the production of income from selling goods or performing services. A trade or business activity is one in which a profit is expected to be made. However, when an activity that is carried on for a profit incurs a loss, no part of the trade or business is excluded from the for profit classification merely because its current operations does not result in a profit in a particular year. In addition, an activity does not lose its identity as a trade or business when it is carried on within a larger complex of other endeavors which may be related to the exempt purposes of the university.

- Regularly Carried On

The trade or business must also be considered "regularly carried on ". This test considers the frequency, continuity of operations and the manner in which the activities are conducted. Comparisons of the university activity must be made with similar commercial activities to arrive at a determination whether the activity may be taxable.

- Not substantially Related to Exempt Purposes

A regularly conducted trade or business is subject to tax if it is also **not** substantially related to the exercise or performance of the exempt functions of the university. The university's need for the income from the activity to further its exempt activities does not change the taxable nature of the income produced from the unrelated activity.

Unrelated business income can be generated from a large variety of university activities. Currently the university reports taxable income as a result of operations from the Electric Service, Inn at VT and Skelton Conference Center, Personal Touch Catering, Tailor Shop, Burrows-Burleson Tennis Center, Golf Course and Athletic Sponsorship agreements. As a general rule, providing goods or services to the public (alumni is included in this category) is considered a taxable activity. Other examples of activities that would most likely generate UBI are:

- Most forms of advertizing that generate revenue for the university
- Rental or sales of mailing lists
- Routine analytical or testing services to non-university users
- Travel tours for alumni or tour purpose is not authentic educational activity
- Renting equipment to non-university personnel
- Excess Computer time sold to an outside company
- On-line stores linked to university web sites
- Printing or audio visual sales and services to non-university users
- Parking revenues generated from general public attendance at a non-university sponsored event

In addition to the activity itself, consideration must be given to where the activity is conducted. If any portion of a property, whose construction was financed with tax-exempt bonds, is used to conduct unrelated business activities, the bond financing could lose its tax exempt status. The percentage of unrelated activity taking place on the property must be monitored to insure the overall use of the facility by exempt activities is sufficient to prevent challenges to the tax-exempt status of the property's financing.

There are specific activities identified in the federal tax law which are exempted from unrelated business income tax even though they may otherwise have the characteristics of an unrelated trade or business.

- Real Property rents

Rent collected from outside entities is considered passive and not subject to UBIT. However, the exclusion may be **lost** if personal services or use of equipment are included in the rental agreement.

- Income from Research Activities

In general, revenue received from research activities is excluded from unrelated business income. There are certain situations that may require further analysis to determine if they fit the research exception. For example, ordinary testing and inspection of products or materials is normally **not** exempt from UBI.

- Member Convenience Activities

An unrelated activity conducted by the university for the benefit of its members (students, faculty, and staff) is not subject to tax unless the income is generated from sales to non-members. In this case only the non-member generated income is taxable

- Dividends, Interest, Annuities, and Royalties

These sources of income are considered passive and are generally excluded from UBI. However, consideration must be given to the investment generating the income before a determination to exclude from UBI. Investments in controlled organizations, partnerships, "S" Corporations, etc. will generally result in UBI.

Addition information on UBI can be found in IRS Publication 598 – Tax on Unrelated Business Income of Exempt Organizations at the following web address.

<http://www.irs.gov/publications/p598/index.html>