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THE UNRELATED BUSINESS INCOME TAX AND ITS EFFECTS UPON COLLEGIATE ATHLETICS

by

FRANK JAMES VARI*

INTRODUCTION

On August 16, 1991, the Internal Revenue Service (IRS) sent shockwaves throughout the tax-exempt organization community when it issued Technical Advice Memorandum (TAM) 91-47-007 applying the Unrelated Business Income Tax (UBIT) to the organizers of two corporate-sponsored college football bowl games.¹ Although TAM 91-47-007 applies only to the organizers of two bowl games,² it will potentially affect numerous tax-exempt organizations that rely upon corporate sponsors for their funding.³

TAM 91-47-007 was primarily directed at the Cotton Bowl Athletic Association (CBAA).⁴ The IRS is concerned with the sponsorship payments the CBAA receives from its primary corporate sponsor, the Mobil Corporation.⁵ The CBAA operates on an \$8 million budget,⁶ including a \$1.5 million contribution from Mobil.⁷ This contribution puts Mobil's name and logo in front of thousands of fans in the stadium and millions more at home via television and radio.

The Cotton Bowl is one of nineteen corporate-sponsored college football bowl games which annually collect \$64 million in corporate sponsorships.⁸ The IRS wishes to tax \$19.6 million of this amount which represents corporate title sponsorships.⁹ The remaining \$44.4 million represents royalty income¹⁰ which is not subject to the UBIT.¹¹ An estimated \$5 million of federal revenue would be

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¹ Tech. Adv. Mem. 91-47-007 (Aug. 16, 1991); see also Michael Hiestand, *Non-Profits Events Fret About Tax Ruling*, USA TODAY, Jan. 21, 1992, at 2C. Tech. Adv. Mem. 91-47-007 deleted the names of the parties involved, but the organizations have been identified as the Mobil Cotton Bowl and the John Hancock Bowl.

² Richard Sandomir, *Tax Ruling Worries Officials of Bowls*, N.Y. TIMES, Dec. 6, 1991, at B9.

³ See, e.g., Joanne Lipman, *IRS Ruling Threatens Firms' Sponsorship*, WALL ST.J., Dec. 5, 1991, at B8; Paul Streckfus, *Cotton Bowl Ruling Draws Fire at ASAE Roundtable Discussion*, 92 TAX NOTES TODAY 12-16, Jan. 17, 1992, available in LEXIS, Fedtax Library, TNT File.

⁴ *Mobil Cotton Bowl Hit in IRS Technical Advice*, 10 TAX MGMT. WEEKLY REP. 1476, Dec. 9, 1991, available in LEXIS, Fedtax Library, TMWEEK File.

⁵ *Id.*

⁶ Edward P. Jones, *IRS Wants Share of Bowl Game Funding*, TAX NOTES, Feb. 4, 1991, available in LEXIS, Fedtax Library, TXNOTE File.

⁷ *Sports-Event Tax Is Opposed*, N.Y. TIMES, July 29, 1992 at D3.

⁸ See Dennis Zimmerman, *Corporate Title Sponsorship Payments to Nonprofit College Football Bowl Games: Should They Be Taxed?*, CONGRESSIONAL RESEARCH SERVICE 92-157E, Doc. 92-1744 (Feb. 11, 1992), reprinted in 92 TAX NOTES TODAY 41-18, available in LEXIS, Fedtax Library, TNT File.

⁹ *Id.*

¹⁰ *Id.*

¹¹ I.R.S. § 512(b)(2) (1990); Rev. Rul. 81-178, 1981-2 C.B. 135.

generated if the UBIT were applied to the bowl games.¹² Significantly more would be generated if the UBIT were applied to the \$1.1 billion which corporate sponsors contribute annually to exempt organizations.¹³

Historically, corporate sponsorship of exempt organizations has avoided IRS scrutiny. However, due to shrinking public and private financial support, exempt organizations have turned to corporate sponsors for their funding.¹⁴ The IRS claims its policy has not changed, but that the exempt organization's increasingly aggressive fund-raising methods have drawn the IRS's unwelcomed attention.¹⁵

