



Non Profit Tax Update  
Presented by  
James K. O'Connor, CPA

For Profit Tax Update  
Presented by  
Michael E. Helton, CPA

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# Non Profit Tax Update

**Presented by: James K. O'Connor, CPA  
Tax Shareholder**



# Unrelated Business Income – Summary of Basics

- An activity is an unrelated trade or business if three conditions exist:
  - The organization is conducting a trade or business for the production of income from selling goods or performing services
  - The trade or business is regularly carried on
  - The activity is “not substantially related” to the carrying out of the organization’s exempt purpose

# Unrelated Business Income – Summary of Basics

- Income excluded from Unrelated Business Income
  - Interest & dividends
  - Royalties
  - Rental income
  - Gains & losses from disposition of property

# Unrelated Business Income – Summary of Basics

- Certain activities are excluded even though they meet all three tests
- The most common statutory exclusions:
  - Volunteer labor
  - Members' convenience
  - Donated merchandise

# Examples of Unrelated Business Income

- Advertising income
- K-1 pass-through income
- Income from controlled organization
- Income on debt financed property

# Trivia Question

- **In this 1994 Best Picture, Tom Hanks character played football for what SEC powerhouse?**

## Forrest Gump (University of Alabama)



# Unrelated Business Income Tax Changes

- Old Law - Nonprofits were able to combine all activities generating UBTI in calculating UBIT
- New Law UBIT Silos – Requires tax-exempt organizations operating one or more unrelated trades or businesses to compute UBTI separately.
- New Flat Federal Corporate Tax of 21%



# Net Operating Loss Changes

- Old Law - NOLs could be carried forward 20 years to offset taxable income or carried back 2 years to offset taxable income reported in the past without limitation.
- New Laws :
  - Carryback of NOLs incurred in 2018 and beyond are no longer permitted.
  - NOLs can be carried forward indefinitely (20 year limit is eliminated).
  - NOLs incurred in 2018 and beyond may only be used against 80% of a corporation's taxable income. However, NOL carryovers from years prior to January 1, 2018 can still be used to reduce 100% of taxable income.



# Why the Change?



# 2013 IRS Colleges and Universities Compliance Project Report

- IRS examined tax returns from 34 of the largest colleges and universities for tax years 2006-2008
- IRS found that UBTI was underreported at 90% of the institutions examined. The report identified 4 primary reasons for understated UBTI:
  1. Lack of profit motive
  2. Improper Expense Allocation
  3. Misclassification of certain activities as exempt
  4. Miscalculated or Unsubstantiated Net Operating Losses.



Form 990-T

Exempt Organization Business Income Tax Return (and proxy tax under section 6033(e))

GMB No 1545-0687

2015

Department of the Treasury Internal Revenue Service

For calendar year 2015 or other tax year beginning 10/01, 2015, and ending 09/30, 2016

A Check box if address changed

Name of organization THE BOARD OF TRUSTEES OF THE UNIVERSITY OF ALABAMA

D Employer identification number 63-6001138

B Exempt under section

501(c)(3) 408(a) 529(a)

E Unrelated business activity codes

C Book value of all assets at end of year

City or town, state or province, country, and ZIP or foreign postal code TUSCALOOSA, AL 35401

F Group exemption number

H Describe the organization's primary unrelated business activity

SPORTS AND RECREATIONAL ACTIVITIES/INVESTMENTS

I During the tax year, was the corporation a subsidiary in an affiliated group or a parent-subsidary controlled group?

Yes X No

J The books are in care of

MR. STAN ACKER Telephone number 205-348-7879

Part I Unrelated Trade or Business Income

(A) Income (B) Expenses (C) Net

1a Gross receipts or sales

5,430,805.

2 Cost of goods sold

789,093.

3 Gross profit

4,641,712.

4a Capital gain net income

110,464.

b Net gain (loss)

-2,602,266.

5 Income (loss) from partnerships

ATTCH 1 -2,602,266.

6 Rent income

7 Unrelated debt-financed income

8 Interest, annuities, royalties and rents

9 Investment income

10 Exploited exempt activity income

11 Advertising income

12 Other income

333,863. ATTCH 2 333,863.

13 Total

2,483,773. 2,483,773.

Part II Deductions Not Taken Elsewhere

(See instructions for limitations on deductions.)

