

Unrelated Business Income – Advertising

June 13, 2018

Introduction and Purpose

Generally, income generated from the sale of advertising is treated as income from an unrelated trade or business and may need to be reported on the University's tax return, Form 990-T. The purpose of this guide is to assist University departments in identifying advertising revenue and recording it appropriately. University departments may also refer to TMOG #5 – Unrelated Business Income – Corporate Sponsorships as a related guideline.

Advertising Defined

The term advertising means any message or other programming material which is broadcast or otherwise transmitted, published, displayed, or distributed, and which promotes or markets any trade or business, or any service, facility or product. The term includes messages containing qualitative or comparative language; price information or other indications of savings or value; an endorsement; or an inducement to purchase, sell, or use a product, service, or facility.

Advertising Medium

The advertising rules generally apply to the advertising in all means of University-owned communications. For example, advertising can be sold on a website, in a brochure, on a billboard, on a scoreboard, or on the back of a ticket. Generally, the medium used does not change the unrelated business income analysis.

Unrelated Business Income

Advertising revenue, like all other income derived by the University, must be tested against the three basic tests in order to determine whether it constitutes unrelated business income. For the revenue to be considered unrelated business income, it must be:

1. a trade or business,
2. regularly carried on, and
3. not substantially related to the University's exempt purpose.

Trade or Business

A standard test for determining the existence of a "trade or business" is whether the activity is carried on with the expectation and intent of realizing a profit. In most cases, the sale of advertising to commercial providers of goods and services meets this test, as long as the advertising or the sale of the publication itself is profitable.

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However, these rules are not intended to encompass a publication with little advertising, which is distributed free or at a nominal charge not intended to cover costs. For a publication to be considered an activity carried on for the production of income, it must be contemplated that the revenues from advertising in the publication or the revenues from sales of the publication, or both, will result in net income. Therefore, there will be no taxable unrelated business income because of the advertising when a publication as a whole is published at a loss.

Regularly Carried On

With respect to the “regularly carried on” facet, it is met if the advertising is part of a journal, newspaper, or similar activity occurring on a regular basis. Exempt organizations engaged in only sporadic business activities will not be considered regularly carried on if they are conducted without competitive and promotional efforts typical of commercial endeavors. On the other hand, where the sales are not merely casual, but are systematically and consistently promoted and carried on, they will be deemed regularly carried on. Key factors to consider include (1) whether volunteers or employees are soliciting the advertising, (2) if the activity is only intermittent and does not continue for an extended period, (3) the seasonal nature and concentrated efforts of the solicitation, and (4) the comparable activities of nonexempt organizations.

Not Substantially Related

The final area to consider is whether the advertising can be treated as “substantially related” to the University’s exempt purpose. Advertising income is often part of an overall exempt function, but the fact that the advertising is conducted as a component of an otherwise exempt function does not prevent the IRS from carving out the advertising income and taxing it as a separate trade or business. In addition, the fact that the generation of the advertising income depends wholly, or in part, upon the exempt function does not make the advertising income a related trade or business.

With that said, there may be times when advertising may be deemed related. When the solicitation, sale, and publication of the advertising are conducted by students, under the supervision and instruction of the University, such income may be deemed related to the University’s exempt purpose of teaching students. There may be other situations where advertising could be deemed to further an educational purpose, though this would be uncommon.

Taxation of Advertising

Income from the sale of advertising generally constitutes unrelated business income, taxable to the extent it exceeds the expenses directly related to the advertising. Business deductions that are directly connected with carrying on the advertising activity may be deducted when calculating net unrelated business income. When expenses are used to carry on both tax-exempt activities and unrelated activities, the expenses, depreciation, and similar items attributable to such activities must be allocated between the two uses on a reasonable basis.

University Steps

University departments selling advertising should record the revenue in account 520222 External Sales - Sale of Advertisements. In addition, the department should work with the Office of General Counsel to make sure an

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Advertising Agreement is being used for appropriate arrangements. The Tax Management Office should be contacted at taxhelp@umn.edu or 612-624-1053 so appropriate analysis and planning can be done with regards to any potential tax and reporting requirements.