

Publication 598

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Tax on Unrelated Business Income of Exempt Organizations

Volume 1 of 3



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Future Developments

The IRS has created a page on IRS.gov for information about Pub. 598, at [IRS.gov/Pub598](https://www.irs.gov/pub598). Information about any future developments affecting Pub. 598 (such as legislation enacted after we release it) will be posted on that page.

What's New

- Mandatory electronic filing. Section 3101 of the Taxpayer First Act, (P.L. 116-25) requires tax-exempt organizations to electronically file information returns and related forms. This law affects tax-exempt organizations in tax years beginning after July 1, 2019. In 2020, the IRS continued to accept paper Forms 990-T pending conversion into electronic format. In 2021, the Form 990-T is being updated and e-filing is required for tax year 2020 filings. The IRS expects e-filing to be available beginning in February 2021. The IRS will

announce the specific dates when the programming comes online. See the Instructions for Form 990-T, *When, Where, and How To File*, for more information.

- Final regulations issued. Section 512(a)(6) requires a tax-exempt organization with more than one unrelated trade or business to compute unrelated business taxable income (UBTI), including any NOL deduction, separately for each trade or business. Final regulations were published in the Federal Register on December 2, 2020, that provide guidance on how an exempt organization determines if it has more than one unrelated trade or business, and, if so, how the exempt organization calculates unrelated business taxable income. T.D. 9933, 85 Fed. Reg. 77952 (Dec. 2, 2020). The final regulations are applicable to tax years beginning on or after December 2, 2020.

In addition, an exempt organization may choose to apply the final regulations under section 512(a) (6) to tax years beginning on or after January 1, 2018, and before December 2, 2020. Alternatively, an exempt organization may rely on a reasonable, good-faith interpretation of section 512(a) (6) for such tax years. For this purpose, a reasonable good faith interpretation includes the methods of aggregating or identifying separate trades or businesses provided in Notice 2018-67 or the proposed regulations published April 24, 2020 (85 Fed. Reg. 23172). See T.D. 9933 for more details.

- Form 990-T has been redesigned for tax year 2020. Schedule M (Form 990-T) has been replaced with Schedule A. Each unrelated trade or business of an organization is reported on a separate Schedule A. At the organization's discretion, each separate trade or

business may be classified by a 2-digit North American Industrial Classification System (NAICS) code. See Regulations section 1.512(a)-6(b)(1). The Instructions for Form 990-T provide 6-digit Business Activity Codes for investment and other activities not represented in NAICS.

- Organizations with more than one unrelated trade or business must compute unrelated business taxable income (UBTI), including for the purpose of determining any net operating loss deduction, separately with respect to each such trade or business. See Regulations section 1.512(a)-6 for more information.
- Retroactive repeal of section 512(a)(7). P.L. 116-94 retroactively repealed the section 512(a)(7), which required exempt organizations to increase their unrelated business taxable income for expenses incurred to provide certain benefits, including qualified transportation fringes.

If your organization reported and paid tax on such amounts included in unrelated business taxable income for tax years 2017 or 2018 and you want to claim a refund, file an amended Form 990-T.

- Net operating loss (NOL) carryback. The Coronavirus Aid, Relief, and Economic Security Act (CARES Act) amended section 172 provides for carryback of any net operating loss arising in a tax year beginning after 2017 and before 2021 to each of the 5 tax years preceding the tax year of the NOL. Taxpayers may elect to waive the carryback period for NOLs arising in those years. To elect to waive the carryback period for an NOL arising in a tax year beginning in 2018 or 2019, attach a statement electing the carryback waiver to your return for the first tax year ending after March 27, 2020. For more information, see Rev. Proc. 2020-24. If you incurred an NOL in a tax year

beginning in 2018 or 2019, you can file an amended return, Form 990-T, to carryback the NOL. See Pub. 536 for more information.

- The maximum cost of a low-cost article, for organizations eligible to receive charitable contributions, was increased to \$11.20 for 2020. See *Distribution of low-cost articles*, later.
- The annual limit on associate member dues received by an agricultural or horticultural organization not treated as gross income was increased to \$171 for 2020. See *Exception* under *Dues of Agricultural Organizations and Business Leagues*, later.

Introduction

An exempt organization isn't taxed on its income from an activity substantially related to the charitable, educational, or other purpose that is the basis for the

organization's exemption. Such income is exempt even if the activity is a trade or business.

However, if an exempt organization regularly carries on one or more trades or businesses not substantially related to the organization's exempt purpose, except that conducting the trade or business provides funds to carry out the exempt purpose, the organization is subject to tax on its income from the unrelated trade(s) or business(es).

This publication covers the rules for the tax on unrelated business income of exempt organizations. It explains:

1. Which organizations are subject to the tax (chapter 1),
2. What the requirements are for filing a tax return (chapter 2),
3. What an unrelated trade or business is (chapter 3), and

4. How to figure unrelated business taxable income (chapter 4).

All section references in this publication are to the Internal Revenue Code.

Useful Items

You may want to see:

Publication

- ☐ **557** Tax-Exempt Status for Your Organization

Form (and Instructions)

- ☐ **990-T** Exempt Organization Business Income Tax Return
- ☐ **Schedule A (990-T)** Unrelated Business Taxable Income From an Unrelated Trade or Business

Visit [IRS.gov/FormsPubs](https://www.irs.gov/forms-pubs) to download forms and publications. Otherwise, you can go to [IRS.gov/OrderForms](https://www.irs.gov/orderforms) to order current and

prior-year forms and instructions. Your order should arrive within 10 business days.

