



Unrelated Business Income Taxes (UBIT)

POLICY STATEMENT

Units of the university that have activities that generate unrelated business income will be charged all applicable income taxes.

REASON FOR POLICY

Cornell University is required by law to pay tax on net taxable income generated from business operations that, under the Internal Revenue Code, are considered unrelated to the university mission. This policy provides guidelines for units to plan for Unrelated Business Income Taxes (UBIT), and procedures to calculate UBIT.

ENTITIES AFFECTED BY THIS POLICY

Endowed Ithaca and contract colleges of the university, including Weill Cornell Medicine

WHO SHOULD READ THIS POLICY

- Departmental business managers
- College officers
- Anyone creating a new program that will generate revenues

WEBSITE ADDRESS FOR THIS POLICY*

www.dfa.cornell.edu/policy/policies/unrelated-business-income-tax

**The Policy Office web pages house the most current versions of all standardized university policies, at [http://www.policy.cornell.edu]*

POLICY 3.15

Volume 3, Financial
Management
Responsible Executive:
Executive Vice President and
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RELATED DOCUMENTS

University Policies

[University Policy 3.9, Capital Assets](#)
[University Policy 3.10, Recharge Entities](#)

Other Documents

Endowed Equipment Inventory Control Guide
Statutory Equipment Inventory Control Guide
Physical Space Inventory Guide

CONTACTS

Subject	Contact	Telephone	Email/Web Address
Policy Clarification	University Tax Office	(607) 255-9465	tax@cornell.edu
New Activity, Business and Finance Advice	University Tax Office	(607) 255-9465	tax@cornell.edu
New Activity, Impact on Community Relations	Community Relations	(607) 255-5348	
New Activity, Liability and Insurance	Risk Management and Insurance	(607) 254-1575	
Endowed Income Codes ("UBIT Survey")	University Tax Office	(607) 255-9465	tax@cornell.edu

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DEFINITIONS

These definitions apply to these terms as they are used in this policy.

Capital Expenditure	An expense that adds to the value or useful life of property is considered a capital expense and generally may not be claimed as a current deduction, but in most cases may be deducted through depreciation. Expenditures that keep property in an ordinarily efficient operating condition and do not add to its value or appreciably prolong its useful life are generally deductible as repairs.
Convenience Exclusion	A business activity conducted by a college or university primarily for the convenience of its faculty, staff and/or students that is generally not taxable regardless of the nature of the activity. ♦ Caution: The convenience exclusion generally does not apply to alumni
Cost of Goods Sold	The cost of articles held for sale to customers in the regular course of a trade or business. Generally, the costs are accumulated in an inventory account prior to sale.
Deductions	The ordinary and necessary expenses of carrying on a trade or business, which are deducted from gross profit. In computing the unrelated business taxable income of a tax-exempt organization, those expenses that are deductible by commercial organizations are also deductible by the tax-exempt organization. Where facilities or personnel are used for both exempt functions and the conduct of an unrelated business, it is necessary to allocate costs and income between the two uses on a reasonable basis. The portion of any such items allocated to the unrelated business is allowable as a deduction in computing taxable income.
Depreciation	A reasonable allowance for the exhaustion, wear and tear of property used in a trade or business, or of property held for the production of income. Depreciation is allowed for tangible property, but not for inventories or land.
Direct Cost	An expenditure that can be identified specifically with a particular business activity or that can be directly assigned to an activity relatively easily with a high degree of accuracy.
Federal Unallowable	A cost identified in Section J, in the OMB Circular A-21 as unreimbursable by the federal government. This term supersedes the term "non-recoverable cost."
Gross Income	For federal income tax purposes, all income or revenue from each source.
Gross Profit	Gross income minus cost of the goods sold.
Ordinary and Necessary	An expense is necessary if it is appropriate and helpful to the taxpayer's business. An expense is ordinary if it is one that is common and accepted in the particular business activity.
Personal Business Property	Furniture and equipment used in a business activity.
Real Business Property	Land and buildings used in a business activity

