Tax Compliance for Bond-Financed Projects

The Ohio State University
Office of Financial Services
Overview

- Who?
- What?
- When?
- Why?
- What is the IRS looking for?
- What do you need to know?
- Exceptions
- Key Contacts for Questions
What is tax compliance?

- The University is implementing new compliance procedures relating to its tax-exempt bonds

- Questionnaires and information gathered by Ohio State for review to ensure adherence to IRS guidelines.

- NOTE: Not every question will be applicable to your specific project- please only answer those that apply
Who is Involved?

- Office of Business and Finance
  - Office of Financial Services

- Legal Counsel

- Departments with current or potential projects located in any bond financed facility
When is this taking place?

- The tax compliance process needs to begin immediately.
- The first questionnaires are due back by June 15, 2011 and then on an annual basis.
- Training and Education – May 2011
Why?

- In order to satisfy that bonds issued by Ohio State University will retain their tax-exempt status by adhering to IRS guidelines outlined in this presentation.

- The IRS may evaluate whether and to what extent tax-exempt bonds are being used to fund for-profit entities unrelated to the mission of the University.

- The IRS has increased its surveillance of University bond issuers. We need to report private business use in our annual IRS reporting. We also need to prepare ourselves in the eventuality of an IRS audit request.
What is the IRS looking for?

Private Business Use

- Use of bond financed property in a trade or business other than the borrower or use by the borrower in unrelated trade or business.
- A “qualified user” is a state or local government or a 501(c)(3) tax-exempt organization
- The federal government is NOT a qualified user
What is the IRS looking for?

Common Private Business Use

- Operating Leases
- Certain Management or Service Contracts with for-profit companies
- Certain Research Agreements
- Certain arrangements with the Federal Government or any agency thereof
- Joint Purchasing or Shared-Service Agreements with non tax-exempt entities.
- “Special Benefits” to non-qualified user
There are IRS guidelines that create “safe harbors”

“A safe harbor is a provision of a statute or a regulation that reduces or eliminates a party's liability under the law, on the condition that the party performed its actions in good faith or in compliance with defined standards.”

If a management or service contract meets the requirements of a safe harbor it does not constitute private business use.

Method of compensation (percentage of revenue, capitation fee, per-unit fees) and term of contract are factors in safe harbor analysis.

Generally looking for compensation that is reasonable and not based on net profits from the operation of the facility.
Research Contracts Raise Special Issues

• The federal government and private companies often enter into agreements with universities to use research facilities and these agreements can create private business use.

• Like management or service contracts, there are “safe harbors” for research agreements – if the agreement meets the requirements of a safe harbor it does not constitute private business use.

• Method of compensation (percentage of revenue, capitation fee, per-unit fees) and term of contract are factors in safe harbor analysis.

• Generally looking for compensation that is reasonable and not based on net profits from the operation of the facility.

Office of Financial Services
Research Contracts Raise Special Issues

- “Basic Research” means an investigation advancement of scientific knowledge not having specific commercial objectives.
- Product testing is not basic research
- There are 3 Safe Harbors under IRS guidelines

SAFE HARBOR #1 – Corporate Sponsor

- Basic Research supported or sponsored by a corporate sponsor is not private business use if the sponsor has to pay a fair price to license any resulting technology and price paid for the license is determined at the time the license becomes available
SAFE HARBOR #2 – Industry Sponsor

- Basic Research supported or sponsored by a corporate sponsor is not private business use if:
  - Qualified user decides how research is to be performed
  - Qualified user retains title to any patent or product created
  - Sponsor gets no more than a non-exclusive royalty-free license to use the resulting product

- Corporate sponsors can use either Safe Harbor #1 or Safe Harbor #2 – most will opt for #1 because they can get exclusivity if they pay fair market value.
Research Contracts Raise Special Issues

SAFE HARBOR #3 – Federal Government Sponsor

• Basic Research supported or sponsored by a corporate sponsor is not private business use if
  • Qualified user decides how research is to be performed
  • Qualified user retains title to any patent or product created
  • Any party other than qualified user gets no more than a non-exclusive royalty-free license to use the resulting product
What do you need to know?

Arrangements for the use of the facility by third parties

- The facilities, services, office space, equipment used or rented by board members, faculty, or administrative staff
- Athletic or residential facilities used for summer camps or private third parties
- Leasing or rent of the facility for conferences
What do you need to know?

- Service or Recharge Centers within the facility – known as “core labs”
  - “Service or recharge centers are centers that provide services to other University departments and would include printing services, graphic arts services or vehicle fleet management. In the research context, service or recharge centers are sometimes referred to as “core labs” or “research core facilities” and generally provide a specialized service or a piece of equipment for shared use by a variety of research teams. Examples include atomic microscope imaging services or the pharmacogenetics core lab.”

- Other “special benefits” to a non-qualified user in conjunction with the bond-financed facility.
  - Naming rights (individual vs. corporate)
  - Also include any third parties providing a significant source of revenue for the facility.
Exceptions

- While we need to be careful in examining private use of facilities, some private use is allowed. Please clear all private use issues through the Office of Financial Services in advance.
- General public use exception
- Temporary use exception
- “Incidental” Use
Contact Information

• If you have any questions regarding compliance and the forms, please contact the Office of Financial Services:

• Al Rodack – rodack.1@osu.edu
• Regina Wright – wright.304@osu.edu