THE UNIVERSITY OF MICHIGAN

STANDARD PRACTICE GUIDE

SECTION:	Sales and Cash Collections	**Number:**	502.4
		Revised:	9/24/04
SUBJECT:	Sales of Goods and Services to Non-University Entities And Federal Unrelated Business Income (UBI)	**Date Issued:**	
		Review Date:	9/24/09
		Attachment(s)	0
APPLIES TO:	All University Units		
ISSUED BY:	Financial Operations – Tax Resources		

POLICY ON THE SALES OF GOODS AND SERVICES

As a public institution for the State of Michigan and governed by its 501c3 organization status certain activities should be reviewed in order to maintain the not for profit status. Sales of goods and services by the University of Michigan to non-University entities, i.e., outside sales, should be undertaken only in unusual situations where the sales of those goods or services are directly and substantially related to and are in support of the mission of the University of Michigan. Sales may be made for specific fundraising purposes; however, University units may not engage in commercial activities, i.e., business operations normally conducted by entities in the private for-profit sector, whose sole purpose is generating income.

Revenues derived from goods sold or services performed by units to unrelated parties may be subject to federal income taxation as unrelated business income (UBI) when that sale or service constitutes a regularly 'carried on' trade or business that is not substantially related to the University's educational mission. However, to determine 'relatedness', the Internal Revenue Code does not focus on the destination of the proceeds but rather on the nature of the activity. Also, many activities conducted with a 'commercial hue' may trigger UBI. Further, most states provide that purchases of goods by units of an educational institution are excluded from sales and use taxation, however, subsequent sales of such goods by these units generally are subject to taxation.

Outside sales may be undertaken at the University of Michigan when the proposed sales activity would further the University's mission, and:

A. When the necessary facilities, goods, or services are unique to the University or are not readily accessible to the general community, and/or

B. When the work can be undertaken without interference to normal University usage, and/or

C. When the results may be of scientific or scholarly value, may lead to an extension of knowledge, or may increase effectiveness in education/research or patient care.

Fees or prices charged must cover the associated direct costs, indirect costs, and the use of any facilities and staff of the University involved in providing these activities, and should be comparable to prices charged for similar goods or services provided in the private sector. Selling units must establish procedures for periodic review of such activities to ensure compliance with applicable University policies and requirements of outside regulatory authorities.

Sales of goods or services to non-University entities must be reported to Financial Operations – Tax Resources. Further, such transactions may trigger tax consequences that impact financial budgets and require reporting responsibilities.

Action Steps:

Units that identify or conduct sales to external parties should visit the web-page for Tax Resources and Reporting within Financial Operations http://www.umich.edu/~finops/index_js.htm or contact the Financial Operations Tax Manager for further information at 734-763-3282. These resources should assist the unit in managing the tax exposure and, if applicable, quantifying tax liabilities.

POLICY – FEDERAL UNRELATED BUSINESS INCOME (UBI) AND SALES AND USE TAX MATTERS

The University is subject to taxable income or unrelated business income (UBI) on revenues derived from trade or business activities that are regularly carried on and that are not substantially related to its mission. Each unit bears the tax liability for any UBI activities it conducts.

Examples of activities that are 'substantially related' to the mission of the University include patient fees for work done at the School of Dentistry by students or Executive Education program fees for the School Business Administration.

Also, types of income are excluded from taxation. Income derived from royalties, rents from real property and sales of capital assets are not subject to UBI.

Examples of activities that may derive **taxable income** include the following:

- Advertising space for commercial businesses on the Internet or in publications.
- Providing services related to rental space, University lodging, meeting halls, office space or student housing to non-university users.
- Catering (food service, etc.) to non-University users.
- Printing or audio-visual sales and services to non-University users.
- Routine analytical or testing services to non-University users.
- Sponsorship funding received for commercial advertising. Although, certain other sponsorship funding may not be taxable when the funding is University mission-related activity and would not be possible due to cost constraints. Sponsorship is defined as revenues generated when a University department or unit receives monies from a non-University entity and provides no goods or services in return. These revenues are considered to be donations, and therefore acknowledgment of the donating entity is allowable, assuming that the acknowledgment is not commercial in nature.

A myriad of exceptions apply that may exclude the income from an otherwise taxable activity, such as, income derived from an unrelated trade or business that is carried on primarily for the convenience of its students, faculty, staff, and patients is not taxable or that is conducted primarily by volunteers. For

example, a college that operates a laundry for the purpose of laundering dormitory linens for students' clothing is not a UBI activity or a gift shop managed by volunteers from the community.

The taxation of each activity is contingent on a facts and circumstances determination. The Internal Revenue Service (IRS) considers as taxable income revenues derived from sales of T-shirts to members of the general public.

The unit must adopt procedures to identify to whom the sales were made. Also, a cost methodology must be implemented to properly allocate indirect costs to the taxable activity to minimize the tax liability.

Additionally, sales to external parties may generate Michigan Sales and Use taxes, Standard Practice Guide Section 502.03. University is exempt from sales and use taxes with the purchase of goods used to further its mission. Sales, however, are typically subject to taxes. It is also the responsibility of each unit to manage the potentially resulting tax liabilities.

Action Steps:

Units that identify UBI activities or conduct sales to external parties should visit the web-page for Tax Resources and Reporting within Financial Operations http://www.umich.edu/~finops/index_js.htm or contact the Financial Operations Tax Manager for further information at 734-763-3282. These resources should assist the unit in managing the tax exposure and, if applicable, quantifying tax liabilities.

Related Information

For information on pricing or direct and/or indirect costs associated with a sales activity, contact the University Treasurer's Office at http://www.umich.edu/~treasury/. See also Standard Practice Guide Section 501.06, *Merchant Credit Card* at http://spg.umich.edu/pdf/501.06.pdf. For assistance with tax issues, see Standard Practice Guide Sections 502.03, *Michigan Sales and Use* Tax or refer to the University's web site for the Tax department on the Financial Operations Home Page at www.umich.edu/~finops/index_js.htm.