Tax Issues for Colleges and Universities

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What is IRS Position on Tax Treatment of University-Provided Residence for President?

- Section 119 says value of employer-provided residence not taxable if employee is required to live there and residence is located “on the business premises”
- Recent news story said that IRS denied tax-free treatment of residence provided by Ohio University to its President even though both tests apparently met
- Reason: The residence was not substantially used for University business activities
- Mirrors position taken by IRS in TAM 9404005
- What does “on the business premises” mean?
Update on Tax Treatment of Fraternities/Sororities

- Fraternities/sororities can be exempt under section 501(c)(7) as “social clubs”

- In PLR 201434022, the IRS denied section 501(c)(7) exemption to an “online” sorority because it conducted very little “commingling” and “fellowship”

- Another issue in the fraternity/sorority area is the extent to which a section 501(c)(3) university can provide assistance to a section 501(c)(7) fraternity/sorority

- Such assistance can only be provided if limited to “educational” items
Using Related Business Activities to Demonstrate a Single Profit Motive

- A section 501(c)(3) organization must conduct an unrelated business activity with a profit motive in order to be able to claim a loss deduction with respect to the activity.

- Can a university combine two separate but related activities to demonstrate a profit motive for each?

- In *Price v. Commissioner*, T.C. Memo 2014-253, the Tax Court said this can be done but only if (1) strong organizational/economic relationship between two activities, (2) conducting both furthers the same business purpose, and (3) the undertakings are similar in nature.
Setting Up a For-Profit Subsidiary

- Universities conduct business activities through for-profit subsidiaries primarily to (1) avoid having the activity taxed as UBI, and/or (2) insulate the university from liability.
- Issue is whether the IRS will “look through” the subsidiary and attribute the subsidiary’s activities to the university.
- In PLR 201503018, the IRS ruled that the activities of a for-profit subsidiary formed by a university would not be attributed to the university.
- The ruling sets forth various factors that led the IRS to this conclusion. Are all such factors required, or do they just reflect the particular facts of that case?
Can Foreign Students Elect to Be Treated as a Resident Alien for Tax Purposes?

- Recent posting on IRS website says that foreign students cannot claim the American Opportunity Tax Credit unless they “elect to be treated as a resident alien for tax purposes.” (See www.irs.gov/Individuals/American-Opportunity-Tax-Credit-Facts)

- But most experts have always thought that the nonresident alien/resident alien determination was totally objective with no “elections” possible
Can Foreign Students Elect to Be Treated as a Resident Alien for Tax Purposes? (cont’d)

- Might such a student in substance elect resident alien treatment if he/she fails to “claim” excluded days of presence in the U.S. on Form 8843 (the statement used by foreign students to report excluded days of presence in the U.S.)?
- Open question and needs to be clarified by the IRS
Form 1098-T: Reasonable Cause and Penalty Abatement

- IRS issued a blanket penalty waiver for colleges and universities that filed Forms 1098-T with missing or inaccurate TINs for the 2011 tax year; however, it has continued collections and even seized assets at some schools.

- IRS issued issue penalty waivers on a case by case basis with respect to the 2012 tax year; however, SBSE agents followed the incorrect procedures for Forms 1098-T and improperly denied many valid requests for penalty abatement.

  - The correct standard for TIN solicitation is whether the college or university “acted in a responsible manner” within the meaning of Treas. Reg. § 1.6050S-1(e)(3)(ii), which is a lower standard than the “reasonable cause” standards applicable to other types of information reporting.
A college or university acts in a responsible manner if it requests the student’s TIN in writing, notifies the student that the law requires the individual to furnish a TIN so that it may be included on an information return filed by the institution.

The regulations specifically state that colleges and universities may use Form W-9S “Request for Student's or Borrower's Taxpayer Identification Number and Certification” to satisfy their responsibilities or develop separate forms or parts of forms to request the student’s TIN, including admission forms or financial aid applications.

IRS agents, however, (1) did not allow colleges and universities to submit Form W-9S as evidence of TIN solicitation, (2) did not consider admission forms or financial aid applications as valid TIN solicitations, and (3) required two TIN solicitations when the regulations clearly say only one is necessary.
Form 1098-T: Reasonable Cause and Penalty Abatement (cont’d)

- SBSE now understands its error and will redo the penalty abatement procedures using the right standards for the 2012 year.
- Opinion:
  - Penalties are inappropriate because schools cannot verify TINs prior to filing.
  - Section 6103 should be modified to allow schools to use the IRS’s TIN verification system.
  - The IRS should issue a blanket waiver of penalties until the statute is changed.
President’s Proposal to Eliminate Box 2 on Form 1098-T

