L. UBIT: SPECIAL RULES FOR PARTNERSHIPS

by
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1. Introduction

Most exempt organizations carry on all their activities directly within, typically, a not-for-profit corporation. Whether conducting its tax-exempt program, or generating investment income, a typical exempt organization may believe that it has no particular reason to venture outside its organizational structure. However, for a variety of reasons, many exempt organizations may choose to carry on some of their activities in other, more indirect ways. Some organizations decide to create wholly-owned taxable subsidiaries for both tax and non-tax reasons. Such a taxable entity often serves as a repository for what would otherwise constitute an unrelated trade or business under IRC 513(a), if it were conducted directly by the exempt organization. Other exempt organizations may choose to participate in a partnership, again for both tax and non-tax reasons. An exempt organization's participation in a partnership may take the form of either a general or a limited partner.

For many years exempt organizations have used partnerships, both as an investment vehicle and as a way to accomplish exempt purposes. Anecdotal evidence supports a conclusion that this trend continues, particularly in view of the popularity of the use of relatively new forms of entities such as a Limited Liability Company ("LLC") as a means of doing business in the context of both taxable and tax-exempt organizations. In view of the reality of exempt organizations' involvement in partnerships, the question presented is what tax consequences are attendant to an exempt organization that is either a general or a limited partner.

The issue of whether an organization's participation in a partnership affects its continued qualification for exemption has been the subject of a number of articles appearing in previous CPE Texts. The purpose of this article is to address issues arising with respect to the Unrelated Business Income Tax ("UBIT").

2. Background

In recent years there has been a proliferation of various types of partnerships and joint ventures involving exempt organizations and for-profit entities, particularly in the health care field. While such arrangements are becoming more sophisticated in terms of participants (such as LLC's, discussed elsewhere in this CPE text), and operations (such as whole hospital joint ventures addressed in Rev. Rul. 98-15 1998-12 I.R.B. 6), the underlying concerns with regard to these arrangements remain largely unchanged: whether an exempt organization's participation might adversely affect its exempt status, and whether such participation results in unrelated business taxable income ("UBTI") to the exempt organization.

The Service's initial position was that an IRC 501(c)(3) organization's participation in a partnership as a general partner was absolutely prohibited based on an inherent conflict of interest. See G.C.M. 36293 (May 30, 1975). If an exempt organization served as general partner in a limited partnership, it would be bound by its fiduciary duty to the limited partners to manage and operate the venture in such a way as to maximize the returns for the limited liability investors. This profit motive was said to be inconsistent with operating exclusively for exempt purposes. Thus, an exempt organization was precluded from serving as a general partner in a limited partnership.

As time passed, the Service's position evolved. G.C.M. 37852 (February 15, 1979) concluded that a partnership in which an exempt organization and a for-profit partner shared the expenses and the output of a blood fractionation laboratory would not preclude exemption. This G.C.M. implied that the Service's position was shifting and that participating in a partnership was not *necessarily* incompatible with the requirements for exemption.

Soon thereafter, the courts addressed this subject in the case of Plumstead Theatre Society, Inc. v. Commissioner, 74 T.C. 1324 (1980), aff'd 675 F.2d 244 (9th Cir. 1982). This case involved a theatrical production company needing to raise revenues through a joint venture vehicle. The court concluded that the organization's serving as a general partner in a limited partnership was not inconsistent with exemption, and that the organization possessed the characteristics of a nonprofit theater rather than a for-profit theater. Following Plumstead, the Service initiated a two-part test in G.C.M. 39005 (June 28, 1983) to determine whether participation by an otherwise exempt organization in a partnership as a general partner adversely affected qualification under IRC 501(c)(3). The test was designed to determine the following: first, whether participation by the organization in the partnership furthered its exempt purpose, and second, whether the partnership arrangement allowed the organization to act exclusively in furtherance of its exempt purpose.