Comments and suggestions. We welcome your comments about this publication and your suggestions for future editions.

You can send us comments through [IRS.gov/FormComments](https://www.irs.gov/FormComments). Or you can write to:

Internal Revenue Service
Tax Forms and Publications
1111 Constitution Ave. NW, IR-6526
Washington, DC 20224

Although we can't respond individually to each comment received, we do appreciate your feedback and will consider your comments as we revise our tax products.

Tax questions. If you have tax questions not answered by the publication, check IRS.gov and *How To Get Tax Help* at the end of this publication.

1.

Organizations Subject to the Tax

The tax on unrelated business income applies to most organizations exempt from tax under section 501(a). These organizations include charitable, religious, scientific, and other organizations described in section 501(c), as well as employees' trusts forming part of pension, profit-sharing, and stock bonus plans described in section 401(a).

In addition, the following are subject to the tax on unrelated business income.

- Individual retirement arrangements (IRAs), including traditional IRAs, Roth IRAs, simplified employee pensions (SEP-IRAs), and savings incentive match plans for employees (SIMPLE IRAs).

- State and municipal colleges and universities.
- Qualified state tuition programs described in section 529.
- Qualified ABLE programs described in section 529A.
- Medical savings accounts (MSAs) described in section 220(d).
- Coverdell savings accounts described in section 530.

U.S. instrumentalities. A corporation that is a U.S. instrumentality described in section 501(c) (1) isn't subject to the tax on unrelated business income if the corporation is organized under an Act of Congress and, under the Act, is exempt from federal income taxes.

Colleges and universities. Colleges and universities that are agencies or instrumentalities of any government or any

political subdivision of a government, or that are owned or operated by a government or political subdivision of a government, are subject to the tax on unrelated business income. As used here, the word “government” includes any foreign government (to the extent not contrary to a treaty) and all domestic governments (the United States and any of its possessions, any state, and the District of Columbia).

The tax is on the unrelated business income of both the universities and colleges themselves and on their wholly owned or controlled tax exempt subsidiary organizations. It is immaterial whether the business is conducted by the university or by a separately incorporated wholly owned or controlled subsidiary. If the business activity is unrelated, the income in both instances will be subject to the tax. If the primary purpose of a wholly owned or controlled subsidiary is to operate or conduct any unrelated trade or

business (other than holding title to property and collecting income from it), the subsidiary isn't an exempt organization, and this rule doesn't apply.

Title-holding corporations. When an exempt title-holding corporation, described in section 501(c)(2), pays any of its net income to an organization that itself is exempt from tax under section 501(a) (or would pay such an amount except that the expenses of collecting its income exceed the amount collected) and files a consolidated return with that organization, the title-holding corporation is treated, for unrelated business income tax purposes, as organized and operated for the same purposes as the exempt payee organization.

Thus, a title-holding corporation whose source of income is related to the exempt purposes of the payee organization isn't subject to the unrelated business income tax if the holding corporation and the payee organization file a

consolidated return. However, if the source of the income isn't so related, the title-holding corporation is subject to unrelated business income tax.

Example. X, a title-holding corporation, is required to distribute its net income to A, an exempt organization. During the tax year, X realizes net income of \$900,000 from source M, which is related to A's exempt function. X also receives \$100,000 from source N, which isn't related to A's exempt function. X and A file a consolidated return for the tax year. X has unrelated business income of \$100,000.

2.

The Tax and Filing Requirements

All organizations subject to the tax on unrelated business income, except the exempt trusts described in section 511(b)(2), are taxable at corporate rates on that income.

All exempt trusts subject to the tax on unrelated business income that, if not exempt, would be taxable as trusts are taxable at trust rates on that income.

However, an exempt trust may not claim the deduction for a personal exemption that is normally allowed to a trust.

The tax is imposed on the organization's unrelated business taxable income (UBTI) (described in chapter 4). Under section 512(a)(6), an organization that conducts more than one unrelated trade or business calculates its UBTI as the sum of the UBTI calculated separately for each unrelated trade or business, and when calculating this sum, the UBTI from any of the separate trades or businesses can't be less than zero. The tax computed on the total UBTI can be reduced by any applicable tax credits, including the general business credits (such as the investment credit) and the foreign tax credit.

Returns and Filing Requirements

Mandatory electronic filing of Form 990-T started in February 2021. Limited exceptions apply. See the Instructions for Form 990-T for more information. The obligation to file Form 990-T is in addition to the obligation to file any other required return or notice.

Form 990-T is required if the sum of the organization's gross income from all unrelated businesses is \$1,000 or more. An exempt organization files a single Form 990-T. The organization reports the income and expenses for each of its unrelated businesses on a separate Schedule A (Form 990-T) attached to the Form 990-T. See Regulations section 1.512(a)-6 for information about how to identify separate unrelated trades or businesses.

Each organization must file a separate Form 990-T, except section 501(c)(2) title-holding corporations and organizations receiving their

earnings that file a consolidated return under section 1501.

The various provisions of tax law relating to accounting periods, accounting methods, at-risk limits (described in section 465), assessments, and collection penalties that apply to tax returns also generally apply to Form 990-T.

When to file. The Form 990-T of an employees' trust described in section 401(a), an IRA (including a traditional, SEP, SIMPLE, Roth, or Coverdell IRA), or an MSA must be filed by the 15th day of the 4th month after the end of its tax year. The Form 990-T of any other exempt organization must be filed by the 15th day of the 5th month after the end of its tax year. If the due date falls on a Saturday, Sunday, or legal holiday, the return is due by the next business day.

