



# **For Sale: Managing Legal Issues Associated with Sales Activities in Today's Commercial Environment**

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## Overview

- Tax Landscape
- Definitions and Rules
- Structuring Your Sales Activities to Maximize Revenue While Managing Risk

## Tax Landscape

- Non-profit organizations with § 501(c)(3) status are not shielded from all tax liability
  - ✓ State sales tax still applies to many non-profit activities
  - ✓ Federal Unrelated Business Income Tax (UBIT)

## What is a Sale?

- OCGA§48-8-2 (31) "Retail sale" or a "sale at retail" means any sale, lease, or rental for any purpose other than for resale, sublease, or subrent.
  - ✓ Resale example: A business owner purchases goods from a warehouse store that she will then sell in her store. She does not pay sales tax on the goods because she is reselling them and her customers will pay the sales tax on the end purchase.
- OCGA§48-8-2 (33) (A) "Sale" means any transfer of title or possession, transfer of title and possession, exchange, barter, lease, or rental, conditional or otherwise, in any manner or by any means of any kind of tangible personal property for a consideration

## What is a Sale? (cont.)

- Be aware that the definitions of “retail sale” and “sale” are very broad
  - ✓ A wide variety of activities fall under these definitions
- Remember that § 501(c)(3) status does not exempt a non-profit from sales tax liability



## What is UBI?

- Unrelated Business Income (UBI): Income derived from trade or business activities not substantially related to the tax-exempt organization's purposes is taxable as if earned by a comparable for-profit enterprise
  - ✓ Example: a restaurant operated by a non-profit hospital that is open to the public daily is likely not sufficiently related to the hospital's purposes
- Income tax must be paid on UBI regardless of §501(c)(3) status
  - ✓ Failure to remit income tax could result in revocation of exempt status

## UBI Central Elements

- Unrelated: Is there a substantial causal relationship between the revenue-generating activity and the organization's exempt purpose?

(the activity must contribute importantly to the accomplishment of the tax-exempt's purposes)

- ✓ Note: The mere fact that the income produced will be used to carry out the mission is not a sufficient causal relationship. The activity must be related.

## UBI Trade or Business

- Trade or business activities typically exhibit an intent to derive a profit from their conduct. In addition, the activities must be regularly carried on.
- ✓ Tip: When considering whether the activity is “regularly carried on” measure the frequency of the activity against the frequency with which a commercial enterprise would conduct it.

## How Does an Organization Know if it is Engaged in Trade or Business?

- Profit motive test
  - ✓ A revenue producing activity that is not expected to produce a profit is not “business”
- Commerciality test
  - ✓ Focus is on how the operation is run
  - ✓ If the activity is conducted like a commercial business then it is likely a trade/business and the income is UBI

## Trade or Business Regularly Carried On

➤ If

- 1) the activity is infrequent;
- 2) the activity is conducted only for a short period during the year; or
- 3) the activity is not engaged in with a competitive or promotional intent,

➤ Then

- ✓ It should not be considered as regularly carried on

➤ Exception

- ✓ Seasonal activities are still considered frequent even though they are only conducted for a short period during the year

## Structuring Your Sales Activities to Maximize Revenue While Managing Risk

- Cause related marketing uses product promotion to promote mission
  - ✓ Payments structured as royalties for use of name and logo
  - ✓ Shifts sales tax burden onto third party
- Internet sales are not a sales tax loophole
  - ✓ In most instances the appropriate sales tax needs to be remitted to the respective state

## **Structuring Your Sales Activities to Maximize Revenue While Managing Risk (cont.)**

- Fragmentation rule provides an exemption for the income from an unrelated business when it is earned in a related setting
  - ✓ Educational: museum store that sells items related to the museum's purpose (e.g. books, artwork replicas)
  - ✓ Convenience: cafeteria for hospital patients and their families



## **Structuring Your Sales Activities to Maximize Revenue While Managing Risk (cont.)**

- Common non-profit sales activities may fall under UBIT exclusions or exemptions
  - ✓ Use of donated goods/services
    - Example: thrift store selling donated goods
  - ✓ Volunteer sales force
  - ✓ Items with logo, name and/or messaging on it
  - ✓ Training programs



# Structuring Your Sales Activities to Maximize Revenue While Managing Risk

## ➤ Thrift Stores

- ✓ All donated items?
- ✓ Volunteers?
- ✓ Sales tax

## ➤ Online Stores

- ✓ Related items?
- ✓ Donated items?
- ✓ Sales tax

## ➤ Books

- ✓ Related?
- ✓ Volunteers?
- ✓ Sales tax



## **For More Information:**

If you would like more information about the services of Pro Bono Partnership of Atlanta, contact us at:

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