The 1981 CPE Text at p. 5 re-emphasized the theory that a partnership arrangement between an exempt organization and a commercial entity or private investors would not per se jeopardize exemption, but whenever such an arrangement is present, all the facts and circumstances should be carefully scrutinized to determine whether any real conflicts exist between the charitable and for-profit purposes. The 1986 CPE Text at p. 136 noted that the Service had moved away from the strict prohibition on participation in partnerships to a facts and circumstances approach, and that a partnership agreement could be structured so as to protect the exclusive charitable interest of an exempt participant. The 1987 CPE Text at p. 224 briefly addressed UBIT issues by recognizing that in addition to determining the effect of partnership activities on exemption, a determination of whether the activities of the partnership generate UBIT must also be made. The 1993 CPE Text at p. 44 demonstrated how far the question of participation of exempt organizations in partnerships and joint ventures had evolved. The article talks in terms of "garden variety" hospital partnerships and joint ventures, citing G.C.M. 39732 (May 19, 1988). Finally, the 1999

CPE Text at p. 1 illustrates the most recent developments in the area of joint ventures by exempt health care organizations and discusses Rev. Rul. 98-15, supra.

3. Partnerships in General

A. Definition of Partners and Partnerships

IRC 7701(a)(2) provides that the term "partnership" includes a syndicate, group, pool, joint venture, or other unincorporated organization, through or by means of which any business, financial operation, or venture is carried on, and which is not a trust or estate or a corporation. The term "partner" includes a member of such a syndicate, group, pool, joint venture, or organization.

Subchapter K of the Internal Revenue Code sets forth extensive rules that are applicable to partners and partnerships. Under IRC 701, a partnership, as such, is not subject to tax, however, the partners are liable for income tax in their separate or individual capacities. In determining their income tax, IRC 702(a) generally provides that partners take into account separately their distributive share of the partnership's gains and losses, charitable contributions, dividends, taxes, other items of income, gain, loss, deduction, or credit, and certain taxable income or loss. Also, under IRC 702(b), the character of any item of income, gain, loss, deduction, or credit included in a partner's distributive share is determined as if such item were realized directly from the source from which realized by the partnership, or incurred in the same manner as incurred by the partnership. Finally, IRC 704(a) provides that a partner's distributive share of income, gain, loss, deduction, or credit is generally determined by the partnership agreement.

B. Limited Partnerships

A limited partnership has been defined by the original Uniform Limited Partnership Act as a partnership formed by two or more persons, having as members one or more general partners and one or more limited partners. The various items of partnership income, gain, loss, deduction, and credit flow through to the individual partners and are reported on their personal income tax returns.

A limited partnership is comprised of one or more general partners who manage the business and who are personally liable for partnership debts, and one or more limited partners who contribute capital and share in the profits, but who take no part in running the business and incur no liability with respect to partnership obligations beyond their capital contributions. See 59A Am. Jur. 2d Partnership sec. 1237, 1238 (1987).

C. Joint Ventures

Joint ventures and partnerships are governed by the same basic legal principles, but there are important differences. A joint venture typically is an ad hoc, one-time grouping that concerns itself with a single transaction or an isolated enterprise. Unlike a partnership,

a joint venture usually does not entail a continuing relationship among the parties. However, a joint venture is treated as a partnership for federal income tax purposes. See 59A Am. Jur. 2d Partnership sec. 14 (1987).

4. Taxation of Unrelated Business Income

A. General Rules

IRC 511(a) imposes a tax on the unrelated business taxable income of certain organizations described in IRC 401(a) and 501(c). IRC 512(a) provides that the term "unrelated business taxable income" means the gross income derived by any organization from an "unrelated trade or business." IRC 513(a) defines "unrelated trade or business" as any trade or business the conduct of which is not substantially related to the exercise or performance of an organization's exempt purpose or function. The modifications contained in IRC 512(b) generally exclude from UBIT interest, dividends, royalties, rents, and gain from the sale of property. Both IRC 512 and 513 contain numerous exceptions and special rules that are applicable to a wide variety of situations.

B. Special Rules for Partnerships

IRC 512(c)(1) provides that if an exempt organization is a member of a partnership regularly engaged in a trade or business which is an unrelated trade or business with respect to such organization, the exempt entity must include in its unrelated business taxable income that portion of its share of the partnership gross income (whether or not distributed), and the deductions attributable thereto, derived from the unrelated trade or business.

Under IRC 512(c)(2), if an exempt organization and the partnership in which it is a member have different taxable years, the partnership items that enter into the computation of the organization's UBTI must be based on the income and deductions of the partnership for the taxable year of the partnership which ends within the organization's taxable year.

Reg. 1.512(c)-1 contains an example of an exempt educational organization which is a partner in a partnership that operates a factory and also holds stock in a corporation. The example states that the exempt organization must include its share of the gross income from the operation of the factory, but not its share of any dividends received by the partnership from the corporation.