Extension of time to file. Use Form 8868, Application for Automatic Extension of Time To File an Exempt Organization Return, to

request an automatic 6-month extension of time to file Form 990-T.

Public Inspection Requirements of Section 501(c)(3) Organizations. Under section 6104(d), a section 501(c)(3) organization that has gross income from an unrelated trade or business of \$1,000 or more must make its Form 990-T return (including amended returns) available for public inspection. See the Instructions for Form 990-T for information about attachments and related forms that are disclosable as part of the return.



A section 501(c)(3) organization filing the Form 990-T only to request a credit for certain federal excise taxes paid doesn't have to make the Form 990-T available for public inspection.

Payment of Tax

Estimated tax. A tax-exempt organization must make estimated tax payments if it anticipates its tax (unrelated business income tax after certain adjustments) to be \$500 or more. Estimated tax payments are generally due by the 15th day of the 4th, 6th, 9th, and 12th months of the tax year. If any due date falls on a Saturday, Sunday, or legal holiday, the payment is due on the next business day.

Any organization that fails to pay the proper estimated tax when due may be charged an underpayment penalty for the period of underpayment. Generally, to avoid the estimated tax penalty, the organization must make estimated tax payments that total 100% of the organization's current tax year liability. However, an organization with taxable income less than \$1 million for each of the 3 preceding tax years can base its required estimated tax payments on 100% of the tax shown on its return for the preceding

year (unless no tax is shown). If an organization's taxable income for any of those years was \$1 million or more, it can base only its first required installment payment on its prior year's tax.

All tax-exempt organizations should use Form 990-W (Worksheet), to figure their estimated tax.

Tax due with Form 990-T. Any tax due with Form 990-T must be paid in full when the return is filed, but no later than the date the return is due (determined without extensions).

Federal Tax Deposits Must be Made by Electronic Funds Transfer

Electronic Deposit Requirement. The organization must deposit all depository taxes (such as employment tax, excise tax, and corporate income tax) electronically. Generally, electronic fund transfers are made using the Electronic Federal Tax Payment

System (EFTPS). For more information about EFTPS or to enroll in EFTPS, visit the EFTPS website at

[EFTPS.gov](https://eftps.gov), or call 1-800-555-4477, 1-800-733-4829 (TDD), or 1-800-244-4829 (Spanish). You can also get Pub. 966, Electronic Federal Tax Payment System: A Guide to Getting Started.

Depositing on time. For EFTPS deposits to be made timely, the organization must initiate the deposit by 8 p.m. Eastern time the day before the deposit is due.

Same-day wire payment option. If you fail to initiate a deposit transaction on EFTPS by 8 p.m. Eastern time the day before the date a deposit is due, you can still make your deposit on time by using the Federal Tax Application (FTA), a same-day federal tax payment system that works in conjunction with EFTPS. Make arrangements with your financial institution ahead of time, noting the institution's availability, deadlines, and costs,

if you believe you would ever need the same-day wire payment option. To learn more, visit [IRS.gov/SameDayWire](https://www.irs.gov/SameDayWire) and also download the Same-Day Payment Worksheet.

Timeliness of deposits. The IRS uses business days to determine the timeliness of deposits. Business days are any day that isn't a Saturday, Sunday, or legal holiday in the District of Columbia. See Pub. 583, Starting a Business and Keeping Records.



If the organization owes tax and is filing a paper Form 990-T, don't include the payment with the tax return. Instead, use EFTPS.

3.

Unrelated Trade or Business

Unrelated business income is the income from a trade or business regularly conducted by an exempt organization and not substantially related to the performance by the

organization of its exempt purpose or function. Use by the organization, of the profits derived from this activity, does not, alone, make the activity substantially related to the performance by the organization of its exempt purpose or function.

Certain trade or business activities aren't treated as an unrelated trade or business. See *Excluded Trade or Business Activities*, later.

Trade or business. The term "trade or business" generally includes any activity conducted for the production of income from selling goods or performing services. An activity must be conducted with intent to make a profit to constitute a trade or business. An activity doesn't lose its identity as a trade or business merely because it is conducted within a larger group of similar activities that may or may not be related to the exempt purposes of the organization.

For example, the regular sale of pharmaceutical supplies to the general public by a hospital pharmacy doesn't lose its identity as a trade or business, even though the pharmacy also furnishes supplies to the hospital and patients of the hospital in accordance with its exempt purpose.

Similarly, soliciting, selling, and publishing commercial advertising is a trade or business even though the advertising is published in an exempt organization's periodical that contains editorial matter related to the organization's exempt purpose.

Regularly conducted. Business activities of an exempt organization ordinarily are considered regularly conducted if they show a frequency and continuity, and are pursued in a manner similar to comparable commercial activities of nonexempt organizations.

For example, a hospital auxiliary's operation of a sandwich stand for 2 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. However, operating a commercial parking lot every Saturday, year-round, would be the regular conduct of a trade or business.

Not substantially related. A business activity isn't substantially related to an organization's exempt purpose if it doesn't contribute importantly to accomplishing that purpose (other than through the production of funds). Whether an activity contributes importantly depends in each case on the facts involved.