The implications of the IRS's memorandum are far reaching. In addition to corporate-sponsored bowl games, exempt organizations ranging from local ballet companies to environmental groups may incur UBIT liability. Public concern over such tax liability has prompted the introduction of legislation which supports both the IRS and the exempt organizations.¹⁶

This article examines the UBIT and its application to corporate sponsorship of college football bowl games and other exempt organizations likely to be affected by TAM 91-47-007. Thereafter, the article will consider the IRS's proposed examination guidelines of corporate sponsorship income, the public policy concerns regarding such income, and the proposed legislation introduced to address the competing concerns.

THE UBIT AND ITS APPLICATION TO COLLEGE FOOTBALL BOWL GAMES

Generally, the Internal Revenue Code (the "Code" or "I.R.C.") grants tax-exempt status to qualifying charitable organizations. Prior to 1950, this grant of tax-exempt status permitted qualified charitable organizations to enter indiscriminately into non-charitable, for-profit activities, thereby allowing those organizations to compete unfairly with non-tax-exempt enterprises.¹⁷

¹² Zimmerman, *supra* note 8. \$91.6 million of the \$64 million received annually by college football bowl games represents corporate title sponsorships. Assuming 25% of the sponsorship amount is properly expensed by the exempted organization, the remaining \$14.7 million is subject to a 34% tax rate which would generate approximately \$5 million of federal tax revenue.

¹³ *Id.*

¹⁴ *Id.* Total corporate sponsorships of exempt organizations' sports, arts, music, community, and cause-related events was \$1.1 billion in 1991.

¹⁵ See, e.g., *Exempt Organizations: IRS Official Discusses Recent UBIT Developments*, 11 TAX MGMT. WEEKLY REP. 579, May 4, 1992, available in LEXIS, Fedtax Library, TMWEEK File; Albert B. Crenshaw, *Separating Charity From Ads: IRS Shift on Corporate Sponsorship Alarms Nonprofit Groups*, WASH. POST, July 21, 1992, at C1.

¹⁶ See Zimmerman, *supra* note 8.

¹⁷ Donald C. Haley, *The Taxation Of The Unrelated Business Activities Of Exempt Organizations: Where Do We Stand? Where Do We Seem To Be Headed?*, 7 AKRON TAX J 61,62 (1990); see also Henry B. Hansmann, *Unfair Competition And The Unrelated Business Income Tax*, 75 VA. L. REV. 605 (1989).

In order to alleviate this competitive disparity, in 1950, Congress enacted the UBIT.¹⁸ The UBIT taxes the non-charitable business activities of otherwise tax-exempt charitable organizations at the same rate as is imposed upon non-charitable organizations that are engaged in similar activities. Presently codified at I.R.C. §§ 512 and 513,¹⁹ the UBIT restricts such taxes to those activities that are not substantially related to the organization's charitable purposes.²⁰

I.R.C. § 501(c) embodies the criteria of an exempt organization.²¹ Such exempt organizations serve many valuable social causes undertaken for the public good.²² The qualifying organizations enjoy tax-exempt status under I.R.C. § 501(a).²³ Under the UBIT, all of an otherwise exempt organization's "unrelated business taxable income" is taxable at corporate income tax rates.

I.R.C. § 513²⁴ defines "unrelated trade or business" as any trade or business the conduct of which is not substantially related, outside of the production of income, to the organization's exempt purpose enumerated in I.R.C. § 501.²⁵ An activity does not lose its identity as a trade or business simply because it is carried out along with a number of other activities which may, or may not, be related to the organization's exempt purpose.²⁶ An exempt organization is entitled to offset certain expenses directly connected with the trade or business, subject to the modifications of I.R.C. § 512(b),²⁷ including a safe harbor exemption for unrelated business taxable income not exceeding \$1000.²⁸

TAM 91-47-007 has no direct effect on the corporate sponsor. A corporate sponsor may properly deduct the contribution as either a I.R.C. § 170 charitable contribution or a I.R.C. § 162 business expense.²⁹

The Treasury Regulations require a three-pronged facts and circumstances test to determine if the UBIT applies.³⁰ An exempt organization's income is subject to the UBIT if: (1) It is income from a trade or business; (2) such trade or business is regularly carried on by the organization; and (3) the conduct of such

¹⁸ Haley, *supra* note 17, at 63.

