

## ALL DISTRICTS AND CLUBS SUBJECT TO USA TAX LAWS

RE: UNRELATED BUSINESS INCOME TAX (UBIT)

The existing provisions concerning liability for "unrelated business income" tax were made applicable to organizations exempt under Section 501(c)(4) of the 1986 Internal Revenue Code. Districts and clubs are exempt under this section. This is a tax on income realized from an unrelated "trade or business" regularly carried on by such exempt organizations. If a district or club has "unrelated business income," it may be liable for payment of this tax. The effect of these provisions on the normal fundraising activities of districts and clubs may be summarized, generally as follows:

- A) Definition of Unrelated Business Income. By definition, the term "unrelated business income" does **not** include:
- 1) Income in the form of dividends or interest (unless received from an entity legally separate from but controlled by the district or club);
  - 2) Income in the form of rentals from real property (unless received from an entity legally separate from but controlled by the district or club, or from a lease for more than five years of property subject to or related to an indebtedness). However, if a lease is for five years or less, it may not be subject to U.B.I.T.);
  - 3) Income in the form of rentals of personal property leased with real property if the rent from the personal property is an incidental amount. An incidental amount is 10% or less of the total rents under a lease;
  - 4) Income from a trade or business in which substantially all the work done in the business operation is done without compensation, i.e. by volunteer help;
  - 5) Income from a trade or business which sells merchandise, substantially all of which is donated;
  - 6) Income from a trade or business which is not "regularly carried on;"
  - 7) Income from conduct of bingo games which are not ordinarily carried out on a commercial basis and do not violate any state or local law.
- B) The ordinary fundraising activity of a district or Lions club is considered to be a trade or business within these provisions. The question then is whether it falls within one of the aforesaid categories. If it is not "regularly carried on," or is run substantially by volunteer

help, or consists substantially of the sale of "donated" merchandise, then the income realized therefrom will not be subject to the "unrelated business income" tax.

With respect to the phrase "regularly carried on" and intermittent fundraising activities, the regulations state the following:

Income producing or fundraising activities lasting only a short period of time will not ordinarily be treated as regularly carried on if they recur only occasionally or sporadically. Furthermore, such activities will not be regarded as regularly carried on merely because they are conducted on an annual recurrent basis. Accordingly, income derived from the conduct of an annual dance or similar fundraising event for charity would not be income from a trade or business "regularly carried on." Reg. Sec. 1.513-1(c).

**Thus, the income realized in the normal fundraising activity of a district or club** (a dance; horse show; sale of lightbulbs, candy, brooms, raffle tickets, etc.; concert; play; style show; car or snowmobile race; sporting event; turkey shoot; etc.) is not "unrelated business income."

However, if a district or club carried on an income producing activity (other than rental of property as above described) which:

- (1) Runs for the length of a "season" (such as horse racing) during which such an income producing activity would normally be run; or
  - (2) Operates on a regular basis throughout a fiscal year, i.e. in a manner similar to a comparable trade or business of a commercial enterprise (such as operating a parking lot one day each week or a restaurant open to the public on a regular basis throughout the year, etc.), then the respective district or club will have "unrelated business income" with respect to such activity and may be liable for the tax imposed thereon. Any district or club in this situation should consult a qualified local attorney or accountant to determine any tax liability it may have.
- (C) Each district and club must file, annually, an Information Return known as Form 990EZ or Form 990 if it meets the criteria discussed in the preceding letter. In addition, each district or club which has gross "unrelated business income" of \$1,000 or more must also file Form 990-T (this is an income tax return and not merely an information return). If the gross "unrelated business income" in the taxable year is \$25,000 or less, some detailed portions of Form 990-T need not be completed. You should consult the form itself in this regard.

It can be seen from the above that most districts and clubs will have no involvement with the "unrelated business income" tax or Form 990-T.

If you have any specific questions, please contact the Legal Division.