N. UBIT: CURRENT DEVELOPMENTS

by
Susan Ruth and Charles Barrett

1. Introduction

The 1997 CPE Text contains a Topic beginning at p. 238 that updates the area of unrelated business income tax ("UBIT") by addressing issues such as royalties, associate member dues, advertising, museum sales and travel tours. Although two years have passed since our last update, many of the same issues are still of great interest to exempt organizations and their representatives, as well as to Service employees. The past two years have seen a number of actions taken by Congress, the courts and the Service with respect to both items of perennial interest and newly identified matters.

In view of these ongoing actions, the purpose of this year's Topic is, once again, to update previous CPE Text discussions concerning a wide variety of developments during the past two years in the UBIT area. This Topic will focus on relatively recent legislative, judicial, regulatory and administrative actions affecting UBIT.

2. Travel Tours

Nonprofit organizations involved in travel tours continue to be under scrutiny by Congress and the for-profit travel industry, as well as the Service. IRS Key District Offices will be studying 88 exempt organizations that offer travel tours to determine whether the tours are educational, or whether they are primarily recreational, in which case any income they produce would be subject to UBIT. The travel tour area was discussed in the 1996 CPE Text at p. 215.

Exempt organizations that offer travel tours must make certain that the trips are consistent with the organizations' exempt purposes in order to avoid tax on tour income. An exempt organization that conducts a tour must be prepared, in case of an audit, to provide the Service with written documentation showing that the tour was "substantially related" to the organization's exempt purpose, which in the case of a museum, college or university would likely be educational.

Organizations have been urged to start the documentation process at the planning stages of the tour - not after the trip has been completed - and should continue documenting throughout the tour. In documenting the planning stages of the tour, an organization must indicate how a destination is chosen, the reason for the destination's selection, whether a guide will accompany the tour and other factors. The actual conduct of the tour must be documented as well.

Even if an exempt organization decides that a tour is not substantially related to its exempt purpose, records still should be kept to allocate expenses to the tour income.

A. Proposed Regulations

On April 20, 1998, the Service published proposed regulations (Reg-121268-97) intended to clarify when the travel and tour activities of exempt organizations are substantially related to the purposes for which exemption was granted. The proposed regulations are intended to augment the guidance that currently exists with respect to travel tours.

The proposed regulations would add a new section 1.513-7, which provides that the determination of whether the travel tour activities of an exempt organization are substantially related to the organization's exempt purpose depends upon the facts and circumstances. The proposed regulations set forth a series of examples to illustrate how various facts and circumstances would be analyzed.

The first example involves a university alumni association, that is described in IRC 501(c)(3). As part of its program, the association operates travel tours for its members and guests. The association works with travel agencies to schedule about ten trips annually to various locations around the world. The members pay a fee to the agency to participate in the tour, and the agency pays a fee to the association for each participant. While the association encourages members to continue their life-long learning, and a faculty member is invited to join the tour as a guest of the association, none of the tours includes any scheduled instruction or curriculum. The proposed regulation concludes that the program does not contribute importantly to the accomplishment of the organization's exempt purposes but, rather, is designed to generate revenue and, therefore, results in UBIT.

Example two involves an IRC 501(c)(3) organization formed to educate individuals about the geography and culture of the United States. In addition to offering courses and publishing periodicals and books, the organization offers study tours to national parks and other sites. The tours are conducted by teachers and other professional educators. The tours are open to all who agree to participate in the required program of study consisting of community college level course work related to the location to be visited on the tour. Five to six hours a day are devoted to organized study, preparation of reports, instruction and recitations by the students. The tour group brings along a library of relevant materials. The participants take an exam, and the state board of education awards credit for participation. The proposed regulation concludes that because the tour program included a substantial amount of required study, lectures, reports and examinations, and is accorded academic credit, the tours further the organization's exempt educational purpose. Accordingly, this tour does not constitute an unrelated trade or business.

The third example involves an IRC 501(c)(4) social welfare organization devoted to advocacy of a particular issue. On a regular basis the organization organizes tours for its members to Washington, D.C. The participants spend substantially all of their time meeting with legislators and government officials and attending briefings on policy developments related to the organization's area of concern. The regulation concludes that conducting this type of tour contributes importantly to the organization's social welfare purposes and does not constitute an unrelated trade or business.

Example 4 is substantially similar to the situation addressed in TAM 97-02-004 (August 29, 1996).

B. TAM 97-02-004

In this TAM the Service concluded that some categories of an organization's travel tours give rise to unrelated business taxable income ("UBTI"), while others serve the organization's exempt purposes and are not subject to tax. The subject of the TAM is a membership organization open to Americans of a specific heritage. Its purposes are to promote the creative survival and foster the unity of the people of that heritage. The organization's activities include conducting study missions, a commission on international affairs, dissemination of study materials and an international study program.

The organization considers its international travel program to be an essential element in achieving its exempt purposes. Consistent with its commitment to the creative survival of its people, the organization regards as essential the direct personal contact between Americans of such heritage and such communities throughout the world. In addition, visits to sites of religious, cultural and historic interest are considered vital to the realization of a religious, cultural and historic identity.

Participation in the tour program is only open to members. During 1990, the organization's travel catalog listed 32 tours, a substantial number of which were to the ethnic homeland. The TAM refers to these as Category "A" tours. The organization also sponsored trips to various other countries around the world (Categories B, C, D and E tours).

The organization's travel catalogue indicates that its Category A tours aim to provide participants with an intensive learning experience in the homeland of their people. Tour itineraries include visits to places of historic, religious and cultural significance, along with interaction with people from all walks of life.

Category B tour participants are provided with an intensive learning experience encompassing the discovery of their ethnic heritage. Day-to-day activities are accompanied by lectures by experts in history and civilization.

Category C tours include visits to museums and communities, but a substantial portion of the itineraries consists of vacation travel. Some of the tours consist of several days of recreational activities aboard luxurious cruise ships. Category D tours did not take place during the year in question due to lack of interest by the organization's members. The Category E tour, which was described as a "relaxing finale" to the tours, consisted of a few days spent at a year-round seaside resort.

In its analysis, the TAM advised that in order to determine if the conduct of a travel tour by an organization described in IRC 501(c)(3) is substantially related to an exempt purpose, it is necessary to ascertain the organization's primary purpose in offering the tour. Where the primary purpose behind conducting the travel tour is to further the organization's exempt purpose, such tour meets the substantially related test, and income earned therefrom is not subject to UBIT. The TAM noted that organizations must demonstrate clearly how each tour accomplishes one or more of its particular exempt purposes.