¹⁹ I.R.C. § 512 (1990) and I.R.C. § 513 (1990).

²⁰ See Revenue Act of 1950, Pub. L. No. 81-814 § 301, 64 Stat. 906, 947 (1950) (codified as amended in 26 U.S.C. §§ 512-13).

²¹ I.R.C. § 501(c) (1990).

²² *Id.*

²³ I.R.C. § 501(a) (1990).

²⁴ I.R.C. § 513 (1990).

²⁵ I.R.C. § 513(a) (1990).

²⁶ I.R.C. § 513(c) (1990).

²⁷ I.R.C. § 512(a)(1) (1990).

²⁸ I.R.C. § 512(b)(12) (1990).

²⁹ I.R.C. § 170 (1990) and I.R.C. § 162 (1990); see also *Hernandez v. Commissioner*, 109 S.Ct. 2136 (1989); *United States v. American Bar Endowment*, 477 U.S. 105 (1986).

³⁰ Treas. Reg. § 1.513-1(a) (as amended in 1993); see also *United States v. American College of Physicians*, 475 U.S. 834, 838-39 (1986).

trade or business is not substantially related, other than through the production of income, to the organization's exempt purpose.³¹ The taxpayer does not incur UBIT liability if any of the test's three elements are not met.³²

Is Corporate Sponsorship Income Received By College Football Bowl Game Organizers Income From A Trade Or Business?

The Regulations' definition of "trade or business" carries the same meaning it has in I.R.C. § 162, which includes any activity carried on for the production of income from the sale of goods or the performance of services.³³ An activity will qualify as a trade or business regardless of its actual profitability.³⁴

The Supreme Court has ruled that an exempt organization is engaged in a trade or business when it provides goods or services with the dominant intent of realizing profit.³⁵ It is very difficult to argue that the CBAA does not intend to realize a profit or provide valuable services to its corporate sponsors.³⁶

Mere recognition of a corporate sponsor does not qualify as a trade or business.³⁷ However, the Supreme Court has ruled that if the donor enters into a quid pro quo exchange with an exempt organization, the payments are income and not gifts or contributions.³⁸ The IRS ruled that the agreement between the CBAA and Mobil involves a significant quid pro quo relationship.³⁹ The terms of the contract between the two organizations firmly supports the IRS's position. The contract's terms include changing the name of the event to include Mobil's name and canceling the contract and revoking the donation if the event is not televised.⁴⁰

³¹ Treas. Reg. § 1.513-1(a) (as amended in 1983).

³² *Veterans of Foreign Wars v. Commissioner*, 89 T.C. 7, 19-20 (1987).

³³ Treas. Reg. § 1.513-1 (as amended in 1983).

³⁴ *Id.*

³⁵ *United States v. American Bar Endowment*, 477 U.S. 105, 110 (1986).

³⁶ Michael Hiestand, *Sponsors Cash In On Bowl Game Bonanza*, USA TODAY, Dec. 31, 1991 at C2. In return for Mobil's \$1.5 million contribution to the CBAA they received \$3.92 million in on-air exposure.

³⁷ Rev. Rul. 67-342, 1967-2 C.B. 187.

³⁸ *Hernandez v. Commissioner*, 109 S.Ct. at 2136, 2138 (1989).

³⁹ Tech. Adv. Mem. 91-47-007 (Aug. 16, 1991).

⁴⁰ Paul Streckfus, *A Glimpse of Mobil-Cotton Bowl Contract Provisions*, 55 TAX NOTES 447, April 27, 1992, available in LEXIS, Fedtax Library, TXNOTE File. The contract between the CBAA and the Mobil Corporation included the following provisions:

1. CBAA must change the name of the Cotton Bowl to the Mobil Cotton Bowl, and add the Mobil logo to the Cotton Bowl logo. The new name and logo must be used exclusively and must be mentioned in all Cotton Bowl press releases.

