

## Unrelated Business Income Tax (UBIT)

Even a tax-exempt educational organization such as UCSF is taxed on its unrelated business taxable income (UBI). There are two types of unrelated business taxable income:

- Income arising from the conduct of unrelated trade or business that is regularly carried on, and
- Debt-financed income, which is usually in the form of rent, interest or royalties arising from financed property

The latter type of taxable income is rare at UCSF, because our transactions generally fit within the exceptions to the debt-financed income rules.

### What is a trade or business?

It is any activity carried on to produce income from the sale of goods or performance of services. Generally we look at:

1. whether the activity generates a profit, or
2. whether it is conducted in the same manner as a for-profit business that provides a similar good or service

Some UBI-generating activities show profits in some years and losses in others, so an activity does not always have to generate a profit in order to be considered UBI. We review the facts and circumstances surrounding each activity at UCSF in determining whether a particular activity is a trade or business.

#### EXAMPLES:

The regular sale of pharmaceutical supplies to the general public by a hospital pharmacy does not lose its identity as a trade or business, even though that pharmacy also provides supplies and medicines to the hospital and its patients in furtherance of the hospital's exempt purpose. Sales to hospital patients would be exempt from UBI, but sales to others would generally be taxable.

Soliciting, selling and publishing commercial advertising is a trade or business even though the advertising is published in a periodical published by a university that predominantly contains printed material that is related the university's exempt purpose, such as scientific findings.

### What does it mean to be regularly carried on?

It means that the exempt organization conducts the activity with the same frequency and continuity, and in a similar manner, as a for-profit organization would conduct a comparable activity.

#### EXAMPLES:

Operating a commercial parking lot every Saturday, year-round, would be the regular conduct of a trade or business.

An auxiliary operation of a sandwich stand for two weeks at a state fair would not be the regular conduct of a trade or business. The stand would not compete with similar facilities that a nonexempt organization would ordinarily operate year-round.

## **How is an activity characterized as not being substantially related to UCSF's exempt purpose?**

UCSF's exempt purposes are patient care, education and research, so an activity whose purpose is not substantially related to one of those purposes would be characterized as unrelated. It is irrelevant that the proceeds from an activity are used to fund education or research. The determining factor is the nature of the activity itself.

## **What are the exceptions to characterizing an activity as UBI-generating that typically apply to activities here at UCSF?**

### **Activities for the Convenience of the University**

Revenue from an activity conducted for the convenience of UCSF faculty, staff, and/or students in connection with their respective roles does not generate UBI.

#### **EXAMPLE:**

If the university offered a laundry service to its students, such a business is considered related.

### **Research Exception**

In general, revenue received by UCSF from research is excluded from UBI. There are certain situations, however, that require further analysis to determine whether or not they fit within the research exception. For example, commercial research and development for a for-profit sponsor would require closer scrutiny to determine whether or not the activity fits within the exception.

### **Passive Investment Income**

(Such as interest, annuities, rents from real property and royalties)

These types of income are generally not treated as UBI-generating. They do become taxable entirely or in part, however, if:

- provision of substantial services is part of the overall arrangement, so that the income is not wholly passive income
- the amount of the payment is based on a percentage of the payer's profits or income; or
- the underlying property generating the income is debt-financed and the transaction falls outside one of the debt-financed income exceptions

**Note:** There is no equivalent exclusion for the rental of personal property, which generates taxable income if the rental activity meets the definition of UBI.

### **Qualified Sponsorship Payment Exception**

When a donor makes cash or in-kind contributions to UCSF and the donor's name and logo are merely acknowledged in a printed program or other University literature or on a building, no UBI is generated.

- If a contribution is contingent on the donor receiving a financial benefit (known as a substantial return benefit) equal to more than 2% of the contribution, however, we need to assess whether the transaction fits within the qualified sponsorship payment exception or another exclusion from UBI

### **EXAMPLES:**

Messages containing qualitative or comparative language, price information or other indications of savings or value

Endorsements

Inducements to purchase, sell or use the products or services

- Regulations in this area suggest that some of the UBI-generating arrangements tend to look like advertising or exclusive provider arrangements, but other situations can also raise questions.
- Qualified sponsorship analysis focuses on arrangements that appear to be business transactions with a donor and, for example, would not include the mere establishment of a charitable remainder trust or charitable annuity trust

### **Volunteer Exception**

Revenue generated from an activity where substantially all the work is performed by volunteers does not generate UBI.

### **Who files the tax returns and pays the tax?**

University of California, Office of the President, Financial Management calculates UBI centrally and reports all resulting profit and loss annually on UC's Form 990-T.

Tax paid on UBI (the tax is sometimes referred to as UBIT) is then allocated among the Campuses generating UBI, based upon the respective amounts of UBI generated by each Campus during the fiscal year for which the return is filed.

### **How does UCSF's Tax Services identify UBI?**

- Information from the Office of the General Counsel
- Information from the Budget Office recharge
- Articles in various University publications
- Information received from Department Administrators, utilizing the **UBIT questionnaire**
- General Ledger

In a decentralized environment such as UCSF we use several approaches, including regular communication with a network of financial administrators in departments across the University, who call Tax Services when they believe they have identified a potential UBI-generating activity in their own department. We very much appreciate everyone's valuable input in helping the University to meet its tax compliance responsibilities.

UBI analysis is complex and requires significant review of specific facts to properly determine whether or not an activity in your department might generate UBI or whether a particular exception applies to your facts. Please refer to the Controller's Office **Tax Contacts** to discuss the particular situation in your department if you believe your department may be engaged in a UBI-generating activity.