14 Compensation of officers, directors, and trustees

15 Salaries and wages

16 Repairs and maintenance

17 Bad debts

18 Interest

19 Taxes and licenses

20 Charitable contributions

21 Depreciation

22 Less depreciation claimed on Schedule A

23 Depletion

24 Contributions to deferred compensation plans

25 Employee benefit programs

26 Excess exempt expenses

27 Excess readership costs

28 Other deductions

29 Total deductions

30 Unrelated business taxable income before net operating loss deduction

31 Net operating loss deduction

32 Unrelated business taxable income before specific deduction

33 Specific deduction

34 Unrelated business taxable income

enter the smaller of zero or line 32

-2,681,520.

Form 990-T (2015)

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Part III Tax Computation

Table with 3 columns: Line number, Description, Amount. Includes Organizations Taxable as Corporations, Trusts Taxable at Trust Rates, Proxy tax, Alternative minimum tax, Total.

Part IV Tax and Payments

Table with 3 columns: Line number, Description, Amount. Includes Foreign tax credit, Other credits, General business credit, Credit for prior year minimum tax, Total credits, Total tax, Payments, Total payments, Estimated tax penalty, Tax due, Overpayment, Refund.

Part V Statements Regarding Certain Activities and Other Information

Table with 3 columns: Question number, Question text, Yes/No. Includes questions about foreign accounts, distribution from foreign trusts, and tax-exempt interest.

Schedule A - Cost of Goods Sold

Table with 3 columns: Line number, Description, Amount. Includes Inventory at beginning of year, Purchases, Cost of labor, Additional section 263A costs, Other costs, Total.

Sign Here section with signature of Travis L. Patton, Date 3/1/2018, and Preparer Information section with name Travis L. Patton, Firm name PRICEWATERHOUSECOOPERS LLP, Firm's EIN 13-4008324, Firm's address 600 13TH STREET NW, SUITE 1000 WASHINGTON, DC 20005-3005.

SCANNED APR 24 2018

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## We've only received limited guidance so far – Notice 2018-67

- Provides transition rules and interim guidance on which organizations may rely pending publication of proposed Regs.
- In Determining Separate Trade or Business – Pending proposed Regs, organizations may rely on reasonable good faith interpretations of Code Section 511-514 including using the NAIC classifications.
- An exempt organization may aggregate its UBTI from its interest in a single partnership with multiple trades or businesses if one of the two tests is met:
  - De minimis test, organization satisfies if it holds directly no more than 2% profits or capital interest.
  - Control test, organization satisfies if it directly holds no more than 20% capital interest and does not have control or influence over the partnership.
  - Additionally, the organization may aggregate all qualifying partnership interests and treat as comprising a single trade or business.



# Should I create a Taxable Subsidiary?

- Tax-exempt organizations engaged in multiple lines of unrelated business may wish to consider organizing those activities inside a single corporate subsidiary to avoid UBTI silo limitation.
- Corporate Subsidiary can also be used as blocker corporation for passthrough entities that issue K-1s subject to UBIT.
- Tax-exempt organizations with growing unrelated businesses can use corporate subsidiary to insulate it's tax-exempt status (Potential Danger of losing your tax exempt status if the unrelated business is Not insubstantial compared to your exempt purposes activities).

# Inclusion of Certain Fringe Benefits in the Calculation of UBTI

- The following fringe benefits paid or incurred by the organization will now trigger UBIT:
  - Qualified transportation fringe benefits,
  - Parking facilities used in connection with Qualified parking.
  - On – premises athletic facilities.
- These deductions have also been limited for For-profit entities. Therefore, these UBIT provisions were added to parallel the limit on deductibility by For-Profit entities.



# Tax Exempt Organizations have 2 options:

- Continue to provide the fringe benefit tax free to employees and pay the associated UBIT liability
- Treat the benefit to the employees as taxable compensation, subjecting the employees to income tax plus employment taxes on these amounts, with the tax-exempt organizations matching its half of payroll tax burden.

# Other Tax Exempt Changes

- New 21% Excise Tax on Annual Compensation paid in Excess of \$1 Million or More
- New 1.4% Excise Tax on the Net Investment Income of Certain Private Colleges and Universities with assets of at least \$500,000 per full-time student and more than 500 full time students (Trivia Question/Harvard Endowment)
- The Act removes the deduction for contributions to schools of 80% of the amount paid for the right to buy tickets for seating at a school athletic event.