2. At the site of the Cotton Bowl, CBAA must imprint the new logo in a prominent place on the field.

3. During the football game, CBAA must display Mobil's commercial messages on the electronic sign in the stadium and broadcast Mobil's commercial messages over the public address system.

4. If the Cotton Bowl is not televised, Mobil may cancel the contract.

5. CBAA, on behalf of Mobil, must arrange for hospitality suites and hotel rooms, tickets to the game, and tickets to event-related activities.

6. In return, Mobil must pay CBAA a sponsorship fee. If the Cotton Bowl achieves a Nielsen (television) rating above a stated level, CBAA is entitled to an additional sponsorship fee from Mobil.

This arrangement calls for much more than incidental recognition of the sponsor's contribution and it should serve as a guidepost to other exempt organizations seeking direction on this issue.

Are The Corporate Sponsorship Activities Of A College Football Bowl Game Regularly Carried On?

The I.R.C. § 512 definition of "regularly carried on" deals with the frequency and continuity with which the income producing activities are conducted and the manner in which they are pursued.⁴¹ Other important factors include the activity's normal time span and seasonal nature.⁴² The IRS compares the exempt organization's activities with the normal activities of other exempt organizations.⁴³ The primary focus is on the exempt organization's competitive and promotional efforts.⁴⁴

The IRS has ruled that an exempt organization's advertising activities which are similar to a commercial advertiser's activities are "regularly carried on."⁴⁵ In TAM 91-47-007, the IRS ruled that the CBAA's activities are similar to a commercial advertiser's and are conducted over a sufficient period of time to be regularly carried on.⁴⁶

The Supreme Court has not had an opportunity to define "regularly carried on." However, one court has determined that advertising activity by an exempt organization which conducts an annual sporting event is not regularly carried on and is not subject to the UBIT.⁴⁷ The court held that although the advertising preparation took place over a long period of time, the advertising activity itself took place only over the four-day duration of the event itself.⁴⁸ The court decided that when determining whether an activity is regularly carried on, the relevant period is only that period during which the advertising itself took place.⁴⁹ The IRS does not follow this decision and claims the court's factual inferences and legal conclusions are erroneous.⁵⁰ The IRS claims that the relevant time period includes the

⁴¹ Treas. Reg. § 1.513-1 (as amended in 1983).

⁴² Treas. Reg. § 1.513-1(c)(2) (as amended in 1983).

⁴³ Treas. Reg. § 1.513-1(c)(2)(ii) (as amended in 1983).

⁴⁴ David A. Haimes, Note, *Corporate Sponsorships of Charity Events and the Unrelated Business Income Tax: Will Congress or the Courts Block the IRS Rush to Sack the College Football Bowl Games?*, 67 NOTRE DAME L. REV. 1079, 1093 (1992).

⁴⁵ Rev. Rul. 73-424, 1973-2 C.B. 190, 191.

⁴⁶ Tech. Adv. Mem. 91-47-007 (Aug. 16, 1991).

⁴⁷ NCAA v. Commissioner, 914 F.2d 1417 (10th Cir. 1990), *action on decision*, 1991-015 (July 15, 1991).

⁴⁸ *Id.* at 1423.

⁴⁹ *Id.*

⁵⁰ I.R.S. Action on Decision, 1991-015 (July 15, 1991), *available in* LEXIS, Fedtax Library, AOD File.

solicitation and preparation time of the advertising.⁵¹ The court's ruling firmly supports the CBAA's position that the activity is not regularly carried on.⁵²

Is The Corporate Sponsorship Activity Substantially Related To The Organization's Exempt Purpose?