In determining whether activities contribute importantly to the accomplishment of an exempt purpose, the size and extent of the activities involved must be considered in relation to the nature and extent of the exempt function that they intend to serve. For example, to the extent an activity is

conducted on a scale larger than is reasonably necessary to perform an exempt purpose, it doesn't contribute importantly to the accomplishment of the exempt purpose. The part of the activity that is more than needed to accomplish the exempt purpose is an unrelated trade or business.

Also in determining whether activities contribute importantly to the accomplishment of an exempt purpose, the following principles apply.

Selling of products of exempt functions.

Ordinarily, selling products that result from the performance of exempt functions isn't an unrelated trade or business if the product is sold in substantially the same state it is in when the exempt functions are completed. Thus, for an exempt organization engaged in rehabilitating handicapped persons (its exempt function), selling articles made by these persons as part of their rehabilitation training is not an unrelated trade or business.

However, if a completed product resulting from an exempt function is used or exploited in further business activity beyond what is reasonably appropriate or necessary to dispose of it as is, the activity is an unrelated trade or business. For example, if an exempt organization maintains an experimental dairy herd for scientific purposes, the sale of milk and cream produced in the ordinary course of operation of the project isn't an unrelated trade or business. But if the organization uses the milk and cream in the further manufacture of food items such as ice cream, pastries, etc., the sale of these products is an unrelated trade or business unless the manufacturing activities themselves contribute importantly to the accomplishment of an exempt purpose of the organization.

Dual use of assets or facilities. If an asset or facility necessary to the conduct of exempt functions is also used in commercial activities, its use for exempt functions doesn't, by itself,

make the commercial activities a related trade or business. The test, as discussed earlier, is whether the activities contribute importantly to the accomplishment of exempt purposes.

For example, a museum has a theater auditorium designed for showing educational films in connection with its program of public education in the arts and sciences. The theater is a principal feature of the museum and operates continuously while the museum is open to the public. If the organization also operates the theater as a motion picture theater for the public when the museum is closed, the activity is an unrelated trade or business.

For information on allocating expenses for the dual use of assets or facilities, see *Deductions* in chapter 4.

Exploitation of exempt functions. Exempt activities sometimes create goodwill or other intangibles that can be exploited in a

commercial way. When an organization exploits such an intangible in commercial activities, the fact that the income depends in part upon an exempt function of the organization doesn't make the commercial activities a related trade or business. Unless the commercial exploitation contributes importantly to the accomplishment of the exempt purpose, the commercial activities are an unrelated trade or business.

For the treatment of expenses attributable to the exploitation of exempt activities, see *Deductions* in chapter 4.

Examples

The following are examples of activities that were determined to be (or not to be) unrelated trades or businesses using the definitions and principles just discussed.

Artists' facilities. An organization whose exempt purpose is to stimulate and foster public interest in the fine arts by promoting

art exhibits, sponsoring cultural events, and furnishing information about fine arts leases studio apartments to artist tenants and operates a dining hall primarily for these tenants. These two activities don't contribute importantly to accomplishing the organization's exempt purpose. Therefore, they are unrelated trades or businesses.

Broadcasting rights. An exempt collegiate athletic conference conducts an annual competitive athletic game between its conference champion and another collegiate team. Income is derived from admission charges and the sale of exclusive broadcasting rights to a national radio and television network. An athletic program is considered an integral part of the educational process of a university.

The educational purposes served by intercollegiate athletics are identical whether conducted directly by individual universities or by their regional athletic conference. Also, the

educational purposes served by exhibiting a game before an audience that is physically present and exhibiting the game on television or radio before a much larger audience are substantially similar. Therefore, the sale of the broadcasting rights contributes importantly to the accomplishment of the organization's exempt purpose and isn't an unrelated trade or business.

In a similar situation, an exempt organization was created as a national governing body for amateur athletes to foster interest in amateur sports and to encourage widespread public participation. The organization receives income each year from the sale of exclusive broadcasting rights to an independent producer, who contracts with a commercial network to broadcast many of the athletic events sponsored, supervised, and regulated by the organization.

The broadcasting of these events promotes the various amateur sports, fosters widespread public interest in the benefits of the organization's nationwide amateur program, and encourages public participation. The sale of the rights and the broadcasting of the events contribute importantly to the organization's exempt purpose. Therefore, the sale of the exclusive broadcasting rights isn't an unrelated trade or business.

Business league's parking and bus services. The exempt purpose of a business league is to retain and stimulate trade in a downtown area that has inadequate parking facilities. The organization operates, as an insubstantial part of its activities, a park-and-shop plan.

The park-and-shop plan allows customers of particular merchants to park free at certain parking lots in the area. Merchants participating in this plan buy parking stamps,

which they distribute to their customers to use to pay for parking.

The park-and-shop plan encourages customers to use a limited number of participating member merchants in order to obtain free parking. This provides a particular service to individual members of the organization and doesn't further its exempt purpose. Therefore, operating the park-and-shop plan is an unrelated trade or business.

Halfway house workshop. A halfway house organized to provide room, board, therapy, and counseling for persons discharged from alcoholic treatment centers also operates a furniture shop to provide full-time employment for its residents. The profits are applied to the operating costs of the halfway house. The income from this venture isn't unrelated trade or business income because the furniture shop contributes importantly to the organization's purpose of aiding its

residents' transition from treatment to a normal and productive life.

Health club program. An exempt charitable organization's purpose is to provide for the welfare of young people. The organization conducts charitable activities and maintains facilities that will contribute to the physical, social, mental, and spiritual health of young people at minimum or no cost to them. Nominal annual dues are charged for membership in the organization and use of the facilities.