# Trivia Question

- **In this 2011 Comedy, Elle Woods, played by Reese Witherspoon, is accepted into this prestigious Law School?**

## Legally Blonde (Harvard Law School)

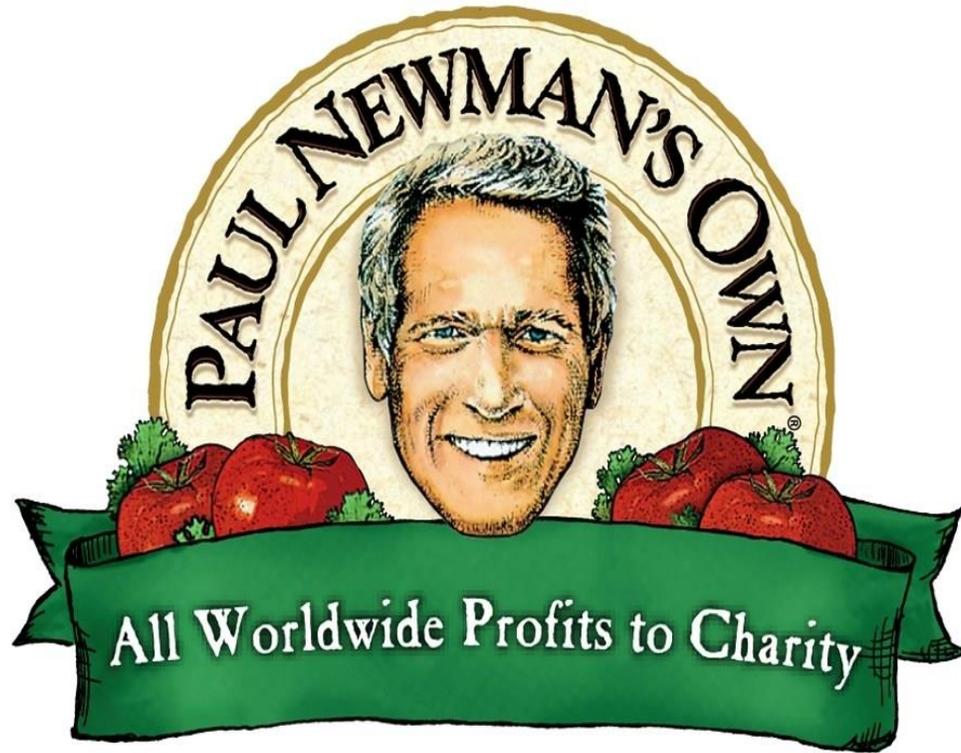


# Repeal of Substantiation Exception in Case of Contributions Reported by Donee

- Old Law authorized the IRS to develop optional donee reporting procedures for substantiating charitable contributions of \$250 or more that could be used in lieu of contemporaneous written acknowledgement
- As a result of the public comments the IRS received in response to 2015 Proposed Regs, the IRS decided to withdraw the regulations.
- As such, the responsibility was put back on the taxpayer to substantiate single charitable contributions in the amount of \$250 or more with contemporaneous written acknowledgement.

# Trivia Question

- **This film icon who passed away in 2008 was quoted as saying:  
“The embarrassing thing is that my salad dressing is out-grossing my films.”**



# Private Foundation – Change to Exception to Excess Business Holdings Rule (Newman’s Own Rule)

- Old Law limited Private Foundations from owning more than 20% of the voting stock of a single corporation
- New Law allows a private foundation to own 100% of an operating business if certain strict requirements are met:
  - 100% ownership requirement be acquired other than by purchase
  - All Profits of the business enterprise must be distributed to the foundations no later than 120 days after the close of the taxable year
  - The business enterprise is operated independently from the private foundation

# Tax Cuts and Jobs Act Summary

**12/22/17 – Signed into Law**

**Presented by: Mike Helton, CPA  
Tax Shareholder**



# Areas of Planning / Awareness

- C-Corporate AMT repealed.
- Individual AMT has a \$109,400 exemption (MFJ) with a \$1MM exemption phase out.
- Bonus Depreciation levels increased to 100% for purchases made after 9/27/2017. Will create significant book-tax differences that will require proper planning.
  - Removes the “original use” requirement. Thus, allowing Bonus for used units purchased
    - Big Deal for M&A allocations.
  - Taxpayers may still elect 50% instead of 100% Bonus depreciation or Elect out entirely.