This element examines the nexus between the exempt organization's income producing activities and the organization's exempt purpose.⁵³ A trade or business is "related" only if the activity has a causal relationship to the exempt organization's exempt purpose, outside of the production of income.⁵⁴ An activity is "substantially" related if the facts and circumstances indicate that the income-producing activities contribute importantly to the organization's exempt purpose.⁵⁵

As discussed above, Congress enacted the UBIT to protect non-tax-exempt organizations from unfair competition.⁵⁶ However, the applicable Treasury Regulations make only one reference to unfair competition.⁵⁷ Consequently, the Supreme Court has determined that the existence of such unfair competition is not a prerequisite to the imposition of the UBIT, but rather a mere likelihood of unfair competition is sufficient.⁵⁸

The Court has ruled that the activities of an exempt organization may be "fragmented" for UBIT analysis.⁵⁹ Thus, the IRS may fragment the exempt organization's activities and determine if the income-producing activities are substantially related to the organization's exempt purposes. Using this approach, the IRS ruled that neither the addition of the sponsor's name nor the prominent display of the sponsor's logo contributes importantly to the CBAA's educational purpose. It is irrelevant that the sponsor also provided the exempt organization with funds used for its exempt purpose.⁶⁰

The IRS rejects the necessity of an unfair competition analysis. The IRS follows a federal court decision that where an organization conducts an activity with a profit motive and the activity is not substantially related to the organization's exempt purpose, the organization's activity presents a sufficient likelihood of unfair competition to be within the policy of the UBIT.⁶¹ As previously analyzed, corporate sponsorship of college football bowl games satisfies both elements of

⁵¹ *Id.*

⁵² Tech. Adv. Mem. 91-47-007 (Aug. 16, 1991).

⁵³ Treas. Reg. § 1.513-1(d)(1) (as amended in 1983).

⁵⁴ Treas. Reg. § 1.513-1(d)(2) (as amended in 1983).

⁵⁵ *Id.*

⁵⁶ See Haley, *supra* note 17.

⁵⁷ Treas. Reg. § 1.513-1(b) (as amended in 1983).

⁵⁸ United States v. American Bar Endowment, 477 U.S. at 105, 115 (1986).

⁵⁹ United States v. American College of Physicians, 475 U.S. 834, 845-46 (1986).

⁶⁰ Tech. Adv. Mem. 91-47-007 (Aug. 16, 1991).

⁶¹ Carolinas Farm & Power Equip. Dealers Ass'n v. United States, 699 F.2d 167, 170 (4th Cir. 1983).

this test. The IRS likewise follows the Supreme Court's holding that no specific finding of unfair competition is necessary to prove that unfair competition exists, but the mere likelihood of unfair competition is sufficient.⁶² Thus, the IRS never analyzed the bowl game's competition with competing advertising outlets such as television, magazines, newspapers, radio, and for-profit sports organizations including professional football. Had it done so, the IRS would have found that the bowl games vigorously compete with for-profit advertisers for corporate advertising dollars and the tax exemption allows them to provide an advertiser with more product at a lower cost. This is certainly more than a mere likelihood of unfair competition.

The IRS has primarily focused its UBIT enforcement upon activities not displaying "economies of scope." Economies of scope are present if the activity is less costly when undertaken in conjunction with the organization's exempt purpose than when undertaken separately.⁶³ An example of economies of scope is a local orchestra which publishes and distributes at its performances a program of the evening's musical selections with small advertisements inside.⁶⁴ This example is contrasted to the orchestra's operation of a gas station, which displays no such economies of scope. Thus, an exempt organization not displaying economies of scope will most likely attract unwelcomed IRS attention.

The CBAA argues that economies of scope are present and whatever benefit the corporate sponsor receives is incidental to the sponsorship funds.⁶⁵ The IRS discounts this contention and asserts that the benefit the CBAA bestows upon the corporate sponsor is very significant, regardless of the sponsorship amount.⁶⁶ The type of economies of scope present strongly supports the IRS position with respect to college football bowl games.⁶⁷

PROPOSED IRS GUIDELINES ON CORPORATE SPONSORSHIP OF EXEMPT ORGANIZATIONS

TAM 91-47-007 generated significant concern in the exempt organization community. It threatened the exempt organization's funding and provided no clear guidance on the subject beyond college football bowl games.⁶⁸ The IRS has responded by issuing proposed examination guidelines regarding an exempt

⁶² *American Bar Endowment*, 477 U.S. at 115.