The TAM sets out several critical factors in its analysis. One critical factor is the method or methods that are used to accomplish the particular exempt purpose. In the case of educational organizations such as colleges or universities, the use of educational methodologies such as organized study, reports, lectures, library access and reading lists is likely to be considered educational. In the case of religious organizations such as churches, synagogues or mosques, the TAM noted, critical factors might include explicitly or implicitly religiously derived requirements to worship in particular locales, visits to sites of spiritual importance, and planning or leadership by clergy or appropriately trained lay persons.

Another critical factor is the ability to demonstrate from contemporaneous evidence that each tour is designed so that its primary purpose is to further one of the organization's exempt purposes. While allocation of time is not always conclusive, organizations should be prepared to demonstrate why it is not. The TAM noted that evidence reflecting the process of tour selection and design, advertising of tours and evidence of what actually happened during the tour, such as a trip report, is also evidentiary. Activities will also be evaluated to determine whether they are central to the tour's purpose. In this regard, the Service would look at whether a particular activity is voluntary, or whether alternate recreational activities are available.

Finally, a third critical element in the analysis of travel tours is whether there are relevant circumstances demonstrating that a particular purpose or purposes are being served. Choice of destination is important in this regard.

The Service took the position that the tours in Categories A and B were substantially related to the organization's exempt purposes. On the other hand, the Service concluded that the tours in Category C consisted of travel accomplishing primarily social, recreational and other purposes. The Service pointedly considered as significant a lack of contemporaneous documentation relating to the Category C tours.

The Service applied the "fragmentation rule" of IRC 513(c) and Reg. 1.513-1(b) and held that tours in Categories A and B were not subject to tax, while the tours in Categories C and E were determined to be taxable. The cancelled Category D tours would also have been subject to tax as well.

3. Royalties

The Service and the Tax Court continue to be at odds with respect to mailing lists and affinity credit cards. The Service continues to view the renting of a mailing list and the marketing of a credit card by an exempt organization as involving services typically provided to the commercial company, while the Tax Court has held that amounts derived from such undertakings constitute royalty income that is excluded from the computation of UBTI under IRC 512(b)(2). For more general information on royalties and mailing lists, see the 1994 CPE Text at p. 114.

A. Sierra Club and the Alumni cases

The affinity credit card aspect of Sierra Club, Inc. v. Commissioner, Tax Ct. Dkt. No. 8650-91, remains on remand to the Tax Court from the Ninth Circuit. The Court of Appeals previously determined that the Tax Court had improperly granted summary judgment to the Sierra Club on this issue by not viewing the evidence in the light most favorable to the Service. For a more detailed discussion of the Sierra Club litigation, see the 1997 CPE Text at p. 239.

In Alumni Association of the University of Oregon, Inc. v. Commissioner, T.C. Memo. 1996-63 and Oregon State University Alumni Association v. Commissioner, T.C. Memo. 1996-34, the Tax Court maintained its position that amounts derived from an affinity credit card program fall within the exception for royalty income under IRC 512(b)(2) and, therefore, do not constitute UBTI. Both Oregon Alumni cases (9th Cir. No. 96-70593 and No. 96-70565) remain on appeal as well. The Court of Appeals for the Ninth Circuit formally consolidated the cases "for all purposes" shortly before oral argument, which took place on September 11, 1997. For more information on the Tax Court opinions in these cases, see the 1997 CPE Text at p. 242.

While these three cases await further action, the Service decided that it would not appeal the decision of the Tax Court in yet another alumni association case, Mississippi State University Alumni, Inc. v. Commissioner, T.C. Memo. 1997-397. In that case, the Tax Court held, as in the earlier cases, that income received by an organization ("MSU Alumni") from an affinity credit card program constituted a royalty under IRC 512(b)(2). The court further concluded that payments with respect to the use of the organization's mailing list in the program were royalties as well.

MSU Alumni entered into a three year agreement with People's Bank and Trust ("PB&T") in 1987 allowing the bank to administer an affinity card program directed at the organization's members. The contract was renewed and amended in 1991, expressly noting that PB&T's payments to MSU Alumni were royalties.

Under the 1987 agreement, PB&T agreed to pay MSU Alumni based on the number of transactions, plus a supplement for each new cardholder or annual fee paid. MSU Alumni agreed to allow PB&T to write a letter over the signature of its (MSU Alumni's) executive director explaining that PB&T was the exclusive provider of the affinity cards. In addition, PB&T was accorded the exclusive right to use MSU Alumni's name and the trademark of the university on the affinity card and advertising materials. PB&T, which agreed to prepare and pay for all marketing materials, drafted the promotional literature and sent it to MSU Alumni's members, parents of students, faculty and staff. MSU Alumni provided its member list twice a year with monthly updates.

Although MSU Alumni was not required to do so, it did make copies of credit card applications available in its offices where interested visitors could pick them up. MSU Alumni did not contact PB&T with respect to the status of any applications or requests for credit limit increases.

It was represented that MSU Alumni's executive director met with PB&T's representatives about four times a year to discuss the contract, and MSU Alumni's marketing coordinator spent a negligible amount of time on matters relating to the contract. While MSU Alumni generally did not rent its mailing list, it did contract with a company to sell items bearing the MSU seal. The bank paid for advertisements in the alumni association newsletter and various student publications, and hired students to give out applications.

The Tax Court rejected each of the Service's arguments. As in the earlier affinity credit card cases, the Tax Court concluded that the bank's payments to the exempt organization "were for the use of valuable intangible property rights, not for services."

The court rejected the Service's contention that the organization regularly rented its mailing list as in the case of Disabled American Veterans v. Commissioner, 942 F.2d 309 (6th Cir. 1991). The court refused to accept the Service's argument that the regular receipt of income over the life of the contracts indicated that it regularly rented its mailing list.

The court compared the facts of the MSU Alumni case with those described in Sierra Club, Inc. v. Commissioner, 86 F.3d 1526 (9th Cir. 1996), where the taxpayer was entitled to set rental rates, review requests to rent the lists, and approve and schedule mailing. In that case (as discussed at length in the 1997 CPE Text), the Ninth Circuit concluded that the rental payments for the list were royalties, and the Sierra Club did not provide services with regard to the mailing lists. The court concluded that the case of MSU Alumni was more like Sierra Club than Disabled American Veterans.

In addition, the court distinguished the case from United States v. American Bar Endowment, 477 U.S. 105 (1986), in which the Endowment was held to have created unfair competition by conducting a trade or business. In this case, the court observed that it was PB&T, not MSU Alumni, that was competing with other credit card issuers. Likewise, the court rejected the Service's argument that because the organization had reported the memorabilia income as UBIT, it should report the income from PB&T as UBIT, noting that such disparate treatment does not deprive the income from the bank of its status as a royalty.