In addition, the organization organized a health club program that its members could join for an annual fee in addition to the annual dues. The annual fee is comparable to fees charged by similar local commercial health clubs and is sufficiently high to restrict participation in the program to a limited number of members of the community.

The health club program is in addition to the general physical fitness program of the organization. Operating this program does not contribute importantly to the organization's accomplishing its exempt purpose and, therefore, is an unrelated trade or business if there is a intent to make a profit.

Hospital facilities. An exempt hospital leases its adjacent office building and furnishes certain office services to a hospital-based medical group for a fee. The group provides all diagnostic and therapeutic procedures to the hospital's patients and operates the hospital's emergency room on a 24-hour basis. The leasing activity is substantially related to the hospital's exempt purpose and isn't an unrelated trade or business.

The hospital also operates a gift shop patronized by patients, visitors making purchases for patients, and employees; a cafeteria and coffee shop primarily for

employees and medical staff; and a parking lot for patients and visitors only. These activities are substantially related to the hospital's exempt purpose and don't constitute unrelated trades or businesses.

Insurance programs. An organization that acts as a group insurance policyholder for its members and collects a fee for performing administrative services is normally carrying on an unrelated trade or business.

Exceptions. Administrative services provided by an organization whose exempt activities may include the provision of insurance benefits, such as fraternal beneficiary societies, voluntary employees beneficiary associations, and labor organizations, are generally not an unrelated trade or business.

Magazine publishing. An association of credit unions with tax-exempt status as a business league publishes a consumer-oriented magazine four times a year and

makes it available to member credit unions for purchase.

By selling a magazine to its members as a promotional device, the organization furnishes its members with a regular commercial service they can use in their own operations. This service doesn't promote the improvement of business conditions of one or more lines of business, which is the exempt purpose of a business league.

Since the activity doesn't contribute importantly to the organization's exempt function, it is an unrelated trade or business.

Membership list sales. An exempt educational organization regularly sells membership mailing lists to business firms. This activity doesn't contribute importantly to the accomplishment of the organization's exempt purpose and therefore is an unrelated trade or business. Also see *Exchange or rental of member lists* under *Excluded Trade or Business Activities*, later.

Miniature golf course. An exempt youth welfare organization operates a miniature golf course that is open to the general public. The course, which is managed by salaried employees, is substantially similar to commercial courses. The admission fees charged are comparable to fees of commercial facilities and are designed to return a profit.

The operation of the miniature golf course in a commercial manner doesn't contribute importantly to the accomplishment of the organization's exempt purpose and, therefore, is an unrelated trade or business.

Museum eating facilities. An exempt art museum operates a dining room, a cafeteria, and a snack bar for use by the museum staff, employees, and visitors. Eating facilities in the museum help to attract visitors and allow them to spend more time viewing the museum's exhibits without having to seek outside restaurants at mealtime. The eating facilities also allow the museum staff and

employees to remain in the museum throughout the day. Thus, the museum's operation of the eating facilities contributes importantly to the accomplishment of its exempt purposes and isn't an unrelated trade or business.

Museum greeting card sales. An art museum that exhibits modern art sells greeting cards that display printed reproductions of selected works from other art collections. Each card is imprinted with the name of the artist, the title or subject matter of the work, the date or period of its creation, if known, and the museum's name. The cards contain appropriate greetings and are personalized on request.

The organization sells the cards in the shop it operates in the museum and sells them at quantity discounts to retail stores. The museum also sells greeting cards by mail order through a catalog that is advertised in magazines and other publications throughout

the year. As a result, a large number of cards are sold at a significant profit.

The museum is exempt as an educational organization on the basis of its ownership, maintenance, and exhibition for public viewing of works of art. The sale of greeting cards with printed reproductions of artworks contributes importantly to the achievement of the museum's exempt educational purposes by enhancing public awareness, interest, and appreciation of art. The cards may encourage more people to visit the museum itself to share in its educational programs. The fact that the cards are promoted and sold in a commercial manner at a profit and in competition with commercial greeting card publishers doesn't alter the fact that the activity is related to the museum's exempt purpose. Therefore, these sales activities aren't an unrelated trade or business.

Museum shop. An art museum maintained and operated for the exhibition of American folk art operates a shop in the museum that sells:

1. Reproductions of works in the museum's own collection and reproductions of artistic works from the collections of other art museums (prints suitable for framing, postcards, greeting cards, and slides);
2. Metal, wood, and ceramic copies of American folk art objects from its own collection and similar copies of art objects from other collections of artworks;
3. Instructional literature and scientific books and souvenir items concerning the history and development of art and, in particular, of American folk art; and

4. Scientific books and souvenir items of the city in which the museum is located.

The shop also rents originals or reproductions of paintings contained in its collection. All of its reproductions are imprinted with the name of the artist, the title or subject matter of the work from which it is reproduced, and the museum's name.

Each line of merchandise must be considered separately to determine if sales are related to the exempt purpose.

The sale and rental of reproductions and copies of works from the museum's own collection and reproductions of artistic works not owned by the museum contribute importantly to the achievement of the museum's exempt educational purpose by making works of art familiar to a broader segment of the public, thereby enhancing the public's understanding and appreciation of art. The same is true for the sale of literature

relating to art. Therefore, these sales activities aren't an unrelated trade or business.

