

FEDERAL TAXATION

Unrelated Business Income—§ 8012

categories is to be determined from all the facts and circumstances of each case. Thus it will disallow exclusion of rents or royalties if it finds that they are in fact:

... a return of profits by a person operating the property for the benefit of the exempt organization or

... a share of profits retained by the exempt organization as a partner or joint venturer.⁵

But the Treasury's attempts to bar exclusion of mineral royalties received by exempt organizations on the theory that, under the particular facts, they weren't really royalties haven't been sustained by the courts.⁶

1. Code Sec. 512(b)(1).
2. Rev. Rul. 66-106, IRB 1966-18, 12.
3. Code Sec. 512(b)(2).
4. Code Sec. 512(b)(3) and (4).
5. Regs. § 1.512(b)-1; Rev. Rul. 54-420, CB 1954-2, 128.
6. *U.S. v. Robert A. Welch Foundation*, 334 F. (2d) 774, aff'd 228 F. Supp. 831; *Amon G. Carter Foundation v. U.S.*, D.C. Tex., 1/31/58.

§ 8009. Gains and losses from certain sales and exchanges are excluded. Unrelated business taxable income doesn't include gains or losses from sale, exchange or other disposition of property other than:

... stock in trade, inventories, or property held primarily for sale to customers in the ordinary course of business.

... timber cutting treated as a Code Sec. 631 sale or exchange.¹

But unrelated business taxable income includes recapturable depreciation gain realized on sale or exchange of depreciable property. The regs so provide with respect to Sec. 1245 personal property and apparently the same rule applies to Sec. 1250 real property.²

1. Code Sec. 512(b)(5).
2. Code Sec. 1250; Regs. § 1.1245-6(b).

§ 8010. Deductions allowed in computing unrelated business taxable income. In computing unrelated business taxable income, all the same deductions as apply to the computation of taxable income are allowed¹ subject to the following special rules:

... A \$1,000 specific deduction is allowed.²

... The net operating loss deduction is computed by taking into account only those items included in the computation of unrelated business taxable income. Thus an unrelated trade or business operating loss isn't diminished by dividend income. Only years in which the exempt organization is subject to tax on unrelated business taxable income are included in computing an unrelated trade or business operating loss. But all years are counted in determining the span of years for which the loss may be carried back or forward.³

... The charitable contribution deduction limitation is 5% of unrelated business taxable income (before the charitable contribution deduction) for those exempt organizations taxed at corporate rates and 20-30% for those exempt trusts taxed at individual rates.⁴

... Bad debt deduction may be taken as specific deductions or under the reserve method subject to the same rules as apply to other taxpayers. The exempt organization may choose either method in its first return of unrelated taxable income but only if it hasn't already selected a method in a prior year in which it made a return of income subject to tax. In that event, it can't change its method without the Commissioner's prior consent.⁵

1. Code Sec. 511.
2. Code Sec. 512(b)(12).
3. Code Sec. 512(b)(6); Regs. § 1.512(b)-1(c).
4. Code Sec. 512(b)(10) and (11); Regs. § 1.512(b)-1(f).
5. Regs. § 1.511-3(c).

§ 8011. Partnership unrelated trade or business taxable income. If an exempt organization is a member of a partnership that carries on an unrelated trade or business, the exempt organization's share of the partnership income and deductions is included in the computation of its unrelated business taxable income, subject to all the exceptions, additions, and limitations applicable to that computation. The partnership items included in the computation of the exempt organization's unrelated business taxable income are those for the partnership taxable year ending with or within the organization's taxable year.¹

A special rule applies to certain trusts created by the will of an individual who died after Aug. 16, '54, and before '57 where by virtue of the provisions of the will the trust is a member of a limited partnership. Under this rule, the trust excludes its share of the partnership's income from an unrelated trade of business, but only to the extent that partnership income is actually distributed.²

1. Code Sec. 512(c).
2. Code Sec. 512(b)(13).

§ 8012. "Business lease" income and deductions are included in unrelated business taxable income. Business lease rents and deductions are included in the computation of unrelated business taxable income.¹

A "business lease" is a lease of real property for a term of more than 5 years, by a tax exempt organization or by a partnership of which the exempt organization is a member. The lease is a business lease only if at the end of the lessor's taxable year there is business lease indebtedness with respect to the leased property.² Real property includes personal prop-