Finally, the court rejected the argument that Commissioner v. Danielson, 378 F.2d 771 (3rd Cir. 1967) precluded MSU Alumni from asserting that the payments under the original contract were royalties because the word "royalties" was not included in the contract until 1991. The court noted that it refused to accept that the enactment of IRC 513(h) implied that renting mailing lists is generally a trade or business. The opinion notes that Ways and Means Chair Rostenkowski stated that the enactment of IRC 513(h) "...carries no inference whatever that mailing list revenues beyond its scope or prior to the effective date should be considered taxable to an exempt organization."

4. Associate Member Dues

During the past two years associate member dues have received a good deal of attention from both Congress and the Service. Developments since this issue was discussed in the 1995 CPE Text at p. 67, and the 1997 CPE Text at p. 245, include legislation, publication of another Revenue Procedure and release of technical advice memoranda that apply general principles to particularly interesting facts.

In summary, associate member dues are amounts paid to membership organizations by persons who may or may not receive all the rights and privileges afforded full members. Associate membership is not a new development, as many organizations have long had various classes of members. Associate membership became a significant UBIT issue, however, in certain instances where the Service took the position (and the courts agreed) that exempt organizations created an associate (or limited benefit) member class in order for such individuals to qualify for insurance coverage, and their dues payments were merely payments for such insurance.

A. IRC 512(d) and Rev. Proc. 97-12

Rev. Proc. 95-21, 1995-1 C.B. 686, provides that dues payments from associate members will not be treated as gross income from the conduct of an unrelated trade or business unless the associate member category was formed or availed of for the principal purpose of producing unrelated business income. Rev. Proc. 97-12, 1997-1 C.B. 631, is substantially similar to its predecessor with two significant clarifying provisions.

First, the newer revenue procedure discusses IRC 512(d), which provides a "safe harbor" from UBIT for dues of $100 or less, indexed for inflation, paid to IRC 501(c)(5) agricultural or horticultural organizations as mandated by the Small Business Job Protection Act of 1996 (P.L. 104-188). The Act amended IRC 512 as it applies to the treatment of dues paid to IRC 501(c)(5) agricultural or horticultural organizations by adding IRC 512(d).

Under IRC 512(d), if an organization requires the payment of annual dues and the amount of the dues does not exceed $100, the dues will not be treated as derived from an unrelated trade or business. The statute provides that the $100 dues ceiling will be indexed according to a cost of living adjustment for tax years beginning in a calendar year after 1995. It also defines "dues" as any payment, whether or not specifically designated as dues, that is required to be made in order to be recognized as a member of the organization.

Secondly, Rev. Proc. 97-12 extends the application of Rev. Proc. 95-21 to organizations described in IRC 501(c)(6), such as business leagues, chambers of commerce, real estate boards and boards of trade.

Essentially, if there is real involvement by associate members in exempt function activities, in policy making, and in decision making, then the principal purpose of having associate members will not be considered to generate UBTI, and associate member dues will not be taxed. If, however, it is determined that the principal purpose for having such members is to raise additional revenue, and the requisite level of involvement in exempt activities is absent, then their dues will be taxable.

B. Application of Rev. Procs. 95-21 and 97-12 to a Labor Union

TAM 97-51-001 (April 25, 1997) discusses an IRC 501(c)(5) labor union ("M") which is affiliated with another labor union ("N") that operates as an independent division of M. M is also affiliated with its chartering organization ("P"). N has associate members who participate in its health insurance plan and collects dues from them. M receives $3.60 per year per associate member and then passes a portion of that amount on to P.

The TAM relied on the conclusions in American Postal Workers Union, AFL-CIO v. United States, 925 F.2d 450 (D.C. Cir. 1991), National Association of Postal Supervisors v. Commissioner, 944 F.2d 859 (Fed. Cir. 1991) and National League of Postmasters of the United States v. Commissioner, 86 F.3d 59 (4th Cir. 1996), all of which held that sponsoring and providing access to health insurance programs for associate or limited benefit members constitutes an unrelated trade or business. The TAM then applied Rev. Procs. 95-21 and 97-12 to determine whether revenues attributable to the dues from associate members constituted UBTI. The TAM concluded that the associate member category was formed and availed of for the principal purpose of producing unrelated income rather than to further any exempt purpose and, therefore, was not substantially related to M's exempt purpose.

The TAM reasoned that in order for associate members to have access to insurance, it is necessary for them to pay the annual fee, including M's specified share. Although M is not itself operating or sponsoring the insurance program, the TAM noted, access to the insurance is structured so that membership in the union and payment of the associate member dues are required.

In arriving at this conclusion, the TAM relied heavily on the provisions in the taxpayers' constitutions, noting that since M's constitution provides that it will receive a certain portion of associate member dues paid to N, M cannot attempt to recharacterize those amounts. In order for associate members to have access to insurance, it is necessary for them to pay the annual fee, including M's specified share. The TAM pointed out that the Service is respecting the separate identities of the two organizations and is not attributing N's activities to M but, rather, is focusing on M's role in providing access to insurance.

C. Application of the Rev. Procs. to an IRC 501(c)(6) Organization

In TAM 97-42-001 (June 26, 1997), the Service considered whether membership dues received from "allied members" of a professional association, ("M"), which is described in IRC 501(c)(6), constitute UBTI. In furtherance of its purposes, M (a) holds educational seminars and an annual exposition, (b) publishes a newsletter twice a year, a trade magazine ten times a year, and a buyers guide twice a year, and (c) employs individuals to bring matters of importance to the industry to the attention of the state legislatures.

M's bylaws provide that any person who is an owner or manager of an ("N"), an executive officer, or acts in a supervisory capacity for an N operating company is eligible for regular membership in M. In addition, the bylaws provide that purveyors or suppliers of any product or service to the industry of M and publishers of N magazines or similar publications are eligible for allied membership.

Regular members in good standing are accorded voting rights at regular meetings and are eligible to be candidates for the board of directors. The bylaws also provide for chapters. While at least a majority of the directors of the individual chapters must be regular members, all members, regular and allied, are eligible to vote and run for chapter offices. In addition, the membership brochure enumerates various other benefits accorded allied members, including a free listing in the buyers guide, regularly held meetings with networking opportunities, advertising at discount rates in and a subscription to the M trade magazine, member access mailing, information on special subjects, receipt of information about state rules and regulations, frequent seminars and roundtables, participation in the various insurance programs, and use of M's logo in its advertising.