On the other hand, the sale (if they intend to make a profit) of scientific books and souvenir items of the city where the museum is located has no causal relationship to art or to artistic endeavor and, therefore, doesn't contribute importantly to the accomplishment of the museum's exempt educational purposes. Even though selling some of these items could, in a different context, be related to the exempt educational purpose of a different exempt educational organization doesn't change this conclusion. Additionally, the sale of these items doesn't lose its character as an unrelated trade or business merely because the museum also sells articles that contribute importantly to the accomplishment of its exempt function. Therefore, these sales by the museum in this example are an unrelated trade or business.

Nonpatient laboratory testing. Nonpatient laboratory testing performed by a tax-exempt teaching hospital on specimens needed for the conduct of its teaching activities isn't an unrelated trade or business. However, laboratory testing performed by a tax-exempt non-teaching hospital on referred specimens from private office patients of staff physicians is an unrelated trade or business if these services are otherwise available in the community.

Pet boarding and grooming services. An exempt organization, organized and operated for the prevention of cruelty to animals, receives unrelated business income from providing pet boarding and grooming services for the general public. These activities don't contribute importantly to its purpose of preventing cruelty to animals.

Publishing legal notices. A bar association publishes a legal journal containing opinions of the county court, articles of professional

interest to lawyers, advertisements for products and services used by the legal profession, and legal notices. The legal notices are published to satisfy state laws requiring publication of notices in connection with legal proceedings, such as the administration of estates and actions to quiet title to real property. The state designated the bar association's journal as the place to publish the required notices.

The publication of ordinary commercial advertising doesn't advance the exempt purposes of the association even when published in a periodical that contains material related to exempt purposes. Although the advertising is directed specifically to members of the legal profession, it is still commercial in nature and doesn't contribute importantly to the exempt purposes of the association. Therefore, the advertising income is unrelated trade or business income.

On the other hand, the publication of legal notices is distinguishable from ordinary commercial advertising in that its purpose is to inform the general public of significant legal events rather than to stimulate demand for the products or services of an advertiser. This promotes the common interests of the legal profession and contributes importantly to the association's exempt purposes. Therefore, the publishing of legal notices doesn't constitute an unrelated trade or business.

Directory of members. A business league publishes an annual directory that contains a list of all its members, their addresses, and their area of expertise. Each member has the same amount of space in the directory, and its format doesn't emphasize the relative importance or reputation of any member. The directory contains no commercial advertisement and is sold only to the organization's members.

The directory facilitates communication among the members and encourages the exchange of ideas and expertise. Because the directory lists the members in a similar noncommercial format without advertising and isn't distributed to the public, its sale doesn't confer private commercial benefits on the members. The sale of the directory does contribute importantly to the organization's exempt purpose and isn't an unrelated trade or business. This directory differs from the publication discussed next because of its noncommercial characteristics.

Sales of advertising space. A national association of law enforcement officials publishes a monthly journal that contains articles and other editorial material of professional interest to its members. The journal is distributed without charge, mainly to the organization's members.

The organization sells advertising space in the journal either for conventional advertising or to merely identify the purchaser without a commercial message. Some of the noncommercial advertising identifies the purchaser in a separate space, and some consists of listings of 60 or more purchasers per page. A business firm identified in a separate space is further identified in an Index of Advertisers.

The organization solicits advertising by personal contacts. Advertising from large firms is solicited by contacting their chief executive officer or community relations officer rather than their advertising manager. The organization also solicits advertising in form letters appealing for corporate and personal contributions.

An exempt organization's sale of advertising placed for the purchaser's commercial benefit is a commercial activity. Goodwill derived by the purchaser from being identified as a

patron of the organization is usually considered a form of commercial benefit. Therefore, advertising in an exempt organization's publication is generally presumed to be placed for the purchaser's commercial benefit, even if it has no commercial message. However, this presumption isn't conclusive if the purchaser's patronage would be difficult to justify commercially in view of the facts and circumstances. In that case, other factors should also be considered in determining whether a commercial benefit can be expected. Those other factors include:

1. The normal manner in which the publication is circulated;
2. The territorial scope of the circulation;
3. The extent to which its readers, promoters, or the like could reasonably be expected to further, either directly or indirectly, the commercial interest of the advertisers;

4. The eligibility of the publishing organization to receive tax-deductible contributions; and
5. The commercial or noncommercial methods used to solicit the advertisers.

In this situation, the purchaser of a separate advertising space without a commercial message can nevertheless expect a commercial benefit from the goodwill derived from being identified in that manner as a patron of the organization. However, the purchaser of a listing can't expect more than an inconsequential benefit. Therefore, the sale of separate spaces, but not the listings, is an unrelated trade or business.

Sales of cattle for commissions. An agricultural organization, whose exempt purposes are to promote better conditions for cattle breeders and to improve the breed generally, engages in an unrelated trade or

business when it regularly sells cattle for its members on a commission basis.

Sales of hearing aids. A tax-exempt hospital, whose primary activity is rehabilitation, sells hearing aids to patients. This activity is an essential part of the hospital's program to test and evaluate patients with hearing deficiencies and contributes importantly to its exempt purpose. The hearing aid sales aren't an unrelated trade or business.

School facilities. An exempt school has tennis courts and dressing rooms that it uses during the regular school year in its educational program. During the summer, the school operates a tennis club open to the general public. Employees of the school run the club, including collecting membership fees and scheduling court time.

Another exempt school leases the same type of facilities to an unrelated individual who runs a tennis club for the summer. The lease

is for a fixed fee that doesn't depend on the income or profits derived from the leased property.