⁶³ See Hansmann, *supra* note 17, at 608-09.

⁶⁴ This example assumes the local orchestra is an I.R.C. § 501 exempt organization.

⁶⁵ See Tech. Adv. Mem. 91-47-007 (Aug. 16, 1991).

⁶⁶ *Id.*

⁶⁷ Micheal J. McCarthy, *Keeping Careful Score on Sports Tie-Ins*, WALL ST. J., Apr. 24, 1991 at B1. John Hancock Mutual Life reaped \$5.1 million in benefits from its \$1.6 million contribution to the 1991 John Hancock Bowl.

⁶⁸ See INTRODUCTION *infra*.

organization's treatment of corporate sponsorship income.⁶⁹ The proposed examination guidelines set forth a UBIT facts and circumstances analysis for corporate sponsorships of exempt organizations. However, the proposed guidelines also raise a number of new questions on the issue.

The IRS examination guidelines focus on a quid pro quo exchange of valuable services from the exempt organization for corporate sponsorship dollars.⁷⁰ The guidelines provide that mere recognition of a corporate sponsor will not trigger the UBIT, but a contract or agreement which contemplates an exchange of marketing services for financial support will.⁷¹

Associating the name of the sponsor with the name of the exempt organization will not, in itself, trigger the UBIT.⁷² The guidelines require a facts and circumstances evaluation of the relationship between the sponsor and the exempt organization.⁷³ A facts and circumstances approach without existing authority to aid its interpretation would generate significant ambiguity. This approach is likely to force every exempt organization with a corporate sponsor to expend precious financial resources to evaluate its position. Congress could remedy this situation by providing safe harbor provisions that can be defined with numerical precision, for example, by raising the I.R.C. § 512(b)(12) safe harbor exemption to \$100,000.⁷⁴

The guidelines, and hence the UBIT, do not apply to (1) organizations of a purely local nature that (2) receive relatively insignificant gross revenue from corporate sponsors and (3) generally operate with significant amounts of volunteer labor.⁷⁵ The IRS cites youth organizations such as little league baseball and soccer teams, local theatre, and youth orchestras as examples of organizations outside of the guidelines scope.⁷⁶

These application criteria raise several interesting questions. What is "purely local"? Do the guidelines apply to nationally recognized exempt organizations which organize local events sponsored by local contributors and only attended by the local community? Is an event sponsored by a corporation or a large city an

⁶⁹ I.R.S. Announcement 92-15, 1992-5 I.R.B. 51 (Feb. 3, 1992).

⁷⁰ *Id.* at 52, 53.

⁷¹ *Id.* at 52.

⁷² *Id.*

⁷³ *Id.* Factors to be considered include:

(1) the value of the services provided in exchange for the payment;

(2) the terms under which payments and services are rendered;

(3) the amount of control the sponsor exercises over the event; and

(4) whether the extent of the organization's exposure of the donor's name constitutes significant

promotion.

⁷⁴ I.R.C. § 512(b)(12) (1990).

⁷⁵ I.R.S. Announcement 92-15, 1992-5 I.R.B. at 52.

⁷⁶ *Id.*

"organization of a purely local nature"? An exempt organization is probably safe if its relationship with the corporate sponsor is simply corporate philanthropy and the organization has not become the sponsor's advertising vehicle.

The definitions of "significant gross revenue" and "significant amounts of volunteer labor" cannot be defined with adequate certainty. Both definitions raise more questions than they answer and should be numerically defined in some manner.

The examination guidelines require the examiner to review any contract or arrangement requiring the exempt organization to perform services for the corporate sponsor in return for its financial support.⁷⁷ The examiner is required to review the contract or arrangement for factors indicating any exchange of consideration.⁷⁸ The IRS will focus upon the prominence of the corporate sponsor's name or logo in connection with the event.⁷⁹

The IRS will also examine perquisites the exempt organization provides for the corporate sponsor's clients or executives.⁸⁰ A corporate sponsor could abuse the Code by disguising I.R.C. § 162(a)(2) lavish or extravagant travel expenses⁸¹ in connection with an exempt organization's event as an I.R.C. § 170 charitable contribution.⁸²

The media and public exposure of the event is examined and any required media exposure of the sponsor's name, logo or product, or services is given particular attention.⁸³ Any required display of the corporate sponsor's name or logo is sure to send up a red flag to the IRS examiner.