In this case, the Service concluded, it is clear that allied member rights were not as extensive as those accorded regular members, however the organization provided allied

members with benefits and rights much more pervasive than those of the associate members in National Association of Postal Supervisors v. United States, American Postal Workers Union, AFL-CIO v. United States, and National League of Postmasters of the United States v. Commissioner, all supra. M's allied members had a voice in the operations of M, as they were able to vote in the chapter operations, which formed a significant part of M's operations, were able to serve as officers at the chapter level, act as representatives and officers of their chapter at M's meetings and be represented in the planning of M's major activities such as the annual trade show and convention. M encouraged the allied members to participate as fully as possible. The Service found that the dichotomy between regular and allied members did not evidence an organizational purpose to generate unrelated business income, since the dues for allied members could be as low as the lowest regular membership dues, and the highest allied membership dues were far less than the highest regular membership dues.

Finally, the TAM concluded that all the facts and circumstances support a finding that the allied member category was not formed or availed of for the principal purpose of producing unrelated business income. Applying the principles set forth in Rev. Procs. 95-21 and 97-12, supra, it was concluded that the allied membership category was formed or availed of for the principal purpose of furthering M's exempt purposes under IRC 501(c)(6), and the dues payments, therefore, did not constitute UBTI.

5. Corporate Sponsorship

This issue was discussed at length in both the 1993 CPE Text at p. 80 and the 1994 CPE Text at p. 244. It was also the subject of proposed regulations that were issued on January 19, 1993. Last year Congress enacted new legislation addressing this matter.

A. IRC 513(i)

Section 965 of the Taxpayer Relief Act of 1997 added IRC 513(i) in order to reduce the uncertainty with regard to the treatment for UBIT purposes of corporate sponsorship payments to exempt organizations. Congress felt that it was appropriate to distinguish sponsorship payments for which the donor receives no substantial return benefit other than the use or acknowledgment of the donor's name or logo as part of a sponsored event, which would not be subject to UBIT, from payments made in exchange for advertising provided by the recipient organization, which would be subject to UBIT.

Under IRC 513(i), "qualified sponsorship payments" received by an exempt organization (or State college or university described in IRC 511(a)(2)(B)) are exempt from UBIT. "Qualified sponsorship payments" are defined as any payment made by a person engaged in a trade or business with respect to which the person will receive no substantial return benefit other than the use or acknowledgment of the name or logo (or product lines) of the person's trade or business in connection with the organization's activities. In determining whether a

payment is a qualified sponsorship payment, it is not relevant whether the sponsored activity is related or unrelated to the organization's exempt purpose. Such a use or acknowledgment does not include advertising of such person's products or services, i.e., qualitative or comparative language, price information or other indications of savings or value, or an endorsement or other indication of savings or products or services.

The legislative history (see H.R. Rep. No. 105-148, 105th Cong., 1st Sess. 414 (1997)) indicates that if, in return for receiving a sponsorship payment, an organization promises to use the sponsor's name or logo to acknowledge the sponsor's support for an educational or fundraising event conducted by the organization, such payment will not be subject to UBIT. On the other hand, however, if the organization provides advertising of a sponsor's products, the payment made to the organization by the sponsor in order to receive such advertising will be subject to UBIT provided that the other requirements for UBIT liability are satisfied. This is consistent with Prop. Treas. Reg. 1.513-4, which provides that the use of promotional logos or slogans that are an established part of the sponsor's identity would not, by itself, constitute advertising for purposes of determining whether a payment is a qualified sponsorship payment.

The legislative history also suggests that the term "qualified sponsorship payment" does not include any payment whose amount is contingent, by contract or otherwise, upon the level of attendance at an event, broadcast ratings, or other factors indicating the degree of public exposure to an activity. However, the fact that a sponsorship payment is contingent upon an event actually taking place or being broadcast, in and of itself, will not cause the payment to fail to be a qualified sponsorship payment. In addition, mere distribution or display of a sponsor's products by the sponsor or the exempt organization to the general public at a sponsored event, whether for free or for remuneration, will be considered to be "use or acknowledgment" of the sponsor's product lines (as opposed to advertising) and, thus, will not affect the determination of whether a payment made by the sponsor is a qualified sponsorship payment.

Further, the legislative history notes that IRC 513(i) does not apply to payments that entitle the payor to the use or acknowledgment of the payor's trade or business name or logo (or product lines) in an exempt organization's periodicals. Such payments are outside the qualified sponsorship payment provisions's safe-harbor exclusion and, therefore, will be governed by the general rules that determine whether the payment is subject to UBIT. Thus, for example, payments that entitle the payor to a depiction of its name or logo in an exempt organization's periodical may or may not be subject to UBIT, depending on the application of the rules regarding periodical advertising and nontaxable donor recognition. For this purpose, the term "periodical" means regularly scheduled and printed material published by (or on behalf of) the payee organization that is not related to and primarily distributed in connection with a specific event conducted by the payee organization. For example, the provision will not apply to payments that lead to acknowledgments in a monthly journal, but will apply if a

sponsor receives an acknowledgment in a program or brochure distributed at a sponsored event. In addition, the safe-harbor exclusion does not apply to payments made in connection with "qualified convention or trade show activities," as defined in IRC 513(d)(3).

Unlike the so-called "tainting rule" contained in the proposed regulations, IRC 513(i) specifically provides for an allocation, whereby, to the extent that a portion of a payment would (if made as a separate payment) be a qualified sponsorship payment, such portion of the payment will be treated as a separate payment. Thus, if a sponsorship payment made to an exempt organization entitles the sponsor to both product advertising and use or acknowledgment of the sponsor's name or logo by the organization, then UBIT will not apply to the amount of such payment that exceeds the fair market value of the product advertising provided to the sponsor. In addition, the provision of facilities, services or other privileges by an exempt organization to a sponsor or the sponsor's designees (such as complimentary tickets, pro-am playing spots in golf tournaments, or receptions for major donors) in connection with a sponsorship payment will not affect the determination of whether the payment is a qualified sponsorship payment.

Rather, the provision of such goods or services will be evaluated as a separate transaction in determining whether the organization has UBTI from the event. In general, if such services or facilities do not constitute a substantial return benefit, or if the provision of such services or facilities is a related business activity, then the payments attributable to such services or facilities will not be subject to UBIT. Also, the legislative history clarifies that just as the provision of facilities, services or other privileges by an exempt organization to a sponsor or the sponsor's designee (complimentary tickets, pro-am playing spots in golf tournaments, or receptions for donors) will be treated as a separate transaction that does not affect the determination of whether a sponsorship payment is a qualified sponsorship payment, a sponsor's receipt of a license to use an intangible asset (e.g. a trademark, logo, or designation) of the exempt organization likewise will be treated as separate from the qualified sponsorship transaction in determining whether the organization has UBTI.