In both situations, the organization's exempt purpose is the advancement of education. Furnishing tennis facilities in the manner described doesn't further that exempt purpose. These activities are unrelated trades or businesses. However, in the second situation the income derived from the leasing of the property may be excluded from UBTI as rent from real property. See *Rents* under *Exclusions* in chapter 4.

School handicraft shop. An exempt vocational school operates a handicraft shop that sells articles made by students in their regular courses of instruction. The students are paid a percentage of the sales price. In addition, the shop sells products made by local residents who make articles at home according to the shop's specifications. The shop manager periodically inspects the

articles during their manufacture to ensure that they meet desired standards of style and quality. Although many local participants are former students of the school, any qualified person may participate in the program. The sale of articles made by students doesn't constitute an unrelated trade or business, but the sale of products made by local residents is an unrelated trade or business and is subject to unrelated business income tax.

Selling endorsements. An exempt scientific organization enjoys an excellent reputation in the field of biological research. It exploits this reputation regularly by selling endorsements of laboratory equipment to manufacturers. Endorsing laboratory equipment doesn't contribute importantly to the accomplishment of any purpose for which exemption is granted to the organization. Accordingly, the sale of endorsements is an unrelated trade or business.

Services provided with lease. An exempt university leases its football stadium during several months of the year to a professional football team for a fixed fee. Under the lease agreement, the university furnishes heat, light, and water and is responsible for all ground maintenance. It also provides dressing room, linen, and stadium security services for the professional team.

Leasing of the stadium is an unrelated trade or business. In addition, the substantial services furnished for the convenience of the lessee go beyond those usually provided with the rental of space for occupancy only.

Therefore, the income from this lease is rent from real property and unrelated business taxable income.

Sponsoring entertainment events. An exempt university has a regular faculty and a regularly enrolled student body. During the school year, the university sponsors the appearance of professional theater companies

and symphony orchestras that present drama and musical performances for the students and faculty members. Members of the general public also are admitted. The university advertises these performances and supervises advance ticket sales at various places, including such university facilities as the cafeteria and the university bookstore. Although the presentation of the performances makes use of an intangible generated by the university's exempt educational functions—the presence of the student body and faculty—such drama and music events contribute importantly to the overall educational and cultural functions of the university. Therefore, the activity isn't an unrelated trade or business.

Travel tour programs. Travel tour activities that are a trade or business are an unrelated trade or business if the activities aren't substantially related to the purpose for which

tax exemption was granted to the organization.

Example 1. A tax-exempt university alumni association provides a travel tour program for its members and their families. The organization works with various travel agencies and schedules approximately ten tours a year to various places around the world. It mails out promotional material and accepts reservations for fees paid by the travel agencies on a per-person basis.

The organization provides an employee for each tour as a tour leader. There is no formal educational program conducted with these tours, and they don't differ from regular commercially operated tours (if there is a intent to make a profit).

By providing travel tours to its members, the organization is engaging in a regularly conducted trade or business. Even if the tours it offers support the university, financially and otherwise, and encourage alumni to do the

same, the travel tours don't contribute importantly to the organization's exempt purpose of promoting education. Therefore, the sale of the travel tours is an unrelated trade or business.

Example 2. A tax-exempt organization formed for the purpose of educating individuals about the geography and the culture of the United States provides study tours to national parks and other locations within the United States. These tours are conducted by teachers and others certified by the state board of education. The tours are primarily designed for students enrolled in degree programs at state educational institutions but are open to all who agree to participate in the required study program associated with the tour taken. A tour's study program consists of instruction on subjects related to the location being visited on the tour. Each tour group brings along a library of material related to the subjects being studied

on the tour. During the tour, 5 or 6 hours per day are devoted to organized study, preparation of reports, lectures, instruction, and recitation by the students. Examinations are given at the end of each tour. The state board of education awards academic credit for tour participation. Because these tours are substantially related to the organization's exempt purpose, they aren't an unrelated trade or business.

Yearbook advertising. An exempt organization receives income from the sale of advertising in its annual yearbook. The organization hires an independent commercial firm, under a contract covering a full calendar year, to conduct an intensive advertising solicitation campaign in the organization's name. This firm is paid a percentage of the gross advertising receipts for selling the advertising, collecting from advertisers, and printing the yearbook. This advertising activity is an unrelated trade or business.

Youth residence. An exempt organization, whose purpose is to provide for the welfare of young people, rents rooms primarily to people under age 25. The residence units are operated on, and as a part of, the premises in which the organization carries on the social, recreational, and guidance programs for which it was recognized as exempt. The facilities are under the management and supervision of trained career professionals who provide residents with personal counseling, physical education programs, and group recreational activities. The rentals aren't an unrelated trade or business because renting the rooms is substantially related to the organization's exempt purpose.

Excluded Trade or Business Activities

The following activities are specifically excluded from the definition of unrelated trade or business.

Gaming. In general, games of chance do not further an exempt purpose. An exempt organization that generates revenue from the conduct of activities will be operating an unrelated trade or business, unless a exception applies. The exceptions to the general rule (that gaming does not usually further an exempt purpose) include organizations whose exempt purposes include social or recreational activities. For these organizations, gaming itself may further an exempt purpose.

More information about gaming activities by exempt organizations can be found in Publication 3079, Tax-Exempt Organizations and Gaming.

Bingo games. Bingo games may qualify for a specific exclusion from the definition of unrelated trade or business. To qualify for this exclusion, the bingo game must meet the following requirements.

