



April 13, 2015

The Honorable John Thune  
*Co-Chair, Business Income Tax*  
Committee on Finance  
United States Senate  
219 Dirksen Senate Office Building  
Washington, DC 20510

The Honorable Benjamin Cardin  
*Co-Chair, Business Income Tax*  
Committee on Finance  
United States Senate  
219 Dirksen Senate Office Building  
Washington, DC 20510

Dear Senators Thune and Cardin:

Farm Bureau supports replacing the current federal income tax with a fair and equitable tax system that encourages success, savings, investment and entrepreneurship. We believe that the new code should be simple, transparent, revenue-neutral and fair to agricultural producers.

We commend the Committee on Finance on its methodical approach to tax reform by forming working groups to review current law and to solicit input from stakeholders. The American Farm Bureau Federation (Farm Bureau) is the nation's largest general farm organization, representing agricultural producers of nearly every type of crop and livestock across all 50 states and Puerto Rico. While Farm Bureau's primary focus is to advocate on behalf of farmers and ranchers, as a 501(c)5 tax-exempt organization, we offer the following comments on tax provisions that potentially impact our revenue stream and our ability to carry out our tax-exempt purpose.

#### Fair Market Test

Interest, rents, royalties and annuities (*i.e.*, payments of passive income) are generally received free of tax by exempt organizations. Under Internal Revenue Code Section 512(b)(13), however, these payments are subject to tax if they are received from a "controlled" organization (*e.g.*, a subsidiary). Prior to the enactment of the *Taxpayer Relief Act of 1997* (TRA 97), an organization was considered controlled if the exempt organization had a direct or indirect ownership interest of 80 percent or more in that organization. TRA 97 changed the ownership percentage to 50 percent.

The *Pension Protection Act of 2006* corrected an anomaly in TRA 97 which resulted in exempt organizations becoming liable for Unrelated Business Income Tax (UBIT) on payments of passive income, even when they reflect fair market amounts. For example, many exempt organizations receive rents at an arm's length amount from taxable subsidiaries. Under TRA 97 these exempt organizations were subject to tax, even though their receipt of rents from unrelated organizations under the exact same terms would not be subject to tax. The fair market test has subsequently been extended three times and most recently expired at the end of 2014. By making this provision permanent, Congress will preserve the impartiality of the fair market test and also prevent the long-term uncertainty that temporary extensions create for many exempt organizations.

## Royalty Income

A royalty is the money paid for the use of intellectual property such as an organization's name, logo, copyrighted content or mailing list. For example, insurance companies may pay royalties to certain tax-exempt organizations for use of their name or logo. 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. Quality-control provisions permit the tax-exempt organization to review and approve in advance all marketing materials to protect the organization's intellectual property. The discussion draft released last year by then- Ways and Means Committee Chairman Dave Camp proposed to treat royalty income as an unrelated trade or business that is subject to unrelated business income tax (UBIT).

Royalty agreements help associations and charities expand public awareness about their organization, and promote the industry, profession or cause they represent. Royalty agreements also allow tax-exempt organizations to offer their members a wide range of benefits from approved service providers and vendors, often at a reduced rate. Royalties are a significant source of non-dues revenue or non-contributed revenue that can be reinvested in education, skills training, standard-setting, research and other activities. Royalties closely resemble other passive income for tax-exempt organizations – such as rent, interest and dividends – which would remain tax-exempt.

## Qualified Sponsorship Payments

The safe harbor for qualified sponsorship payments is an exception to the unrelated business income tax (UBIT). A qualified sponsorship payment is a payment made by a business sponsor to support an activity or event of a tax-exempt organization where the business sponsor receives no more than an acknowledgement or "thank you" for that support – for example, "The Keynote Address, Sponsored by Ajax Corporation." The Camp plan proposed to render qualified sponsorship payments taxable if the acknowledgement refers to any of the business sponsor's product lines, and to require organizations receiving more than \$25,000 in qualified sponsorship payments for any one activity or event to treat all sponsors acknowledgement in substantially the same manner.

Qualified sponsorship payments should not be treated as advertising income in cases where there is no more than a "thank you" provided by the tax-exempt organization. There is also a clear expectation that a major sponsor of an activity or event would receive greater recognition than other sponsors. Requiring that all sponsors be acknowledged in substantially the same manner is non-intuitive and will discourage sponsorships.

## Advertising Income

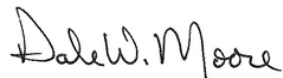
Although generally subject to unrelated business income tax (UBIT), the sale of advertising space in a tax-exemption organization's publication can produce an important source of revenue

for tax-exempt organizations. For example, an association publishes a monthly journal that contains articles and other editorial material of professional interest to its members. The organization sells advertising space in the journal either for conventional advertising or to merely identify the purchaser without a commercial message.

Both the discussion draft released last year by then-Ways and Means Committee Chairman Dave Camp and the Senate Finance Committee's Discussion Draft on Cost Recovery and Accounting Rules proposed changes in the deduction for advertising expense. This proposal to amortize a portion of advertising expenses marks a drastic departure from the historical treatment of advertising as an ordinary and necessary business expense, which has allowed it to be virtually one hundred percent deductible in the year in which the expense is made. Changing the deductibility of advertising expenses has the potential to create disincentives for advertising spending to the detriment of tax-exempt organizations that depend on this revenue.

Farm Bureau greatly appreciates your consideration of our views on tax provisions that impact tax-exempt organizations like Farm Bureau. We would be glad to meet with members of the Business Income Tax Working Group to provide additional information or to discuss our position in greater detail.

Sincerely,

A handwritten signature in cursive script that reads "Dale W. Moore".

Dale Moore  
Executive Director  
Public Policy