IRC 513(i) applies to qualified sponsorship payments solicited or received after December 31, 1997. No inference is intended as to whether any sponsorship payment received prior to 1998 was subject to UBIT. It should be noted that IRC 513(i) provides an appropriate framework for the resolution of corporate sponsorship issues arising in years prior to January 1, 1998.

B. Acknowledgment v. Advertisement

The line between a permissible acknowledgment and a taxable advertisement is at the heart of each corporate sponsorship case. TAM 98-05-001 (October 7, 1997) considered whether an organization, established to increase interest in and improve the breeds of some animals and to hold an annual show, is described in IRC 501(c)(4), and whether it is subject to UBIT on income from the sale of broadcasting rights and/or corporate sponsorship revenue.

The organization sold the television broadcast rights for the annual show to a commercial network, enabling the event to reach a much broader audience. A sponsoring pet food company received a number of benefits from the organization in return for an annual payment, including discounted booth space, two full-page ads in the show catalogue, the right to advertise its support of the show and survey the "Best of Breed" winners for advertising purposes. In addition, the organization could include its half-page logo and identification on the back of the premium list, and its products' names appeared on judging program envelopes and armbands worn by exhibitors.

The taxpayer agreed to use all reasonable efforts to maximize the sponsor's visibility and publicity arising out of its participation. Most of the organization's income was from the show.

The TAM concluded that the sale of the broadcast rights to the annual show furthered the organization's social welfare purposes by making the show available to a wider audience. The TAM took the position that the agreements did not require the organization to do anything for the pet food company that would rise to the level of prohibited advertising. The TAM noted that the ad submitted as representative contained no language comparing the pet food company's products with others or claiming that it is rated best by veterinarians. Finally, the TAM concluded that the identification logos used on armbands, brochures, etc., are in the nature of acknowledgments. Furthermore, the right to "survey" best of breed winners does not result in UBIT, as the competitors are not obligated in any way to participate in pet food advertisements.

6. Subsidiaries of Exempt Organizations - IRC 512(b)(13)

Over the years this has been a popular topic in a number of CPE Texts: 1980 at p. 245, 1986 at p. 37 and 1987 at p. 52. Last year Congress revised the rules applicable to some of the revenues received by exempt organizations from their subsidiaries.

IRC 512(b)(13) was originally enacted (as IRC 512(b)(15)), in part, to prevent subsidiaries of exempt organizations from reducing their otherwise taxable income by borrowing, leasing, or licensing assets from an exempt parent organization at inflated levels. In addition, however, IRC 512(b)(13) is intended to prevent a tax-exempt parent from obtaining what is, in effect, a tax-free return on capital invested in its subsidiary. Because of the way in which this provision was drafted, organizations were often able to avoid its application, especially by creatively planning around the control test. For example, the issuance of 21 percent of nonvoting stock with nominal value to a separate friendly party, or the use of tiered or brother/sister subsidiaries were often effective in thwarting the rules under IRC 512(b)(13). Congress believed that modifications to the control requirement and inclusion of attribution rules will insure that this provision works in a manner consistent with its intended purpose.

The Taxpayer Relief Act of 1997 modifies the test for determining "control" for purposes of IRC 512(b)(13). Control now means (in the case of a stock corporation) ownership by vote or value of more than 50% of the stock. In the case of a partnership or other entity, control means ownership of more than 50 percent of the profits, capital or beneficial interests.

In addition, the TRA of 1997 applies the constructive ownership rules of IRC 318 for purposes of IRC 512(b)(13). Thus, an exempt parent organization is deemed to control any subsidiary in which it holds more than 50 percent of the voting power or value, directly (as in the case of a first tier subsidiary) or indirectly (as in the case of a second tier subsidiary).

Congress also made technical modifications to the method provided for determining how much of an interest, rent, annuity, or royalty payment made by a controlled entity to an exempt organization is includible in the latter organization's UBIT. Such payments are subject to UBIT to the extent the payment reduces the net unrelated business income (or increases any net unrelated loss) of the controlled entity.

The revised provisions in IRC 512(b)(13) generally apply to taxable years beginning after enactment. They do not apply to any payment made during the first two taxable years after the date of enactment if such payment is made pursuant to a binding contract in effect on June 8, 1997, and at all times thereafter before such payment.

7. Museum Gift Shop Sales and Use of Museum Facilities

The issue of museum gift shop sales was also discussed in the 1997 CPE Text at p. 257.

A. Application of the Primary Purpose Test

TAM 97-20-002 (November 26, 1996) revisits the issue of liability of an art museum for UBIT, focusing particularly on the proceeds from its sales of children's merchandise, as well as the receipts from restaurant business with members of the public who are not museum patrons.

Many of the museum sales issues were addressed previously in TAM 83-26-003 (November 17, 1982). The earlier TAM took a more general view that it would characterize the sale of children's interpretive teaching items that have artistic themes as being in furtherance of educational purposes.

Exploring this area in greater detail, TAM 97-20-002 applied a primary purpose test to determine if the sale of an item by a museum is related to its exempt purpose. Where the primary purpose behind the production and sale of the item is utilitarian, ornamental, a souvenir in nature, or only generally educational, the Service position is that it should not be considered "substantially related" within the meaning of IRC 513. Where, however, the

primary purpose behind the production and sales activity is to further the organization's exempt purpose, the sale is related, even though the item has a utilitarian function or value.

In applying the "primary purpose" test, the Service looks to the nature, scope and motivation for the particular sales activities. For example, the degree of connection between the item and the museum's collection and the extent to which the item relates to the form and design of the original item are considered. Size, location, accuracy of the representation as well as the overall impression conveyed by the article are to be considered. One must consider whether the dominant impression one gains from viewing or using the article relates to the original article and determine whether the non-charitable use or function predominates.

Many of the children's books and toys were found to be related to the museums's collections. Sales of items that are reproductions or adaptations of articles displayed in the museum would generally constitute related trade or business. While certain items may have a utilitarian purpose, they may contribute to the museum's exempt purpose by increasing the public's awareness of the period's art and history.

Articles that develop a child's artistic skills were deemed to be substantially related, as opposed to the sales of items which only generally develop a child's motor skills. The TAM pointed to Rev. Rul. 73-105, 1973-1 C.B. 264, which notes that the fact that the sale of the items could, in another context, be related to the exempt purpose of another educational organization does not change the conclusion that, in this context, such sales do not contribute importantly to this organization's exempt purpose.