⁷⁷ *Id.*

⁷⁸ *Id.*

⁷⁹ *Id.* Factors tending to indicate that an exempt organization's corporate sponsorship activities are an unrelated trade or business include whether the corporate sponsorship contract or arrangement requires:

1. the corporate sponsor's name or logo to be included in the official event title;
2. the corporate sponsor's name or logo to be prominently placed throughout the stadium, arena, or other site where the event is held;
3. the corporate sponsor's name or logo to be printed on materials related to the event;
4. the corporate sponsor's name or logo to be placed on participant uniforms or other support personnel uniforms;
5. the corporate sponsor to refer to its sponsorship in advertisement over the course of the contract;
6. the participants be available to the corporate sponsor for personal appearances and endorsements; or
7. the exempt organization to arrange for special seating, accommodations, transportation, and hospitality facilities at the event for corporate sponsor clients or executives.

⁸⁰ *Id.* at 52-53.

⁸¹ I.R.C. § 162 (a)(2) (1990).

⁸² I.R.C. § 170 (1990).

⁸³ I.R.S. Announcement 92-15, 1992-5 I.R.B. at 52.

The examiner must also review the use of the income by the institutions participating in the game.⁸⁴ All college football game organizers are required to pay the participating institutions seventy-five percent of the gross receipts of the event, with a minimum payout of \$650,000 per institution.⁸⁵ Officials of the institutions claim the bowl payouts are put to good use,⁸⁶ but the actual accounting often proves otherwise.⁸⁷

The guidelines fail to address some obvious questions. What if the exempt organization accepts a corporate contribution and the corporate sponsor chooses to publicize the contribution on its own initiative? Will this trigger the UBIT at the exempt organization's expense? The guidelines do not address which, if any, expenses may be offset against the taxable income if the UBIT applies. The IRS has adopted an "all or nothing" approach to the UBIT which does not recognize expenses incurred by the exempt organization on the sponsor's behalf. A better approach is to allow the organization to offset ordinary and necessary expenses against the benefit conferred upon the sponsor and tax the difference. However, the Supreme Court has given the all or nothing approach its mandate.⁸⁸ The IRS also departs from a traditional UBIT analysis and makes no mention of the regularly carried on analysis or any corporate title sponsorships masquerading as royalties.

The guidelines' focus on contracts or arrangements will discourage formal agreements and promote instability to the detriment of the exempt organization. Public policy dictates that the guidelines be modified for this reason alone.

The IRS has sought public comment on these guidelines,⁸⁹ and public hearings have been held for the first time in IRS history.⁹⁰ The IRS is reviewing these comments and plans to revise the guidelines accordingly. IRS officials have stated that no adverse opinions will be issued in pending audits until the final guidelines are published.⁹¹

⁸⁴ *Id.*

⁸⁵ National Collegiate Athletic Association Manual, § 31. 5.1 (1992-93) .

⁸⁶ Dick Rosenthal & John David Crow, *Bowl-Game Taxes Hurt Charity, Schools, and Business*, N.Y. TIMES, Feb. 9, 1991, § 8, at 11.

⁸⁷ John Weistart, *College Bowls: Apple Pie and Taxation With Justification*, N.Y. TIMES, Dec. 22, 1991, § 8, at 9. The University of Oregon reported only a \$5000 net gain from the \$600,000 payout it received from the 1990 Freedom Bowl. The remaining funds provided expenses for 103 university staff members, spouses, relatives, and friends who attended the game.

⁸⁸ *United States v. American Bar Endowment*, 477 U.S. 105, 112 (1986).

⁸⁹ I.R.S. Announcement 92-15, 1992-5 I.R.B. at 53.

⁹⁰ I.R.S. Announcement 92-88, 1992-26 I.R.B. 34.

