

What Nonprofits Need to Know About Corporate Sponsorships

In 2002, the IRS released final regulations concerning “qualified corporate sponsorships.” Several rulings and court cases prompted these rules, which are enumerated in Treasury Regulation 1.513-4.

Ultimately, the requirements boil down to whether payments by “sponsors” are corporate sponsorships (excluded from unrelated business income) or advertising (subject to unrelated business income tax). The final regulations consider advertising to be a “substantial return benefit.”

Basically, corporate sponsorships represent an IRS-granted exception to the unrelated business income tax (UBIT) in the federal tax code. Exempt organizations must pay UBIT on income-producing activities that are:

1. a trade or business;
2. regularly carried on; and
3. unrelated to their exempt purposes.

There are numerous exclusions from UBIT, including “corporate sponsorships.”

The corporate sponsorship rules provide a closely defined safe harbor of activities or actions on which no tax will be due. The 2002 final regulations provide six acceptable actions, or corporate sponsorship elements, that would avoid the “substantial return benefits” realm:

1. Listing the name, logo, or product line of the sponsor; Awarding exclusive sponsorship (for example, only one airline would be a sponsor, only one hotel would be a sponsor, etc.);
2. Providing logos or slogans that do not contain any qualitative language or comparative description of the products;
3. Listing the payor’s locations, addresses, phone numbers, and Internet addresses;
4. Providing value-neutral descriptions of the sponsor’s product display; and
5. Listing the sponsor’s brands or trade names.

Conversely, the regulations list four things that are deemed substantial return benefits, including “advertising.” These actions (e.g. “what you can’t do”) are:

1. Advertising;
2. Designating a sponsor as an exclusive provider;
3. Providing facilities, services, or other privileges to the sponsor unless they are of “insubstantial value;” and
4. Granting either exclusive or nonexclusive rights to use the sponsor’s intangible asset (e.g., name or logo).

Example 1:

Calvary College, a private college that is exempt under IRC section 501(c)(3), receives \$5,000 from a local auto dealer to hang a banner in the college’s basketball/volleyball arena. The only content on the banner is the name of the auto dealer, the logo of its national brand, and a web address.

Because the banner contains only the type of information that is included in the qualified sponsorship rules — and not any qualified language or inducement to buy — the \$5,000 sponsorship would be excluded from unrelated business income.

Beyond the lists of activities, let’s look at three areas of the rules that can cause issues:

1. Substantial return benefits
2. Services provided
3. Internet issues

Substantial Return Benefits

Note that number three on the list of four “advertising” activities concerns “insubstantial benefits.” By rule, anything the sponsor receives in return for their sponsorship (greens fees, facilities use, tickets, goods or services, etc.) must have a fair market value of 2% or less of the sponsorship payment. If the value is more than 2%, the entire value of the return benefit is subject to UBIT. While 2% does not sound “substantial,” the rules are the rules.

Example 2:

The same Calvary College situation as in Example 1 but in addition, the college gives the sponsor two season tickets to all basketball and volleyball games. The fair market value of these tickets is \$400.

Because the value of the season tickets is more than 2% of the \$5,000 payment, the entire \$400 “return benefit” is considered the value of the advertising and subject to UBIT.

Services Provided

A subset of the substantial return benefit rules concerns the value of services that may be provided by the tax-exempt organization to a given sponsor. If services are required, the fair market value of those services would generally be considered unrelated business income. It can be a particularly interesting project to reasonably value such services.

Example 3:

The same Calvary College situation as in Example 1 but in addition, the sponsorship contract requires the college’s basketball coach to make three appearances at events for the sponsor — wearing the sponsor’s logo on his clothing and speaking about the sponsor’s “great service.” The fair market value of these appearances is \$1,000.

Because services are required as part of the sponsorship agreement, the \$1,000 fair market value of the coach’s appearances is considered unrelated business income.

Internet Issues

If a sponsorship payment also includes a hyperlink to the sponsor’s website placed on the tax-exempt organization’s website (maybe as part of the sponsor’s name or logo), care should be taken to ensure that unrelated business income is not generated. Rulings have stated that a “clickable” link to a sponsor’s website will not result in unrelated business income — even if there is advertising verbiage on the linked website — as long as the tax-exempt organization does not “endorse” the sponsor’s products. However, the IRS has not released guidance in this area. We cannot be sure that such guidance, when it is issued, will be in accordance with what we’ve seen historically.

Example 4:

The same Calvary College situation as in Example 1, except that the college also includes the sponsor’s logo on its athletics website, along with a clickable link to the sponsor’s website.

Because only the sponsor’s logo and a link to its website are provided on the college’s website, without

endorsement or advertising language, no unrelated business income should be generated from this logo and link.

Recent Tax Reform

In early 2014, the House Ways and Means committee released a draft paper enumerating many proposed changes to the tax code. The draft makes significant changes to the treatment of corporate sponsorships for UBIT purposes. As proposed, if an organization uses or acknowledges the name or logo of a sponsor’s product line, the sponsor’s payment will be treated as per se unrelated trade or business income. Additionally, if an organization receives more than \$25,000 of qualified sponsorship payments for any one event, the use or acknowledgement of the sponsor’s name or logo must appear with the names of a “significant portion” of the other donors to the event.

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