In addition, the TAM concluded that the operation of the restaurant is a trade or business regularly carried on that is, in part, unrelated to the museum's exempt purpose. The Service reasoned that the restaurant's size and scope were not commensurate with the needs of the staff and visitors and was designed, in part, to serve as a restaurant for the general public.

Under the "fragmentation rule" of IRC 513(c), the unrelated segments of a trade or business must be separated from the related aspects and, therefore, restaurant sales to museum visitors and employees would not constitute UBTI, while sales to those who do not pay admission to the museum would constitute UBTI.

B. Renting of a Museum's Facilities

Museums are increasingly becoming involved in the rental of their facilities as the locale for balls, benefit dinners, award ceremonies and other business and social affairs. In TAM 97-02-003 (August 28, 1996), the Service considered the rental of museum facilities to corporate and business patrons for special events to constitute an unrelated trade or business. While acknowledging that there are educational aspects to the museum's rental of its facilities for business and social functions such as business meetings, awards dinners, cocktail parties

and dinner dances, the TAM pointed out that these educational aspects are clearly ancillary to the events' principal business and social purposes.

The TAM distinguished this situation from a case in which an outside sponsor asks the museum to create an educational program for its participants and, incidentally, food and other services are provided. Furthermore, relying on Reg. 1.512(b)-1(c)(5), the TAM noted that the rental income exception is not available, as providing such services is primarily for the benefit of the sponsoring organization, and the services are other than those ordinarily or customarily rendered in connection with rentals that come within IRC 512(b)(3).

In John W. Madden, Jr., et al. v. Commissioner, T.C. Memo. 1997-395, the Tax Court considered various rental activities of an outdoor museum, which owned an amphitheater, and concluded that while the organization did not generate UBTI from leasing building spaces to the public, it did incur liability for UBIT on the lease of an amphitheater to a particular company, MCA.

Madden formed a company to develop and manage an office complex on 200 acres in Denver, Colorado, and founded the Museum of Outdoor Arts to promote the public's interest in art forms through an outdoor and indoor museum.

During the years at issue, the museum employed a related maintenance company, GMC, to perform maintenance work for the museum for special events held on the premises under leases with the museum. From 1985 to 1989 the museum derived $31,000 in revenue from these special events and incurred $26,000 in expenses.

In addition to leasing space for these smaller, individual, special events, the museum leased, on a long-term basis, an outdoor amphitheater to MCA Concerts, Inc., which held various concerts at the theater featuring many popular performers. This lease specified that MCA would pay the museum a fixed percentage of its gross receipts but not less than $120,000 per year.

The Service argued that the revenues received by the museum from the special event leasing were subject to UBIT. The Tax Court followed a traditional three step analysis, noting that all the elements are conjunctive and must be present for there to be UBTI.

In contrast to the approach taken in TAM 97-02-003, the court agreed with the museum that leasing spaces to the public for special events is substantially related to the museum's exempt purpose. The museum argued that the events were intended mainly to expose outdoor art work to people who otherwise would not have seen it, rather than as a revenue generating activity. In its analysis, the court considered as significant the manner in which the leasing was conducted, and the fact that the annual revenue from the activity was not significant.

However, the court disagreed with the museum's position with respect to the lease of the amphitheater to MCA and rejected the museum's contention that the activity did not constitute a trade or business and was not regularly carried on. The court reasoned that the lease was not a short-term arrangement, the amphitheater could seat 18,000 patrons, and the museum was required to make parking and security arrangements under the lease. The court took issue with the museum's contention that it could have put on the performances itself, and that the lease substantially furthered its exempt purpose. In rejecting this argument, the court emphasized that the amount of money involved was substantial, and MCA put on performances by popular performers and commanded high prices.

As in TAM 97-02-003, the museum also failed to convince the court that the MCA lease fell within the real property rental exception under IRC 512(b)(3) and the regulations thereunder, which require that (1) a landlord not render certain services to the tenant, and (2) the determination of rent not be dependent on profits.

The court disagreed with the Service's contention that the museum rendered services to MCA by securing parking and providing security and maintenance services, concluding that the services were of a type usually and customarily rendered by landlords to tenants. However, the court concurred in the Service's position that the rent under the MCA lease was dependent on profits, rejecting the museum's suggestion that the court recognize a de minimis exception to the requirement that the determination of rent not be dependent on profits.

The Madden case also addressed a number of issues involving self-dealing under IRC 4941.

8. Advertising

A. Contractors and Control

In State Police Association of Massachusetts v. Commissioner, 125 F.3d 1 (1st Cir. 1997), cert. denied (February 23, 1998), the Court of Appeals upheld the decision of the Tax Court (T.C. Memo. 1996-407), that a state police association is liable for UBIT from advertising solicited by another entity under a contract for its annual publication.

The taxpayer is an IRC 501(c)(5) labor organization that operates on behalf of state police officers. The association publishes an annual yearbook consisting of photographs, articles, a business directory and advertisements. Gross receipts related to the publication for the years at issue totalled $8,798,211. Of this, the association retained somewhat over 40% of the receipts. A deficiency was assessed by the Service for taxes due on the advertising income.

On the merits, the association advanced two challenges: it asserted that the activities in question did not constitute a trade or business and that, in any event, the activities were not regularly carried on.

The operating model permitted the association to exercise significant control over the sales of the advertising, the handling of the funds generated and the publication of the yearbook. The association contracted with two companies over a number of years to solicit advertisements for the publication and to publish the book. The telemarketers were considered joint employees of the association and the outside firm. Troopers monitored all solicitations, and the association retained the right to inspect, without prior notice, the field offices from which solicitations were done. Prospective customers were offered the opportunity to purchase display advertisements and lists. The association produced five regional editions with common editorial material.

Payments for the ads sold were made to the association, which deposited the receipts in its account. The association made a weekly accounting, retaining a stipulated percentage for itself, paying a set percentage of the gross receipts to the telemarketers, defraying the costs of the publication and keeping any excess.

The association's members acted as the editorial staff, writing and editing articles and approving the contents of the yearbook. The publication was distributed at various troopers' barracks, at the annual picnic and on other occasions. Some copies were distributed to advertisers.

The Service maintained that the association was engaged in the business of selling advertising. The association took the position that it did not engage in that business, but merely used the display ads to identify sponsors. The Tax Court and the Court of Appeals rejected this argument as well as the organization's belated attempt to recharacterize the advertisements as acknowledgments within the meaning of Prop. Treas. Reg. 1.513-4, noting that the proposed regulation, by its terms, does not apply to periodicals produced by tax-exempt organizations.