C. Unrelated Debt-Financed Income

IRC 514 provides that amounts derived by an exempt organization from "debt-financed property" are subject to tax under IRC 511. "Debt-financed property" is defined as any property held to produce income, and with respect to which there is "acquisition indebtedness." The term "acquisition indebtedness" as used in IRC 514(c) means the outstanding amount of the principal indebtedness incurred in acquiring or improving the

property. Acquisition indebtedness may also be present where the indebtedness is incurred either before or after the acquisition or improvement.

Reg. 1.514(c)-1(a)(2), Example (4), describes a situation in which an exempt organization was a limited partner in a partnership. The organization invested its own funds and some borrowed funds in the partnership, which purchased an office building. Part of the purchase price of the office building was borrowed from a bank that placed a mortgage on the building. The Example states that by reason of IRC 702(b) the character of any item realized by the partnership and included in the partner's distributive share is determined as if the partner realized such item directly from the source from which it was realized by the partnership and in the same manner. Therefore, a portion of the organization's income from the building is debt-financed income. Under these circumstances, both the indebtedness incurred by the organization in acquiring its partnership interest and the allocable portion of the partnership's indebtedness incurred with respect to acquiring the office building were incurred in acquiring income-producing property. The organization therefore has acquisition indebtedness attributable to both its own borrowing and the partnership's borrowing.

IRC 514(c)(9) provides an exception to the debt-financed rules for indebtedness incurred by a "qualified organization" in acquiring or improving any real property. "Qualified organizations" are qualified trusts under IRC 401, educational organizations described in IRC 170(b)(1)(A)(ii) and their supporting organizations described in IRC 509(a)(3), and organizations described in IRC 501(c)(25). The exception set forth in IRC 514(c)(9) contains a number of general requirements, as well as certain specific requirements that are applicable to real property held by a partnership. Reg. 1.514(c)-2 contains comprehensive rules with respect to partnership allocations under IRC 514(c)(9). Consistent with the statute, these regulations, which were prepared by the Office of Chief Counsel (Passthroughs & Special Industries) (CC:DOM:P&SI), engraft partnership concepts onto the debt-financed rules. Questions concerning the interpretation of these regulations are handled by CC:DOM:P&SI.

5. Situations Involving Partnerships and UBIT

A. Rev. Rul. 79-222

In Rev. Rul. 79-222, 1979-2 C.B. 236, an exempt employees' trust became a limited partner in a partnership that was created under the laws of a state which recognized such interests. The limited partners did not participate in the management of the partnership, and their liability was limited to the amount of their contributions. The partnership regularly carried on a trade or business. The revenue ruling holds that in determining unrelated business income derived from a partnership under IRC 512(c), there is no distinction between general and limited partners.

Rev. Rul. 79-222 notes that IRC 512(c) uses the term "member" of a partnership without qualification. In setting forth special rules applicable to members of partnerships in computing their UBTI, the revenue ruling states that IRC 512(c) makes no distinction between general and limited partners. The revenue ruling refers to S. Rep. No. 1402, 85th Cong., 2d. Sess. 2 (1958), 1958-1 C.B. 656, at 657, which states that, "under existing law, income from a partnership interest held by a charitable organization - whether the partnership interest was that of a general partner or that of a limited partner - is unrelated business income except to the extent that the income received by the partnership is specifically excluded as dividends, interest, royalties, and the like."

The revenue ruling holds that the exempt trust's investment as a limited partner in a partnership carrying on an unrelated trade or business may result in UBTI. Thus, a workable rule was adopted concerning an investment by an exempt organization in a partnership without regard to the exempt organization's involvement in the management of the partnership.

B. Service Bolt & Nut Co. Profit Sharing Trust v. Commissioner

In Service Bolt & Nut Co. Profit Sharing Trust v. Commissioner, 724 F.2d 519 (6th Cir. 1983), aff'g 78 T.C. 812 (1982), the court considered whether amounts received from limited partnership interests constitute UBTI. Qualified profit sharing trusts exempt under IRC 501(a) as organizations described in IRC 401(a) received income from limited partnerships. The court cited IRC 512(c), which provides that an exempt organization can be taxed on its share of the income received from a partnership of which it is a member, even though the partnership and not the exempt organization is the entity actively engaged in carrying on a trade or business. Refusing to distinguish between general partners and limited partners, the court concluded that income derived from limited partnership interests constitutes UBTI.