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DEFINITIONS, CONTINUED

Regularly Carried on	<p>With a frequency and manner comparable to that of the same or similar activity by a taxable organization. The following are two examples of activities that are NOT considered "regularly carried on":</p> <ol style="list-style-type: none"> 1. The one-time sale of university computer equipment and programs. 2. The operation of a sandwich stand at one or several events would not be the regular conduct of a trade or business. However, conducting the sandwich stand one day each week year-round would constitute a regularly carried on trade or business.
Overhead Costs	<p>Expenditures that are incurred for joint objectives and cannot be readily identified with a particular business activity. These costs are often classified as overhead (either at the unit or central level). ♦ Note: The University Tax Office will work with a unit to allocate the costs to a particular activity on a reasonable basis (square footage, percentage of time, etc.).</p>
Trade or Business	<p>An activity carried on with a profit motive--an intention to produce a net income after deducting all direct and indirect expenses.</p>
Unrelated Business Income (UBI)	<p>Income from an activity that does not contribute importantly to the exempt purpose of the university is classified as unrelated. ♦ Note: The fact that the income from the activity will be used to support the exempt purpose of the university does not make the activity related; it is the activity itself that must be mission related.</p>
Unrelated Business Taxable Income	<p>The gross profit from any unrelated trade or business regularly carried on, minus business deductions connected to the trade or business. To be taxable, income must be from a business not substantially related to the exercise of the charitable, educational, or other purpose on which the exemption of the organization is based.</p>

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OVERVIEW

Introduction to this Policy

Each fiscal year, the university is required to file an Exempt Organization Business Income Tax Return (Form 990-T) with the Internal Revenue Service (as well as a similar return with New York State) to report any unrelated business income generated by the activities of its academic and support units. The Internal Revenue Code states that a college or university is generally deemed to have unrelated business taxable income when it realizes income from any regularly conducted trade or business that is not substantially related to its exempt purposes, which at Cornell University are: education, research, public service, and patient care.

Each activity generating unrelated business income must be able to document all revenues as well as all expenses incurred in creating those revenues. The expenses must include both the expenditures directly charged to the business activity as well as expenditures that may have been charged elsewhere but still are associated with the business activity.

The University Tax Office will consult with any department that has unrelated business income to identify all reporting requirements and will facilitate all calculations of income and expenses.

Annual Review

After the close of each fiscal year, the University Tax Office reviews activities where unrelated business income may exist.

Examples of Potential Unrelated Business Activities

The following are examples of potential unrelated business income generating activities.

- Sale or rental of any goods or services other than for the convenience of faculty, staff, or students. ♦ **Caution:** IRS does not classify “alumni” as members of this group.
- Any form of advertising that generates revenue for the university;
- Rental of real property when services are provided to the renter;
- Participation in joint ventures with for-profit entities.

♦ **Note:** Prior to undertaking any activity that might generate unrelated business income, contact the University Tax Office for business guidance, and Community Relations for information on your activity's impact on the community.

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OVERVIEW, CONTINUED

Possible Tax Liability

The presence of these activities does not necessarily mean that a tax liability exists. It may be determined that the activity is not subject to unrelated business income tax, or if it is a taxable activity, the revenue may be substantially or completely offset by expenses incurred.

The University Tax Office, working with the local unit, and the Accounting, Reporting, and Analysis Department, will calculate overhead expenses to be charged against an activity that generates UBI. **Taxable income = Gross Income minus Cost of Goods Sold minus Direct Costs minus Overhead Costs.**

	Gross Income	\$XXXX.XX
minus-->	<u>Cost of Goods Sold</u>	<u>XXX.XX</u>
equals-->	Gross Profit	\$XXXX.XX
minus-->	Direct Costs	XXX.XX
minus-->	<u>Overhead Costs (allocated)</u>	<u>XXX.XX</u>
equals-->	Taxable Income	\$XXXX.XX

◆ **Note:** Allocation of actual tax expense related to UBI will not be booked to a unit's account unless the University Tax Office has contacted that unit to discuss a specific allocation and to provide supporting documentation related to that expense allocation. Actual tax expense depends upon myriad factors: the net taxable income from all Cornell's UBI generators; whether the return as a whole reflects a tax liability; whether IRS, under audit, proposes an adjustment to a return as filed; whether Cornell is subject to alternative minimum tax; etc.

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INCOME

General Comments

All revenues are considered unrelated business income if the revenue-generating activity is:

- unrelated to the exempt purpose of the university; **and**
- regularly carried on; **and**
- considered a “trade or business;” **and**
- not one of the exceptions described below.

Exceptions to Unrelated Business Income

Certain activities of not-for-profit educational organizations that appear to be unrelated business income are generally not classified as UBI because of specific exemptions under the Internal Revenue Code. The most common examples of these activities are listed below:

- royalties, dividends, interest, and annuities;
- rents from real property where no services are provided;
 - ◆ **Caution:** Rents from real property may generate tax issues other than Unrelated Business Income Tax. For more information, contact the University Tax Office.
- gains or losses on the sale or exchange of investment property;
- income from research grants and contracts;
- income from a trade or business activity in which substantially all the work in carrying on the trade or business is performed by volunteers;
- income from a trade or business activity conducted by a college or university, primarily for the convenience of its faculty, staff, and/or students.
 - ◆ **Caution:** The convenience exception does not apply to alumni.