# Areas of Planning / Awareness

- Limitation on Business Interest Expense Deduction – will be capped to 30% of business' **adjusted** taxable income.
  - Exceptions apply for businesses under \$25M average gross receipts.
- Entertainment expenses 100% non-deductible.
  - Guidance provided in Notice 2018-76 (Oct. 3, 2018)
- The State and Local tax (SALT) deductions including Property taxes are capped to a combined \$10,000 limit.

# Pass-Through Entities

- New Law limits use of “excess business losses” against other income.
  - MFJ - \$500K; \$250K for others – Carryovers are allowed
  - Creates new Code §461(l) – No guidance yet, but many questions remain
  - Loss disallowance provision – after basis, at risk and passive hurdles
- Creates a new IRC Sec. 199A which allows a deduction of the lesser of “qualified business income” (QBI) or 20% of taxable income.
  - Sounds simple, but the calculation is complex and has Limits.

# Pass-Through Entities - §199A

- QBI is defined as all domestic trade or business income (§162)- excludes investment income.
- General Focus on K-1 Income for QBI purposes except for:
  - S-T and L-T Capital Gains
  - Interest Income
  - Dividend Income
- Limitations for filers making \$157,500 (joint \$315,000) or more.



# Pass-Through Entities - §199A

- Deduction is limited to the LESSER of:
  1. 20% of Taxable Income over the sum of any Net Capital Gain OR
  2. the GREATER of:
    - 50% of the taxpayer's Allocable Share of "W-2 wages" paid ("Wage") or
    - the sum of 25% of the taxpayer's Allocable Share of "W-2 wages" paid plus 2.5% of the unadjusted basis, immediately after acquisition, of all qualified property ("UBIA").
- Aggregation of multiple trades or businesses / entities is possible; except for SSTB's.
- Note – Replaces the prior §199 DPAD deduction

# Pass-Through Entities - §199A

- Reasonable compensation / Guaranteed Payments paid to owners not counted toward QBI.
  - Requirement for S-Corps. to pay Reasonable Compensation.
  - No requirement for Partnerships to pay Guaranteed Payments.
- Special rules for trusts and estates including multiple non-grantor trusts.
- Specified Service Trade or Business Limitation
  - Guidance provided in Proposed Regulations issued August 9, 2018
  - *Health, Law, Accounting, Actuarial Science, Performing Arts, Consulting, Athletics, Financial Services, Brokerage Services, any business where the principal asset is the reputation or skill of any one employee or owner, Investment Management, Trading or Dealing in Securities*

# General Tax Bill Changes

- C-Corps – 21% Flat Corporate Tax Rate – Beginning in 2018
- NOL rule changes eliminate carrybacks and cap carryforward utilization to 80% of taxable income.
- Luxury auto depreciation limits virtually tripled.
- Sec. 179 dollar limitation expanded for qualifying property used in a trade or business.
- Repeal of ACA individual mandate after 12/31/2018.
- Individual Income Top tax will fall to 37%, while the bracket range is expanded. New withholding tables issued Jan. 2018



# General Tax Bill Changes

- Increased Standard Deduction set to \$24,000 for MFJ returns (\$12K single). *Planning tip:* Put legal age working children on payroll.
- Repealed the deduction for personal exemptions; however child tax credits enhanced to \$2,000.
- \$750,000 debt cap for Mortgage interest limitation for debt after 12/15/17. \$1MM threshold still in place for debt incurred before 12/15/17. Interest deduction for HELOC is repealed after 12/31/17.
- Repeal of miscellaneous itemized deductions subject to 2% floor.
- Alimony paid is not deductible for MSA's after 12/31/18.
- Deduction for Moving expenses is suspended after 12/31/17.

# Estate Tax

- Unified Credit equivalent doubled to \$11.2 Million per taxpayer in 2018.
  - That's \$22.4M per married couple using portability.
- Stepped up basis for inherited assets still allowed.
- Planning still required for non tax purposes even if below the threshold for paying Estate tax.

# QUESTIONS?

Contact:

**James K. O'Connor, CPA**  
**joconnor@rgcocpa.com**

or

**Michael E. Helton, CPA**  
**mhelton@rgcocpa.com**

