



The Tax Cuts and Jobs Act: What Nonprofits Need To Address

The Tax Cuts and Jobs Act (the "Act") was signed into law on December 22, 2017. The Act was the most comprehensive overhaul of the U.S. tax code in over thirty years, and the Nonprofit community is especially concerned with how certain provisions, mainly the significant increase of the standard deduction and estate tax exemption, will impact charitable giving going forward.

While there have been several articles focusing on the substantial negative economic effects the Act will have on charitable giving, we wanted to address some of the lesser-discussed provisions that will directly affect nonprofits. This article discusses the provisions that, if overlooked, may cause stumbling blocks to your nonprofit organization.

The Unrelated Business Income Tax Rules Have Changed

The unrelated business income tax ("UBIT") is imposed on the unrelated business taxable income ("UBTI") of nonprofits that regularly carry a for-profit component with their activities.

Typical examples of unrelated business taxable income are advertising income, rental income on debt-financed property, and pass-through operating income from Partnerships and S corporations. Before the Act, nonprofits were able to combine all activities generating UBTI when calculating UBIT.

Now, the Act will impose a tax on nonprofits at the new corporate rate of 21% on income from each unrelated business activity. Nonprofits will no longer be able to use losses from an unprofitable unrelated business to net against taxable income of another profitable unrelated business.

Nonprofits should analyze each trade or business that generates UBTI and consider whether consolidating them would result in lower taxes. More guidance is needed from the IRS as to what exactly are separate UBIT activities and how such activities will be reported for purposes of calculating the UBIT.

Nonprofits with multiple activities that generate UBIT should consider whether they would benefit from creating a taxable subsidiary. A taxable subsidiary can also be an appropriate solution when the for-profit activity is a growing component of the Nonprofit.

There is the potential danger that a 501(c)(3) organization could lose its tax-exempt status if the for-profit activities are substantial in relation to your exempt purpose activities. Thus, now is an appropriate time to review your for-profit activities and plan accordingly.

Additionally, the Act includes the fringe benefits of paying for on-site gym memberships and commuting/parking expenses for employees as UBTI. While this might seem strange at first, these deductions have also been limited to for-profit entities under the Act.

These UBIT provisions were added to parallel the limit on deductibility by for-profit entities. It's important for nonprofits to review their transportation fringe benefits policies to prevent being caught off guard with a potential UBIT issue.

New Excise Tax On Executive Compensation

The Act imposes a new 21% excise tax on a Nonprofit's payment of compensation of \$1 million or more for its five highest-paid employees. With this change, nonprofits are brought into parity with taxable corporations, which are unable to deduct compensation in excess of \$1 million for certain employees.

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New Excise Tax On The Net Investment Income Of Certain Private Colleges And Universities

The Act imposes a new 1.4% excise tax on the net investment income (generally endowment earnings, interest, dividends, rents, royalties and capital gain net income reduced by expenses incurred to earn income) of nonprofit private colleges and universities with assets of at least \$500,000 per full-time student and more than 500 full-time students, 50% of which are in the U.S.

This new tax does not apply to public colleges and universities. Amounts used directly to carry out educational purpose are excluded from the calculation of net investment income for purposes of the excise tax.

Other Charitable Provisions

The deduction of payments for seating rights at college sports events has been removed.

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. Before the Act, this was a significant exception to the prohibition on "quid pro quo" contributions to charities.

Nonprofits and the Tax Cut And Jobs Act

This article reviews some of the more under the radar provisions under the Act that impact nonprofits. Further guidance from the IRS is expected and necessary on some provisions of the Act, which hopefully will clarify unclear provisions. Nonprofits must continue to stay informed and adapt to the changes while still concentrating on their critical missions at hand.

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