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ASAE Talking Points on Royalty Income

UBIT rules require a tax-exempt organization to pay income tax when the organization regularly carries on a trade or business that is not substantially related to the organization's exempt purposes. There are several exceptions in current tax law where unrelated and regularly carried on business activity will not be subject to UBIT. With Congress intent on overhauling the tax code, associations and other tax-exempt organizations are advised to prepare for changes to the tax treatment of income previously excluded from UBIT. These changes could affect:

Royalty income

A royalty is the money paid for the use of intellectual property such as an organization's name, logo or copyrighted content. Royalties are regarded as passive income, meaning the organization has entered into a licensing arrangement for use of its name or logo but is not actively involved in the marketing or administration of the product or service connected with the arrangement.

- The tax code contains a number of exclusions and exceptions to the unrelated business income tax (UBIT) statute. Those exceptions exist because there is a nexus between the furtherance of an organization's tax-exempt purpose and the business activity in question.
- Any expansion of the UBIT statute to include activities currently excluded from the computation of taxable income could significantly impact any association's bottom line, directly affecting its ability to carry out its mission.
- Royalties have historically been treated as passive income, meaning the organization has entered into a licensing arrangement for use of its name or logo but is not actively involved in the marketing or administration of the product or service connected with the arrangement.
- Royalties are a significant source of non-dues revenue for associations that can be reinvested in education, skills training, standard-setting, research and other activities. Royalties also closely resemble other passive income for tax-exempt organizations – such as rent, interest and dividends – which may not be directly mission-related but are excluded from UBIT.
- Royalties should not be taxed when there is little service offered by the tax-exempt organization in return for the payment