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DETERMINING TAXABLE LIABILITY

Cost of Goods Sold

The cost of goods sold includes the inventory cost of the article sold plus delivery costs, warehousing costs, etc. The cost of goods sold is subtracted from the gross income to determine the gross profit.

Deductions

Deductions are subtracted from the gross profit to determine the unrelated business taxable income. The three types of deductions are:

- direct expenses (charged to the business activity accounts);
- allocated direct expenses (charged to other departmental accounts);
- indirect expenses.

Direct Expenses

Direct expenses fall into two categories:

Deductible direct expenses charged to the business activity account

These include ordinary and necessary business expenses such as:

- salaries, wages, and applicable university benefit rates;
- supplies and materials;
- subcontracts and outside services;
- external interest paid;
- facilities expense (rental, utilities, maintenance, and custodial cost) paid by the business activity for the occupied space;
- equipment lease or rental;
- other expenses associated with the activity (e.g., travel, communications);

◆ **Caution:** Federal unallowable expenses (i.e., not eligible for reimbursement from the federal government) **are deductible for tax purposes** if they are ordinary and necessary business expenses of the activity (although some of these expenses may *otherwise* be subject to limitations in the Internal Revenue Code). Some examples of costs that are unallowable for federal purposes but deductible for tax purposes are: entertainment; bad debt; advertising; public relations; alcoholic beverages; donations. Note, however, that if the product is paid for by a federal grant or contract, the rate charged to the federal award must recover only federal allowable costs (see University Policy 3.10, Recharge Entities).

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DETERMINING TAXABLE LIABILITY, CONTINUED

Deductible direct expenses charged to departmental accounts other than the business activity account

These include ordinary and necessary business expenses that can be specifically identified with the business activity. These are the same types of expenses as listed above. The only difference is that the expenses were not recorded directly into the business activity accounts. The University Tax Office will help you identify and allocate these costs, based on information that must be supplied to them. Some of the typical expenses that fall into this category are:

- salaries of people within the department who work on the business activity, but are charged to accounts other than those of the business activity (e.g., receptionists who cover multiple areas, managers responsible for multiple areas, etc.). For these expenses, you should document percentage of time spent on the business activity;
- supplies used in the business activity, but charged to a central departmental account;
- facilities expense (utilities, maintenance, and custodial cost) paid by the department for the occupied space.

◆**Note:** If any expense benefits two or more activities in proportions that can be determined without undue effort or cost, the expense should be allocated to the activities based on the proportional benefit. If an expense benefits two or more activities in proportions that cannot be determined because of the interrelationship of the work involved, then the expense may be allocated to the benefited activities on a reasonable basis.

Overhead Costs

Deductible expenses also include a pro rata share of expenses incurred for common or joint objectives that cannot be identified readily or specifically with any particular business activity.

These are generally university or divisional expenses that are indirectly related to the business activity. A few examples of these types of expenses are:

- general university administration (president's costs, legal, etc.);
- equipment depreciation;
- building depreciation;

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DETERMINING TAXABLE LIABILITY, CONTINUED

- facilities expense (utilities, maintenance, and custodial cost) paid by the university.

◆ **Note:** The University Tax Office will work directly with the units and the Accounting, Reporting, and Analysis Department to determine a reasonable basis for allocating university or divisional "overhead costs" to the activity generating unrelated business income.

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RESPONSIBILITIES

The major responsibilities each party has in connection with University Policy 3.15, Unrelated Business Income Taxes (UBIT), are as follows:

Division of Financial Affairs (University Tax Office)	<p>At the end of each fiscal year, review activities where unrelated business income may exist.</p> <p>Consult with departments that have unrelated business income to facilitate calculations of expenses.</p> <p>Calculate overhead expenses to be charged against any activity that generates UBI.</p>
Unit	<p>Prior to undertaking any activity that might generate business income, contact the University Tax Office for business guidance, Community Relations for information on your activity's impact on the community, and the Office of Risk Management and Insurance for issues related to liability and insurance.</p> <p>Cooperate with the University Tax Office regarding issues surrounding University Policy 3.15, Unrelated Business Income Taxes.</p> <p>Identify and deduct direct expenses and overhead costs in accordance with University Policy 3.15, Unrelated Business Income Taxes, consulting with the University Tax Office when necessary.</p>
University	<p>File an Exempt Organization Business Income Tax Return (Form 990-T) with the Internal Revenue Service (as well as a similar return with New York State) to report any unrelated business income generated by the activities of its academic and support units.</p>

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