- Section 6050S(b)(2)(B) currently requires colleges and universities to report either *payments received* or *amounts billed*:
  - Box 1 of Form 1098-T: aggregate amount of payments received for qualified tuition and related expenses with respect to the student during the calendar year
  - Box 2 of Form 1098-T: aggregate amount billed for qualified tuition and related expenses with respect to the student during the calendar year

- President proposes to eliminate the Box 2 reporting option and to require Box 1 reporting.
  - In other words, the proposal would require a college or university to determine for each *calendar year* how much it *received* from each student and *categorize* the payment into *qualified* tuition and related expenses or *non-qualified* expenses. Sounds easy, doesn’t it?
President’s Proposal to Eliminate Box 2 on Form 1098-T (cont’d)

- It would be helpful for the IRS to have “clean” Box 1 data.
  - Prevent taxpayer fraud involving the American Opportunity Tax Credit
  - Encourage more students to claim AOTC if they are eligible.

- However, Box 1 reporting is not even theoretically possible.
  - Schools receive payments throughout the academic year running from fall to spring. Yet students must claim the AOTC on a calendar tax year, so Box 1 requires calendar year reporting.
  - However, schools have no way of knowing whether a payment they receive is for qualified tuition and related expenses or for nonqualified expenses. For example, a payment received in January may equally relate to qualified expenses billed in the fall of the prior calendar year or nonqualified expenses billed in the spring of the subsequent calendar year.
President’s Proposal to Eliminate Box 2 on Form 1098-T (cont’d)

- Opinion:
  - 6050S should be modified:
  - Form 1098-T Box 1 should not require schools to categorize payments received as qualified or nonqualified.
    - Colleges and universities know the total amount of uncategorized payments they receive from a student during the calendar year
    - They do not know the amount of payments received for qualified expenses.
  - Form 1098-T Box 2 should be kept.
    - Colleges and universities know the aggregate amount billed for qualified tuition and related expenses with respect to the student during the calendar year.
  - Together, modified Box 1 and Box 2 should give the IRS enough data to police the AOTC and students enough information to claim the credit.
Form 8300 FAQs

- Form 8300 is required when a trade or business receives a cash payment in excess of $10,000, whether in one transaction or a series of related transactions. See Code § 6050I.
- The purpose of the form is to assist government agencies, including the IRS and the Financial Crimes Enforcement Network, to detect and prevent money laundering.
- Colleges and universities are generally required to file Form 8300 when they receive cash payments (but not personal checks, credit/debit card, or wire transfer) in excess of $10,000 in connection with trade or business activities.
Are State-Supported Colleges and Universities Exempt From Filing Form 8300? The IRS website says “yes.”

Colleges and universities are required to file Form 8300 upon receiving, for one transaction or two or more related transactions, more than $10,000 in cash (for example, a tuition payment) in the course of their trade or business of providing educational products and services, regardless of the fact that the money may be excludable from gross income under section 115 of the Internal Revenue Code. The section 115 income exception is distinct from, and does not relieve an educational institution of, the requirement under section 6050I to file a Form 8300 information report.
State colleges and universities are not exempt from federal income tax under section 115.

- As instrumentalities of a state, they are exempt under the constitutional doctrine of intergovernmental tax immunity (federal government cannot tax the states). See PLR 9143048 (July 26, 1991).

The FAQ says Form 8300 is required for payments of tuition for educational services because it is a trade or business.

- Tuition is a related trade or business.
- Does that mean all trades or businesses of colleges and universities are potentially subject to Form 8300?
Form 8300 FAQ 10

“If a nonprofit organization is selling a tangible asset like furniture or vehicles and receives cash for it that exceeds $10,000, is there a Form 8300 filing requirement?” The FAQ says “no.”

Exempt organizations do not need to report the receipt of cash donations over $10,000 because an exempt organization is not, in carrying out its exempt function, considered in the definition of a trade or business under IRC section 162. To fall under this category, an organization must have obtained section 501(c)(3) or other tax-exempt status under the Internal Revenue Code; having in its possession a determination letter or an approved application for tax-exempt status from the Internal Revenue Service. The proceeds of a sale must be exempt from tax as part of the carrying on of the exempt organization's tax-exempt activities; in which case, Form 8300 reporting is inapplicable. Form 8300 is required for cash received in the conduct of unrelated trade or business activity of the organization.
Form 8300 FAQ 10:  
(cont’d)

- FAQ 10 distinguishes related from unrelated trade or business activities.
  - Section 501(c)(3) organizations are exempt from Form 8300 reporting on related income
  - Required to file Form 8300 on unrelated trade or business income.
- But tuition is related income, so why is it subject to Form 8300?
- FAQ 10 should have said that 501(c)(3)s are exempt from Form 8300 for donations because self-fundraising is not a trade or business.
  - A gift is defined as a payment without a quid pro quo.
  - If the school provides nothing in exchange for the gift, the gift cannot be income from a trade or business.
Questions and Answers