The Court of Appeals maintained that the Service's view was more in keeping with common sense and noted that even the association referred to the displays and listings as advertisements during the first four years of the venture. Furthermore, the court found well-reasoned precedent for the Service's position in Fraternal Order of Police v. Commissioner, 87 T.C. 747 (1986), aff'd 853 F.2d 717 (7th Cir 1987). In both cases the publications included display ads, a directory and a message asking readers to patronize the businesses listed. In both cases, the size of the insertion was directly proportionate to the price charged, and in both instances the organizations had described the insertions as advertisements. The Court of Appeals noted its view that the FOP case was correctly decided and found that the Tax Court did not err in finding that the association's solicitation, sale and publication of the displays and listings constitute advertising.

In addition, the court rejected the association's fallback argument that the Service erred in treating the outside firms as agents of the association rather than as independent contractors. The court was not persuaded, noting that an independent contractor can be an agent if and to the extent that the contractor acts for the benefit and under the control of another in a transaction.

In examining the relationship between the contractors and the association, the court noted that no single factor is controlling, but rather it depends on many factors, including control over the manner and means of performing the work, the skill required, the method of payment, the duration of the relationship, etc. The Court of Appeals supported the position of the Tax Court, noting that the manner in which the association conducts its affairs undercuts its claim that it lacked the requisite degree of control over the outside firm's activities.

The association also failed to convince the court that the activities were not regularly carried on. The Court of Appeals rejected the association's attempts to rely on National Collegiate Athletic Association v. Commissioner, 914 F.2d 1417 (10th Cir. 1990), action on decision, 1991-015 (July 3, 1991) (nonacq.), and other cases in which the advertising activity was tied to the program for a specific event and which depended on Reg. 1.513-1(c)(2)(ii). That section specifically provides that publication of advertising in programs for sports events or music or drama performances will not ordinarily be deemed to be the carrying on of a trade or business. In addition, the Court of Appeals pointed to Reg. 1.513-1(b) to distinguish the case from NCAA and similar cases, in that the publication is not pegged to a particular event. In such a case, the opinion notes, the court must look to the activities which collectively comprise the business. Reg. 1.513-1(b) refers to the activities of soliciting, selling and publishing advertising as a singular business. Those activities were carried on by the association approximately 46 weeks per year. Finally, relying on Reg. 1.513-1(c), the court rejected the association's argument that it did not regularly engage in a business because it did not carry on the advertising activity with the same entrepreneurial zeal that might typify a commercial operation. The court noted that the regulations require only that the activity in question is to be judged in light of the purpose of the tax, but does not require that either actual competition or competitive equality be shown. Accordingly, the Court of Appeals determined that there was no clear error by the Tax Court, and the assessment of the Service should be upheld.

B. Computation of Advertising Income - The Pro Rata Allocation Test

TAM 97-34-002 (August 22, 1997) considered the appropriate computation of an exempt organization's circulation income under Reg. 1.512(a)-1(f)(4)(iii). The subject organization, which is described in IRC 501(c)(5), has different types of membership including chapter associations. Chapters are self-governing and independent in their internal operations. The organization published a magazine for one of its chapters that was distributed only to association members who are also members of the chapter. In an earlier TAM, the Service stated that revenues from the magazine advertising were subject to UBIT.

Pursuant to Reg. 1.512(a)-1(f)(4)(iii), circulation income includes a portion of membership receipts when the right to receive the publication is associated with membership status in the organization for which dues, fees, or other charges are received. The portion of membership receipts included in circulation income is determined by the ratio of total periodical costs to those costs plus the cost of other exempt organization activities.

The TAM reasoned that since only chapter members had the right to receive the magazine, the chapter was "the organization" for purposes of determining membership receipts. In addition, the TAM further concluded that the chapter was also "the organization" for purposes of determining the "the cost of other exempt activities of the organization" and, therefore, only expenses attributable to the chapter should be used to compute circulation income.

9. Gambling

A. Pull Tabs - Bingo v. Instant Bingo

In Julius M. Israel Lodge of B'nai B'rith No. 2113 v. Commissioner, 98 F.3d 190 (5th Cir. 1996), the Court of Appeals affirmed the Tax Court's decision that the lodge's instant bingo games did not qualify for the "bingo game exception" to UBIT, where the instant bingo game player did not place the markers over randomly called numbers in an attempt to form preselected patterns but, rather, purchased a prepackaged card and removed "pull tabs" to determine whether numbers on the front of the card match the numbers of the back of the card.

The lodge conducted traditional bingo as well as an instant bingo operation. Both are authorized and conducted in accordance with applicable state bingo laws. Upon audit, the Service determined that the instant bingo activities generated UBTI. The Service's position was that instant bingo, in contrast to regular bingo, does not constitute "bingo games" within the meaning of IRC 513(f), which excepts the sponsorship of certain bingo games from the definition of unrelated trade or business. The Tax Court sustained the Service's position.

The Court of Appeals looked first to the plain language of the statute (IRC 513(f)) as a starting point for its analysis and concluded that the taxpayer's instant bingo is devoid of the critical element of bingo that runs through the ordinary, every day definition - that players place markers over randomly called numbers in an attempt to form a preselected pattern.

The Court of Appeals upheld the Tax Court's opinion that participation by the instant bingo players in the game is wholly independent of one another and requires only that the player remove a pull tab to win. The Court of Appeals agreed with the Tax Court's view that instant bingo is for all intents and purposes a lottery. The court further noted that even if the instant bingo game met the preliminary requirement of IRC 513(f) that it be "any game of

bingo," it would still fail to meet the secondary requirement - that the winners be determined in the presence of all persons placing wagers in such games." This conclusion, the court reasoned, is compelled by the fact that winners in the instant bingo games are determined at the time the deck of cards is manufactured and, thus, the winners are already predetermined outside the presence of any other external events, such as the random calling of numbers in a "traditional bingo" game.

B. Computation of Tax

The treatment of "instant bingo" proceeds was addressed by the Tax Court in Women of the Motion Picture Industry, et al. v. Commissioner, T.C. Memo. 1997-518. The Tax Court considered whether exempt organizations that conduct "instant bingo" games are entitled to business expense deductions under IRC 162 for amounts transferred from their segregated instant bingo bank accounts to their general accounts. The petitioners, including several exempt organizations, argued that under state law, transfers from their instant bingo accounts to their general accounts qualified as charitable disbursements; however, the Tax Court concluded that state law is not dispositive of the issue. The court found that under federal law "...the transfer of 'Instant Bingo' proceeds to an organization's general fund is no more deductible than would be a contribution to a reserve for future liabilities."