Rev. Rul. 79-222 and Service Bolt & Nut Co. Profit Sharing Trust, both supra, underscore the position that for UBIT purposes it makes no difference whether an exempt organization serves as a general or a limited partner.

C. Publicly Traded Partnerships

In the 1980's concerns arose that income received by an exempt organization from a publicly traded partnership would not be taxed at any level. The specific concern was that where an exempt organization invested in a publicly traded partnership, both the corporate level and shareholder tax could often be avoided. Consequently, as part of the Omnibus Budget Reconciliation Act of 1987, Congress amended IRC 512(c) to provide that an organization's share of the gross income of a publicly traded partnership would be treated as gross income derived from an unrelated trade or business. The organization's share of the partnership deductions was allowed in computing UBTI.

The term "publicly traded partnership" is defined in IRC 469(k)(2) as a partnership whose interests are either traded on an established securities market, or are readily tradable on a secondary market (or the substantial equivalent thereof). This provision applied whether or not the underlying character of the income was considered "related" or "unrelated;" the provision was applicable to partnership interests acquired after December 17, 1987. Under these provisions, exempt organizations were effectively deterred from investing in publicly traded partnerships, as all income from such investments was taxed as unrelated business income.

The Omnibus Budget Reconciliation Act of 1993 repealed the rule that automatically treated income from publicly traded partnerships as unrelated business income, effective for partnership years beginning on or after January 1, 1994. Thus, investments in publicly traded partnerships are now treated the same as investments in other partnerships for purposes of UBIT.

6. Examples of Recent Cases

During the past few years a number of private letter rulings and technical advice memoranda have addressed situations involving partnerships and UBIT. The following four examples are of particular interest:

A. Sale of a Partnership Interest

TAM 96-51-001 (June 27, 1996) discusses whether an exempt organization's sale of an interest in a partnership that owns debt-financed property is subject to UBIT. An IRC 501(c)(3) educational organization participated in a partnership, the purpose of which was to own, operate, manage, and develop various real estate holdings. These real estate holdings were held for investment and for ultimate disposition. The partnership's financial information reflected mortgages payable that were used to compute the average acquisition indebtedness under IRC 514. After paying tax on unrelated debt-financed income from rental payments, the organization sold its interest in the partnership. The gain on the sale was not reported as unrelated debt-financed income.

The TAM cited IRC 702(b) and 512(c)(1), which provide that the income of a partnership retains its character in the hands of the partners, and, thus, the organization reported its share of (rental) income attributable to debt-financed property. However, there was disagreement with regard to the treatment of income from the sale of the exempt organization's partnership interest, which was not purchased with borrowed funds, but the property within the partnership was purchased by the partnership itself with borrowed funds. Had the partnership instead sold the debt-financed real estate, its distributive share of gain from the sale would have been reportable as unrelated debt-financed income.

The organization argued that because it did not borrow directly to purchase its interest in the partnership, gain from the sale of the partnership interest, rather than from the sale of the debt-financed real estate itself held by the partnership, was not reportable as unrelated debt-financed income. However, the TAM asserted that whether the organization sold its interest in the partnership, or the partnership sold the real estate, the organization was accomplishing economically the same result of realizing its share of any appreciation in the debt-financed real estate.

The TAM stated the following:

> A partnership can be viewed in two ways under Subchapter K: as a separate entity or as an aggregate of its partners. See Casel v. Commissioner, 79 T.C. 424, 432-33 (1982). The entity view of partnerships treats each partner as owning no direct interest in partnership assets or operations, but only an interest in the partnership entity itself. The aggregate view treats each partner as the owner of a direct and undivided interest in partnership assets and operations. Subchapter K is an attempt to balance the entity view and the aggregate view to avoid the use of a partnership as a means of obtaining improper tax advantages. The many situations not clearly covered by Subchapter K can be resolved by both looking to whether the Subchapter applies an entity or aggregate approach in analogous situations and considering the purpose of the particular provision of the Code to be applied.
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> The House Conference committee report addressing the enactment of Subchapter K states that, even though Subchapter K takes an entity approach in transactions between a partner and a partnership, "no inference is intended, however, that a partnership is to be considered as a separate entity for purposes of applying other provisions of the internal revenue laws if the concept of the partnership as a collection of individuals is more appropriate for such provisions." H.R. Rep. No. 2453, 83d Cong., 2d Sess., 59 (1954).

