

UBIT - Unrelated Business Income Tax for Churches

Churches may engage in income-producing activities unrelated to their tax-exempt purposes, as long as the unrelated activities are not a substantial part of the organization's activities. However net income from such activities will be subject to UBIT (Unrelated Business Income Tax) if the following three conditions are met:

1. The activity constitutes a trade or business
2. The trade or business is regularly carried on, and
3. The trade or business is not substantially related to the organization's tax exempt purpose. (The fact that the organization uses the income to further its charitable or religious purposes does not make the activity substantially related to its exempt purposes.)

Exceptions to UBIT

Even if an activity meets the above three criteria, the church's income may not be subject to UBIT tax if it meets one of the following exceptions:

1. Substantially all of the work in operating the trade or business is performed by volunteers
2. The activity is conducted by the organization primarily for the convenience of its members, or
3. The trade or business involves the selling of merchandise substantially all of which was donated

In general, rents from real property, royalties, capital gains, and interest and dividends are not subject to the unrelated business income tax **unless financed with borrowed money.**

Examples of Frequent Church UBIT Activities

Advertising – This may include the sale of advertising space in weekly bulletins, magazines or journals, or on church or religious organization web sites. Generally this income is unrelated traded or business income.

Sale of merchandise and publications – This can be considered conduct of an unrelated trade or business if the items involved do not have a substantial relationship to the exempt purposes of the organization.

Rental Income – Generally rental income is excluded from UBIT. However, there are exceptions:

- a. If a church rents out property on which there is a debt outstanding (such as a mortgage), the rental income may constitute unrelated debt-financed income subject to UBIT. (However, if a church acquires debt-financed land and intends to use it for exempt purposes within 15 years of the time of acquisition, then income from the rental of the land may not constitute unrelated business income.)
- b. If personal services are rendered in connection with a rental, then the income may be UBIT income.

Parking Lots – If used for attending church, fees paid would not be subject to UBIT. If a church operates a parking lot used by the general public, parking fees would be taxable, as this activity would not substantially be related to the church tax exempt purpose, and parking fees are not treated as rent from real property. If the church enters into a lease with a third party who operates the church's parking lot and pays rent to the church, such payments would NOT be subject to tax, as they would constitute rent from real property.

Whether income-producing activity is an unrelated trade or business activity depends on all the facts and circumstances. See IRS Publication 598 for more information.

If a church has gross income of \$ 1,000 or more for any taxable year from the conduct of any unrelated trade or business, it is required to file IRS Form 990-T and pay UBIT tax. If this applies, a church should enlist guidance from a competent tax professional.