The court did find, however, that one of the petitioners, the Waldorf School Association of Texas, paid $1.2 million to its bookkeeper during the year 1989, and that it could deduct a percentage of those expenses based upon what the ratio of its instant bingo proceeds was to its total bingo proceeds. The Tax Court further concluded that the Waldorf School Association of Texas was entitled to deduct as an ordinary and necessary business expense under IRC 162 the entire amount of its charitable payments in excess of the minimum percentage (35%) required to be distributed under state law.

The court rejected the Service's argument that attempted to distinguish the case from South End Italian Independent Club, Inc. v. Commissioner, 87 T.C. 168 (1986), acq. in result, 1987-2 C.B. 1. In that case the court considered whether a social club's donations from beano game proceeds were deductible as business expenses in determining UBTI. There, state law required that profits shall be used for charitable, religious or educational purposes and shall not be distributed to the members of the organization. In finding that the donations were not charitable contributions, the court concluded that the organization was under a legal compulsion to make the donations and, therefore, such amounts could not be considered as contributions. Further, since the social club could have lost its license if it were not in compliance with the distribution requirements, the distributions were, in effect, a quid pro quo for the bingo license.

The court concluded that the Waldorf School risked losing its bingo license, if it used any part of its net bingo proceeds for other than charitable purposes and, therefore, as in the South End Italian Club case, the Waldorf School was assured that its license would not be revoked by making the contributions in excess of the statutory minimum.

10. Miscellaneous Issues

A. Covenant Not to Compete

In Ohio Farm Bureau Federation v. Commissioner, 106 T.C. 222 (1996), (discussed with respect to administrative services in the 1997 CPE Text at p. 253), an organization entered into a written contract with a statewide cooperative it formed. Under the contract, the Bureau agreed to perform educational and promotional activities for the cooperative in exchange for a fee. After many years, the Bureau and the cooperative entered into a termination agreement wherein the Bureau agreed not to sponsor or promote a competing cooperative on an exclusive basis. In consideration for the nonsponsorship and noncompetition agreement, the Bureau received a substantial payment. The Tax Court concluded that the fees received pursuant to the agreement did not result in UBIT, as it was a one time activity and did not constitute a trade or business that was regularly carried on.

The Office of Chief Counsel previously had reached a contrary conclusion in G.C.M 39865 (December 12, 1991) in a case involving a cemetery which entered into a covenant not to compete with a mortuary as part of a sales agreement. Counsel took the position that whether an activity is a trade or business does not depend on whether it is active or passive but, rather, whether it is conducted with a profit motive. In addition, Counsel concluded that the covenant not to compete was a regularly carried on activity because the obligation continues throughout the term of the noncompetition agreement. In addition, it was concluded that the obligation not to compete did not contribute importantly to the cemetery's exempt purpose.

With little comment, the Office of Chief Counsel, in G.C.M. 39891 (January 3, 1997), revoked its position as enunciated in the 1991 G.C.M. and noted the Tax Court's decision in the Ohio Farm Bureau Federation case.

B. Golf

Universities, as well as other exempt organizations, have found that golf facilities can be valuable sources of revenue, and the Service has actively pursued cases, carefully looking at the various classes of users as well as the organization's exempt purposes.

TAM 96-45-004 (July 17, 1996) addressed the issue of whether amounts received by a state-assisted university from use of its golf course by various classes of individuals constituted UBTI. The university argued that no trade or business exists, basing its argument primarily upon the lack of a profit motive, and claimed that the golf course was important to the university development program. However, the Service rejected this argument, noting that it is indisputable that the university offers use of the course for a profit and that it constitutes the operation of a trade or business. Similarly, the Service concluded, the business is regularly carried on since the course is open to play by certain classes of members six days a week.

The TAM went on to consider whether alumni and President's Club members' use is substantially related to the university's exempt purpose under IRC 513(a), and whether alumni and President's Club members should be treated differently from members of the general public in this regard. The TAM, relying on Rev. Rul. 78-43, 1978-1 C.B. 164, refused to distinguish the two classes from the general public. The Service specifically rejected the argument that by making the golf course available, the university is providing an inducement for President's Club members and alumni to make contributions. Furthermore, the Service concluded that the organization has failed to establish the existence of a substantial causal relationship between alumni and President's Club member use of the golf course and the accomplishment of any exempt educational purpose.

Clearly, amounts derived from students and employees who played on the golf course would not be subject to UBIT; however, the TAM considered whether the children and spouses of students and employees come within the "convenience exception" of IRC 513(a)(2). The TAM looked to the clear language of the statutory exception. IRC 513(a)(2) states that the term unrelated business income, in the case of a college or university, does not include any trade or business carried on primarily for the convenience of members, students, patients, officers, or employees. Accordingly, the Service concluded that the spouses and children of students and employees do not come within the convenience exception, and the receipts attributable to them, as well as to guests, would constitute UBTI.

The Service took the same approach in TAM 97-20-035 (February 19, 1997), where a supporting organization of a university claimed that there is a strong demonstrable financial tie between the alumni who use the golf course and the university. In this case the organization did not dispute that the income from alumni was income from a trade or business, but claimed that the activity was substantially related to its exempt purpose. The Service reiterated its position that alumni use of the golf course does not contribute importantly to the accomplishment of an exempt purpose, and that the status of the alumni as members does not transform the golf activity into a related trade or business. The TAM noted that although the Service considered the substantial donations made by alumni who use the golf course, it was not sufficient to establish that their golf course membership advances exempt purposes. Further, the TAM suggested that the alumni in question would make

substantial contributions regardless of the existence of the golf course. Finally, the TAM once again strictly interpreted the "convenience exception" as not being available with respect to spouses and children of faculty, staff and students.

C. Indexation of UBIT Amounts

Rev. Proc. 97-57, 1997-52 I.R.B. 20, sets out the indexed limitations on associate member dues (see section 4, supra) and low cost articles for years beginning in 1998, as follows:

> Section 3.10 Treatment of Dues Paid to Agricultural or Horticultural Organizations.
>
> For tax years beginning in 1998, the limitation under [IRC] 512(d)(1) regarding the exemption of annual dues required to be paid by a member to an agricultural or horticultural organization is $109.
>
> Section 3.11 Insubstantial Benefit Limitation for Contributions Associated with Charitable Fund-Raising Campaigns.
>
> (1) Low cost article
>
> For tax years beginning in 1998, the unrelated business income of certain exempt organizations under [IRC] 513(h)(2) does not include a "low cost article" of $7.10 or less.