The TAM cited Example (4) of Reg. 1.514(c)-1(a)(2), supra, which shows that both debt incurred to acquire a partnership interest and debt incurred by the partnership to acquire property are included in calculating that portion of a partnership's interest that is subject to acquisition indebtedness. Most importantly, the TAM stated that an interest in a

partnership that holds debt-financed property is effectively an interest in the underlying assets and liabilities of the partnership. The TAM emphasized that an anomalous result would occur if ownership of debt-financed property through a partnership would result in one tax treatment, when direct ownership would result in another. The TAM thus concluded:

> It would make no economic or policy sense that the exempt organization should defeat the existing aggregate approach to IRC 512(b)(4) simply by selling an intermediary rather than having the intermediary sell the debt-financed property. We believe that Congress could not have intended that section 512(b)(4) could be so easily avoided. Consequently, the organization's sale of its interests in the partnership at a gain resulted in unrelated business income.

As a side note, the TAM explained that the exception provided in IRC 514(c)(9)(A) was not applicable, because the indebtedness was incurred before the effective date of the provision, July 18, 1984. In addition, there was no showing that the specific requirements of IRC 514(c)(9)(B) had been met.

B. One General Partner & 39 Limited Partners

TAM 97-39-001 (May 30, 1996) discusses whether an exempt organization's distributive share of ordinary income from a limited partnership constitutes UBTI. A limited partnership was formed consisting of one general partner and 39 limited partners ("LP's"). The LP's consisted of 39 organizations, each of which owned an equal limited partnership interest. The partnership was formed for the purpose of administering purchasing and related activities. Each LP was an organization described in IRC 501(c)(3), and each LP owned and operated one or more medical facilities, principally hospitals described in IRC 170(b)(1)(A)(iii).

The purpose of the partnership was to facilitate the continuing availability of quality medical and pharmaceutical supplies and other products and services at attractive prices for use by the medical facilities owned or operated by the LP's and their affiliates. The partnership negotiates and executes purchase contracts between the partnership and vendors of such supplies and products, monitors the purchases by the LP's and their affiliates, and monitors the quality of such supplies. The partnership itself did not make any purchases; instead, the individual LP's made the purchases based on contracts negotiated by the partnership.

The partnership agreement provided that 90% of the income allocated to the LP's was to be allocated equally to each LP, and 10% was "to be allocated in proportion to the Limited Partner's level of compliance as determined by compliance monitoring reports compiled by the General Partner." (Thereafter, the 10% allocation was referred to as the "Bonus.") The share of the exempt organization described in the TAM was approximately

2%.

The partnership agreement contained a number of provisions, such as the requirement that the LP's participate in the 248 purchase contracts entered into between the partnership and various suppliers. The TAM describes umbrella agreements with major corporations in which an agreement may contain two or more product areas and requires the supplier to pay to the partnership an amount equal to 2% of the total sales of certain products to each LP and participating affiliates. The agreements refer to this payment either as a "management fee" or an "administrative fee." Also, the supplier pays certain amounts directly to each LP based on various formulas relating to the volume of purchases of certain products and/or services from the supplier. The partnership reports the fees as revenue and allocates the net income derived from this revenue to the GP and to the LP's, as described above. To encourage LP participation in the purchasing arrangements, LP's that extensively participate may be entitled to share in the Bonus.

The partnership reported as revenue the fees received from the vendors with which it had executed agreements. The partnership reported the net income from these revenues to each LP on their respective Schedule K-1. The partnership reported the Bonus to the LP's as a guaranteed payment and reported the remaining net income, other than investment gains and losses, as ordinary income. The TAM notes that if the various suppliers from whom the LP purchased supplies and services had paid the fees directly, rather than to the partnership, the LP would have received approximately 3% of the total fees earned by the partnership.

The TAM begins its analysis by stating that the partnership is engaged in a regularly carried on trade or business whereby fees are paid, the amount of which is based on the total amount purchased by the LP's during the year. Under IRC 512(c)(1) and Reg. 1.512(c)-1, each partner must take into account its share of this gross income. The TAM states that in order to determine whether the organizations's distributive share of the ordinary income from the partnership constitutes UBTI, it is necessary to "look through" the partnership and determine whether the partnership's trade or business is substantially related to the organization's exempt purposes under IRC 501(c)(3). The various purchasing activities engaged in by the partnership constitute a trade or business that generally does not further exempt purposes under IRC 501(c)(3). However, the TAM states that to the extent such activities result in medical and non-medical supplies and services being made available to the four hospitals that are controlled by the organization, such activities are substantially related to its exempt purpose. If the organization were to engage directly in purchasing activities on behalf of the hospitals that it controls and be paid a management or administrative fee, such amounts would not be subject to tax. The fact that such activities are carried out through a partnership should result in no different substantive treatment in accordance with IRC 512(c)(1).