1. It meets the legal definition of bingo.

2. It is legal where it is played.
3. It is played in a jurisdiction where bingo games aren't regularly conducted by for-profit organizations.

Gambling activities other than bingo.

Games of chance conducted by an exempt organization may avoid being treated as an unrelated trade or business if they are:

- Conducted with substantially all volunteer labor,
- Qualified public entertainment activities, and
- Games of chance conducted in North Dakota.

Legal definition. For a game to meet the legal definition of bingo, wagers must be placed, winners must be determined, and prizes or other property must be distributed in the presence of all persons placing wagers in that game.

A wagering game that doesn't meet the legal definition of bingo doesn't qualify for the exclusion, regardless of its name. For example, "instant bingo," in which a player buys a prepackaged bingo card with pull-tabs that the player removes to determine if he or she is a winner, doesn't qualify.

Legal where played. This exclusion applies only if bingo is legal under the laws of the jurisdiction where it is conducted. The fact that a jurisdiction's law that prohibits bingo is rarely enforced or is widely disregarded doesn't make the conduct of bingo legal for the exception and is therefore an unrelated trade or business.

No for-profit games where played. This exclusion applies only if for-profit organizations can't regularly conduct bingo games in any part of the same jurisdiction. Jurisdiction is normally the entire state; however, in certain situations, local jurisdiction will control.

Example. Tax-exempt organizations X and Y are organized under the laws of state N, which has a law that permits exempt organizations to conduct bingo games. In addition, for-profit organizations are permitted to conduct bingo games in city S, a resort community located in county R. Several for-profit organizations conduct nightly games. Y conducts weekly bingo games in city S, while X conducts weekly games in county R. Since state law confines the for-profit organizations to city S, local jurisdiction controls. Y's bingo games conducted in city S are an unrelated trade or business. However, X's bingo games conducted in county R outside of city S aren't an unrelated trade or business.

See Pub. 3079, for more detailed information.

Convenience of members. A trade or business conducted by a 501(c)(3) organization or by a state college or university primarily for the convenience of its

members, students, patients, officers, or employees isn't an unrelated trade or business. For example, a laundry operated by a college for the purpose of laundering dormitory linens and students' clothing isn't an unrelated trade or business.

Convention or trade show activity. An unrelated trade or business doesn't include qualified convention or trade show activities conducted at a convention, annual meeting, or trade show.

A qualified convention or trade show activity is any activity of a kind traditionally conducted by a qualifying organization in conjunction with an international, national, state, regional, or local convention, annual meeting, or show if:

1. One of the purposes of the organization in sponsoring the activity is promoting and stimulating interest in, and demand for, the products and services of that industry or educating

the persons in attendance regarding new products and services or new rules and regulations affecting the industry; and

2. The show is designed to achieve its purpose through the character of the exhibits and the extent of the industry products that are displayed.

For these purposes, a qualifying organization is one described in section 501(c)(3), 501(c)(4), 501(c)(5), or 501(c)(6). The organization must regularly conduct, as one of its substantial exempt purposes, a qualified convention or trade show activity.

The rental of display space to exhibitors (including exhibitors who are suppliers) at a qualified convention or trade show isn't an unrelated trade or business even if the exhibitors who rent the space are permitted to sell or solicit orders. For this purpose, a supplier's exhibit is one in which the exhibitor displays goods or services that are supplied

to, rather than by, members of the qualifying organization in the conduct of these members' own trades or businesses.

Certain Internet activities conducted by a trade association described in section 501(c)(6) will be considered qualified convention and trade show activity if conducted on a special supplementary section of the association's website in conjunction with a trade show conducted by the association. The trade show itself must be a qualified convention and trade show activity. The supplementary section of the website must be ancillary to, and serve to augment and enhance, the trade show, as when it makes available the same information available at the trade show and is available only during a time period that coincides with the time period that the trade show is in operation. Conversely, Internet activities that aren't conducted in conjunction with a qualified convention and trade show activity

and that don't augment and enhance the trade show can't themselves be qualified convention and trade show activity.

Distribution of low-cost articles. The term "unrelated trade or business" doesn't include activities relating to the distribution of low-cost articles incidental to soliciting charitable contributions. This applies to organizations described in section 501 that are eligible to receive charitable income tax deductible contributions.

A distribution is considered incidental to the solicitation of a charitable contribution if:

1. The recipient didn't request the distribution,
2. The distribution is made without the express consent of the recipient, and
3. The article is accompanied by a request for a charitable contribution to the organization and a statement that the recipient may keep the low-cost

article regardless of whether a contribution is made.

An article is considered low cost if the cost of an item (or the aggregate costs if more than one item) distributed to a single recipient in a tax year isn't more than \$11.20 (in 2020), indexed annually for inflation. The cost of an article is the cost to the organization that distributes the item or on whose behalf it is distributed.

Employee association sales. The sale of certain items by a local association of employees described in section 501(c)(4), organized before May 17, 1969, isn't an unrelated trade or business if the items are sold for the convenience of the association's members at their usual place of employment. This exclusion applies only to the sale of work-related clothes and equipment and items normally sold through vending machines, food dispensing facilities, or by snack bars.

Exchange or rental of member lists. The exchange or rental of member or donor lists between organizations described in section 501 that are eligible to receive charitable contributions isn't included in the term unrelated trade or business.

Hospital services. The providing of certain services at or below cost by an exempt hospital to other exempt hospitals that have facilities for 100 or fewer inpatients isn't an unrelated trade or business. This exclusion applies only to services described in section 501(e)(1)(A).