Nonprofit Navigator

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Multiple sources of UBTI could mean more taxes for nonprofits

By Steven Taylor, CPA

When you think of nonprofits, taxes are probably not the first thing that come to mind as nonprofits are generally exempt from income tax. However, some nonprofits have alternative revenue sources that do not relate to their exempt purpose that would fall under Unrelated Business Taxable Income (UBTI).

New rule

Internal Revenue Code Section 512(a)(6) created a new rule in calculating UBTI. Nonprofits with more than one source of UBTI can no longer offset income from one source with losses from another source. UBTI must be computed separately with respect to each such trade or business. Before, nonprofits could combine revenue and expenses from all trade or businesses subject to UBTI. This new rule is effective for taxable years beginning after December 31, 2017.

UBTI will now be reported separately on Form 990-T for nonprofits with more than one unrelated trade or business. You will complete a separate schedule if you have more than one unrelated business, report total income for each business and subtract direct and indirect expenses for each to get the total UBTI for each unrelated trade or business on a separate basis.

Example

Nonprofit A has one exempt purpose program and two sources of UBTI, B and C. Let's say Nonprofit A has $75,000 of income from unrelated business B and $5,000 of income from unrelated business C. Nonprofit A also has direct expenses of $50,000 from unrelated business B and $5,000 from unrelated business C. Nonprofit A must allocate indirect expenses between its exempt purpose and both sources of UBTI. Nonprofit A has indirect expenses of $30,000 and has determined that it is reasonable to allocate $20,000 of the indirect expenses to the exempt purpose program, $8,000 to unrelated business B and $2,000 to unrelated business C. This table shows the calculation of UBTI under Internal Revenue Code Section 512(a)(6):

	Unrelated Business B	Unrelated Business C
Income	$75,000	$5,000
Direct expenses	$50,000	$5,000
Indirect expenses	$ 8,000	$2,000
UBTI	$17,000	$2,00

Prior to the rule change, the net UBTI would have been only $15,000. Although many nonprofits only have one type of UBTI, you should consult with your Henry+Horne accountant to see if this new rule will affect you.

If you have any questions, Steven can be reached at (480) 839-4900 or StevenT@hhcpa.com.

Fast Facts

- 150+ team members
- 50% are CPAs
- Arizona's largest locally owned accounting firm
- Your money stays in the state
- Well-known leader in CPA services for AZ nonprofits
- Nonprofit CPAs volunteer on boards and committees for local charities
- Your team provides complimentary CPE and customized presentations for nonprofit boards and staff

Bequests: determining when and how much to record
By Karen Lord, CPA

As an increasing number of nonprofit organizations develop gift acceptance policies and have planned giving departments, the number of bequests received is also rapidly increasing, especially as the number of Baby Boomers entering retirement continues to grow.

What exactly is a bequest? It's a gift of personal property or financial assets to an individual or organization through the provisions of a will, trust or estate plan upon death. There are four types of bequests:

- General bequests – a precise dollar amount of money or a percentage of the estate to be paid to a beneficiary taken from general assets and not a specific fund.
- Specific bequests – those that allocate a particular asset to a beneficiary.
- Demonstrative bequests – include distributions from or of a particular asset (i.e., a specific bank account or the sale of stock in a corporation).
- Residuary bequests – includes all property/assets not disposed of after all other bequests are paid out to beneficiaries and administrative expenses and estate taxes are paid.

For an organization, it is quite an honor to be named as a beneficiary. Donors often name nonprofit organizations in their will because they believe in the organization's mission, they want to honor a loved one and/or because they believe that their gift will be used wisely.

If your organization receives communication that you have been included as a beneficiary in a donor's will, you must determine if this represents an intention to give or an unconditional promise to give. This is imperative as it determines when the gift is recognized as a contribution. If the donor is living, they have the ability to modify their will, so your organization should only deem the notification that you are named as a beneficiary as an intention to give. Only upon the donor's death and when the will is declared valid by the probate court, does the intention to give become an unconditional promise to give. At that point in time, you would record the gift as a contribution.

Determining the value of the contribution to record is dependent on the type of bequest. If your organization is named as the beneficiary of a general bequest, which identifies a specific dollar amount, determining the value is straight forward. However, if you are named the beneficiary of a residuary bequest, specific bequest of a piece of property or a percentage of the estate, your organization must recognize the bequest by estimating the value of the gift to be received. This can be done by using the executor's estimate of the estate's assets and liabilities and the expected amount and time as to when your organization will receive payment of the interest in the estate. This can often be a difficult and a time-consuming process; however, your organization should have a reasonable basis to support your estimate. The executor may give a low fair value amount or a dollar range. Recording the low fair value or the low estimate of the range would be appropriate.

If you have any questions, Karen can be reached at (480) 839-4900 or KarenL@hhcpa.com.

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Henry+Horne has performed several audits of our annual financial statements, and each year they have submitted the reports on or before deadline. All members of the engagement team are very knowledgeable, extremely responsive and professional.