Nevertheless, the TAM also states that to the extent such purchasing activities are directed to organizations other than the organization and the hospitals it controls, these activities do not meet the substantially related test under IRC 513(a). In general, if the

organization were to engage in purchasing activities on behalf of otherwise unrelated organizations, such as hospitals that it does not control, and be paid a management or administrative fee, such amounts would be subject to UBIT. Where such activities are carried out through a partnership, the same holding would be appropriate.

The TAM's analysis is as follows:

> Where a Partnership provides for an equal distribution to its limited partners, if an exempt organization's portion of management or administrative fees were no greater than the fees it would have received based on actual purchases, the organization would receive no unrelated business taxable income. However, if the management and administrative fees allocated to the exempt organization were greater than the fees it would have received based on actual purchases, the excess fees would represent income from performing purchasing services not only for itself but also for otherwise unrelated limited partners; such amounts would constitute unrelated business taxable income under section 512(a)(1) of the Code.
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> Stated another way, if the exempt organization's portion of actual purchases equals or exceeds its distributive share of management or administrative fees, then such fees are wholly attributable to the organization's accomplishment of its own exempt purposes. Conversely, if the exempt organization's portion of actual purchases is less than its distributive share of management or administrative fees, then a part of such fees is not attributable to the accomplishment of the organization's exempt purposes. Acting through the Partnership, the organization is receiving management and administrative fees in return for providing purchasing services to otherwise unrelated limited partners.

Consistent with this analysis, the TAM concluded that because the LP's 2% allocation of fees under the partnership agreement was no greater than the fees it would have received based on actual purchases (approximately 3%), the LP received no UBTI.

C. A Hospital's Partnership Interest

PLR 97-50-056 (Sept. 16, 1997) involves a number of issues, including whether income realized by an exempt hospital with respect to its partnership interest in a for-profit entity constitutes UBTI.

The subject of the PLR is an IRC 501(c)(3) organization that was the parent of another IRC 501(c)(3) organization. The organization also owned, directly and indirectly, some or all of the stock of a number of nonexempt corporations, through which it indirectly owned interests in several partnerships. The partnership provides durable medical equipment, respiratory equipment and infusion services to customers in their homes. It employs allied health professionals, nurses, technicians, pharmacists, therapists, and other supporting personnel.

Citing Rev. Rul. 68-376, 1968-2 C.B. 246, the PLR states that the activities of the partnership that are being carried on primarily for the convenience of the Hospital's patients are not considered an unrelated trade or business under IRC 513(a). However, the provision of medical equipment by the partnership to other persons does not further the exempt purpose of the Hospital, and, therefore, constitutes an unrelated trade or business.

The PLR refers to Service Bolt & Nut Co. Profit Sharing Trust v. Commissioner and Rev. Rul. 79-222, both supra, to support a conclusion that one-half of the partnership's unrelated business income, if any, will be attributed to the Hospital.

D. A Community Development Organization's LLC

PLR 1999-09-056 (December 7, 1998) describes an IRC 501(c)(3) community development organization, whose purpose was to strengthen the economy in an area generally considered to be one of the poorest and most economically distressed in the country. The organization established and controlled a limited liability company ("LLC") to obtain a portion of the financing needed to carry out its charitable programs. The organization, which is the managing member of the LLC, proposed to amend its LLC agreement to create a new funding vehicle by targeting new investors such as individuals and institutional investors. The new investment vehicle would pay the investors a variable return based on five year Treasury notes. The PLR concluded that the exempt organization, after the amendment to the LLC agreement, was still using the LLC to further its exempt purposes. The PLR also noted that the organization continued to assist economic growth in an economically depressed area and retained control over the LLC's operations.

7. Conclusion

Generally, the UBIT provisions cover situations where an exempt organization itself pursues an unrelated trade or business as a part of its overall activities. It is possible, however, for an organization to derive unrelated business income not only through direct business dealings, but also as a member of a partnership. If so, the organization must treat its share of the partnership income in the same fashion as if it had conducted the business activity in its own capacity. The special rules relating to partnerships contained in IRC 512(c) should be applied in such situations.