

**Playing by the Rules:  
A Fresh Look at Corporate Sponsorship & Affinity Program Income**

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**QUALIFIED CORPORATE SPONSORSHIPS**

1. **Defined**: Payments to a tax-exempt organization by a person engaged in a trade or business when there is no arrangement or expectation that the sponsor will receive a substantial return benefit for the payment other than the use or acknowledgment of the name or logo (or product lines) of the sponsor's trade or business in connection with the tax-exempt organization's activities.
2. **Payments Covered**: "Payment" means the payment of money, transfer of property, or performance of services.
3. **Substantial Return Benefit**: The term "substantial return benefit" means any benefit other than:
  - a. **2%**: Goods, services or other benefits of insubstantial value as defined by Reg § 1.513-4(c)(2)(ii).
    - i. ***Insubstantial Value***: Aggregate fair market value of all the benefits provided to the sponsor in connection with the sponsorship during the tax-exempt's taxable year does not exceed 2% of the amount of the payment to the tax-exempt. If the aggregate fair market value of the benefits exceeds 2% of the amount of the payment, then the entire fair market value of these benefits, not merely the excess amount, is a substantial return benefit.
      1. ***Illustration***:
        - a. N, an art museum, organizes an exhibition and receives a large payment from a corporation to help fund the exhibition. N recognizes the corporation's support by using the corporate name and established logo in materials publicizing the exhibition, which include banners, posters, brochures and public service announcements. N also hosts a dinner for the corporation's executives. The fair market value of the dinner exceeds 2% of the total payment. Because the fair market value of the dinner exceeds 2% of the total payment, the dinner is a substantial return benefit. Only that portion of the payment, if any, that N can demonstrate exceeds the fair market value of the dinner is a qualified sponsorship payment.<sup>1</sup>
      - b. **Use or Acknowledgement**: A use or acknowledgment described in Reg § 1.513-4(c)(2)(iv). In addition, product displays and sales are permissible. However, advertising is a taxable activity.

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<sup>1</sup> Reg § 1.513-4(f). Ex. 2.

- i. *Acknowledgement*: a use or acknowledgment that does not constitute a substantial return benefit to the sponsor includes:
  - 1. Logos and slogans that do not contain qualitative or comparative descriptions of the sponsor's products, services, facilities or company;
  - 2. A list of the sponsor locations, telephone numbers, or Internet address;
  - 3. Value-neutral descriptions, including displays or visual depictions, of the sponsor's product-line or services; and
  - 4. The sponsor's brand or trade names and product or service listings.
  
- ii. *Established Slogans*: The use of promotional logos or slogans that are an established part of the sponsor's identity does not, by itself, constitute advertising for purposes of determining whether a payment is a qualified sponsorship payment.<sup>2</sup>
  - 1. *Illustration*:
    - a. A pharmaceutical company makes a payment to U to fund U's booth at a health fair. U places a sign in the booth displaying the pharmaceutical company's name and slogan, "Better Research, Better Health," which is an established part of the company's identity.<sup>3</sup> The use of the slogan does not convert this acknowledgment into advertising.
  
- iii. *Weblinks*: The use of weblinks in website acknowledgements can result in taxable income if the linked site includes advertising or endorsement language.
  - 1. *Illustrations*:
    - a. W, a symphony orchestra, maintains a website containing pertinent information and a concert schedule. The Music Shop makes a payment to W to fund a concert series. W posts a list of its sponsors on its website, including the Music Shop's name and Internet address, which appears as a hyperlink from W's website to Music Shop's. The site does not promote the Music Shop or advertise its products. W's posting of the Music Shop's name and address constitutes acknowledgement of the sponsorship. The entire payment is a qualified sponsorship payment.<sup>4</sup>
    - b. X, a health-based charity, sponsors a year-long initiative to educate the public about a medical condition. A large company that makes a drug used in treating the condition provides funding for the initiative that helps X produce educational materials and post information on X's website. X's website contains a hyperlink to the company's website.

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<sup>2</sup> S Rept No. 105-33 (PL 105-34) p. 415.

<sup>3</sup> Reg § 1.513-4(f), Ex 9.

<sup>4</sup> Reg § 1.513-4(f), Ex 11.