⁹¹ *See Changes Will Be Made To Proposed Sponsorship Guidelines, Owens Says*, 11 TAX MGMT. WEEKLY REP. 691, May 25, 1992, available in LEXIS, Fedtax Library, TXWEEK File. Marcus Owens, IRS Exempt Organizations Technical Divisions Director, said, "the IRS plans to change, perhaps radically, proposed examination guidelines regarding unrelated business income tax in connection with corporate sponsorships and likely will not adopt any 'adverse positions' in pending audit cases until it has 'a chance to exchange ideas with the exempt organization community.'"

PUBLIC POLICY AND PROPOSED LEGISLATION

A public policy analysis of the IRS position requires balancing the social value of tax-exempt college football bowl games and the additional federal revenue the UBIT would generate. Any tax exemption to an organization amounts to a government subsidy of the exempt organization. The government subsidy of college football bowl games currently is \$5 million.⁹² The IRS's application of the UBIT to the bowl games will end this subsidy and increase federal tax revenues accordingly.

Today, college football is an institution of American popular culture. It also represents a powerful lobbying group. This group includes millions of American football fans, hundreds of colleges and universities and their alumni, and the corporations which benefit from the media exposure. Any threat to the number and quality of college football bowl games will raise the ire of these groups and others.

The opposing viewpoint highlights the alternative uses of the foregone federal revenue. Is the money represented by the bowl game subsidy better spent on AIDS research, social welfare projects, deficit reduction, or cultural institutions such as museums? These are precisely the questions that Congress seeks to answer.

A number of legislative items have been introduced addressing this controversy. Most of the proposals favor protecting the bowl games, but at least one favors taxing the bowls.⁹³ H.R. 5645 favors protecting the bowl game subsidy and has received the House of Representative's approval.⁹⁴

H.R. 5645 is representative of most bills protecting the bowl games. This bill would revise I.R.C. § 513 to permit tax-free solicitation of corporate sponsorships. Additionally, the bill shields from income corporate sponsorship and royalty payments to exempt organizers of annual athletic events of thirty days or less.⁹⁵ The bill also ensures tax protection to the organizers of the 1996 Atlantic Olympic games.⁹⁶

In order to offset this potential revenue loss, the bill revokes the tax-exempt status of exempt organizations which allow their names and membership lists to

⁹² See *supra* note 12.

⁹³ H.R. 969, 102d Cong., 1st Sess. (1991).

⁹⁴ H.R. 5645, 102d Cong., 2d Sess. (1992).

⁹⁵ *Id.*

⁹⁶ *Id.*

be used in "affinity" credit card programs.⁹⁷ Thus, exempt organizations that rely upon affinity credit card programs for a significant portion of their funding, such as the Sierra Club, are left out in the cold.

This bill, as well as others, protects athletic event organizers, particularly the organizers of college football bowl games and the 1996 Atlanta Olympic games. Unfortunately, most other worthy exempt organizations with corporate sponsors remain exposed to the UBIT.

CONCLUSION

There is no doubt that many exempt organizations depend upon corporate sponsorships for their existence. The UBIT's application to these organizations raises strong policy arguments for both sides. However, legal precedent slightly favors the exempt organization's position. The point may soon be moot, at least as far as the bowl games and 1996 Olympics are concerned, if Congress continues in its current direction.

Until Congress acts, exempt organizations with corporate sponsors can only sit and wait. In the meantime, an exempt organization should review all documentation of arrangements with corporate sponsors to determine if a quid pro quo agreement exists. If so, the exempt organization should restructure the agreement to provide for a corporate contribution without an expectation of substantial benefits from the exempt organization.

This issue is sure to prompt much future debate until concrete guidelines or legislation is in place. Until then, exempt organizations can only hope that a strong defense will throw the IRS's offensive posture on corporate sponsorship for a loss.

⁹⁷ In a typical affinity card arrangement, an exempt organization solicits consumers to purchase a credit card displaying the exempt organization's logo from a particular financial institution which gives the group a small donation, typically a single payment for a new account plus 0.5% of every purchase made with the card.