On the company's website a statement appears which states that X endorses the product and suggests that the reader ask a doctor for a prescription if the reader has the condition. X reviewed the endorsement and gave permission for its use. The endorsement is advertising.<sup>5</sup>

iv. *Product Displays/Sales*: Distributing or displaying a sponsor's products (either by the sponsor or the tax-exempt organization) to the general public at a sponsored activity, whether for free or for remuneration, is not considered an inducement to purchase, sell or use the sponsor's product for these purposes and, thus, does not affect the determination of whether a payment is a qualified sponsorship payment.<sup>6</sup>

v. *Advertising*: Advertising is generally defined as:

1. Messages containing qualitative or comparative language;

a. *Illustration*:

“Visit the Music Shop today for the finest selection of music CDs and cassette tapes.” This is an advertisement because of the qualitative (“finest”) language.<sup>7</sup>

2. Price information or other indications of savings or value; or

3. An endorsement or other inducement to purchase, sell, or use the products or services.

a. *Illustration*:

i. The statement “X endorses the use of our drug, and suggests that you ask your doctor for a prescription if you have this medical condition” constitutes advertising<sup>8</sup>.

vi. *Mixed Messages*: A single message that contains both advertising and an acknowledgment is advertising.

1. *Illustration*:

a. S is a noncommercial broadcast station that airs a program funded by a local music store. In exchange for the funding, S broadcasts the following message: “This program has been brought to you by the Music Shop, located at 123 Main Street. For your music needs, give them a call today at 555-1234. This station is proud to have the Music Shop as a sponsor.” Because this single broadcast message contains both advertising and an acknowledgment, the entire message

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<sup>5</sup> Reg § 1.513-4(f), Ex 12.

<sup>6</sup> Conf Rept No. 105-220 (PL 105-34) p. 476.

<sup>7</sup> Reg § 1.513-4(f), Ex. 8.

<sup>8</sup> Reg § 1.513-4(f), Ex 12.

is advertising.<sup>9</sup>

c. Exclusive Arrangements:

- i. *Exclusive Sponsor.* An arrangement that acknowledges the sponsor as the exclusive sponsor of an exempt organization's activity, or the exclusive sponsor representing a particular trade, business or industry, generally does not, by itself, result in a substantial return benefit.<sup>10</sup>

1. *Illustration:*

- a. If in exchange for a payment, an organization announces that its event is sponsored exclusively by the sponsor (and does not provide any advertising or other substantial return benefit to the sponsor), the sponsor has not received a substantial return benefit.

- ii. *Exclusive Provider.* An arrangement that limits the sale, distribution, availability, or use of competing products, services, or facilities in connection with an exempt organization's activity generally results in a substantial return benefit.

1. *Illustration:*

- a. If in exchange for a payment, the exempt organization agrees to allow only the sponsor's products to be sold in connection with an activity, the sponsor has received a substantial return benefit.

- d. Contingent Payments: The term “qualified sponsorship payment” does not include any payment if the amount of such payment is contingent upon the level of attendance at one or more events, broadcast ratings, or other factors indicating the degree of public exposure to one or more events. However, if a sponsorship payment is contingent on an event actually taking place or being broadcast, the payment can still be a qualified sponsorship payment.

4. Allocation of Payment:

- a. Where Safe Harbor Doesn't Apply: The unrelated business income tax (UBIT) treatment of any payment (or portion thereof) that is not a qualified sponsorship payment is determined by application of the usual UBIT rules.
- b. Fair Market Value: The fair market value of any substantial return benefit provided as part of a sponsorship arrangement is the price at which the benefit would be provided between a willing recipient and a willing provider of the benefit, without regard to any other aspect of the sponsorship arrangement.
- c. Valuation Date: In general, the fair market value of the substantial return benefit is determined when the benefit is provided. However, if the parties enter into a binding, written sponsorship contract, the fair market value of any substantial return benefit

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<sup>9</sup> Reg § 1.513-4(f), Ex 7.

<sup>10</sup> Reg. § 1.513-4(c)(2)(vi)(A).

provided pursuant to that contract is determined on the date the parties enter into the sponsorship contract.

- i. *Subsequent Material Changes*: If the parties make a material change to a sponsorship contract, it is treated as a new sponsorship contract as of the date the material change is effective. A material change includes an extension or renewal of the contract, or a more than incidental change to any amount payable (or other consideration) pursuant to the contract.

1. *Illustration*:

- a. On June 30, 2001, a national corporation and Z, a charitable organization, enter into a five-year binding, written contract effective for years 2002 through 2007. The contract provides that the corporation will make an annual payment of \$5,000 to Z, and in return the corporation will receive no benefit other than advertising. On June 30, 2001, the fair market value of the advertising to be provided to the corporation in each year of the agreement is \$75, which is less than the disregarded benefit amount provided for in paragraph (c)(2)(ii) of this section (2% of \$5,000 is \$100). In 2002, pursuant to the sponsorship contract, the corporation makes a payment to Z of \$5,000, and receives the specified benefit (advertising). As of January 1, 2002, the fair market value of the advertising to be provided by Z each year has increased to \$110. However, for purposes of this section, the fair market value of the advertising benefit is determined on June 30, 2001, the date the parties entered into the sponsorship contract. Therefore, the entire \$5,000 payment received in 2002 is a qualified sponsorship payment.<sup>11</sup>

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<sup>11</sup> Reg. § 1.513-4(f).