



American Institute of CPAs
1455 Pennsylvania Avenue, NW
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December 2, 2015

Ms. Victoria Judson
Associate Chief Counsel (TEGE)
Office of Chief Counsel
Internal Revenue Service
1111 Constitution Avenue, N.W.
Washington, DC 20224

Ms. Janine Cook
Deputy Associate Chief Counsel (TEGE)
Office of Chief Counsel
Internal Revenue Service
1111 Constitution Avenue, N.W.
Washington, DC 20224

Re: Unrelated Business Income Expense Allocation Methodologies for Dual Use
Facilities

Dear Mmes. Judson and Cook:

The American Institute of CPAs (AICPA) strongly supports the efforts by the Internal Revenue Service (IRS) Office of Chief Counsel to issue clear guidance for tax preparers and taxpayers on how a tax-exempt organization should allocate expenses attributable to facilities and/or personnel which are used for both tax-exempt activities and unrelated trade or business activities. To further this mission, you requested we provide an outline with suggestions of various unrelated business income (UBI) expense allocation methodologies for consideration. Accordingly, see below for our suggested allocation methodologies which are based on our prior discussions with the Office of Chief Counsel.

The AICPA is the world's largest member association representing the accounting profession, with more than 412,000 members in 144 countries, and a history of serving the public interest since 1887. Our members advise clients on federal, state and international tax matters and prepare income and other tax returns for millions of Americans. Our members provide services to individuals, not-for-profit organizations, small and medium-sized businesses, as well as America's largest businesses.

The comments and recommendations included in this letter were developed by the AICPA Exempt Organizations Taxation Technical Resource Panel and approved by the Tax Executive Committee.

We appreciate your consideration of our recommendations and welcome the opportunity to discuss them further at our meeting with you on December 3, 2015. If you have any

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questions, please feel free to contact me at (801) 523-1051 or tlewis@sisna.com; Betsy Krisher, Chair, AICPA Exempt Organizations Taxation Technical Resource Panel, at (412) 535-5503, or bkrisher@md-cpas.com; or Ogochukwu Anokwute, AICPA Lead Technical Manager, at (202) 434-9231, or [oanokwute@aicpa.org](mailto: oanokwute@aicpa.org).

Sincerely,

A handwritten signature in black ink, appearing to read "Troy K. Lewis". The signature is written in a cursive style with a horizontal line above the first name.

Troy K. Lewis, CPA
Chair, AICPA Tax Executive Committee

AICPA SUMMARY OF UNRELATED BUSINESS INCOME EXPENSE ALLOCATION METHODOLOGIES FOR DUAL USE FACILITIES

Request from IRS Office of Chief Counsel:

Provide a list of bullet points addressing how an exempt organization should allocate expenses attributable to facilities and/or personnel which are used both for exempt activities and unrelated trade or business activities.

AICPA Recommendations:

1. Deductible expenses must bear a proximate and primary relationship to the conduct of the activity.
2. Deductible expenses include both direct costs and indirect costs.
3. Indirect costs include *fixed* expenses (those which do not change when the unrelated activity is conducted or not conducted) and *variable* expenses (those which increase or decrease when the unrelated activity is conducted or not conducted).
4. The methodology for allocating expenses relating to dual-use facilities/personnel should be reasonable and consistently¹ followed from year to year.
5. The methodology for allocating expenses relating to dual-use facilities/personnel should be based on the character of the expenses involved.
 - a. Facility costs apportioned based on the portion of the facility used for each activity.
 - b. Personnel costs apportioned based on the time spent on each activity.
6. The methodology for allocating expenses relating to dual-use facilities/personnel might be based on one or more of the following:
 - a. Square footage.
 - b. Hours/days spent on the activity (see #7 below).
 - c. Ratio of direct costs to allocable costs.
 - d. Ratio of revenue generated in unrelated activity to total revenue earned from dual-use facility/personnel.
 - e. Cost allocation methodology provided for universities as described in OMB Circular A-21.²
 - f. Cost allocation methodology provided for Medicare cost reporting (“step-down”).

¹ Allocation methods are revised from time to time as the organization’s activities and related expenses evolve over time. These changes which enhance the accuracy of expense allocations do not violate the consistency principle.

² We are aware that OMB Circular A-21 has been superseded but believe it has value for this purpose. In particular, we suggest consideration of the safe harbors for allocation of expenses which were presented in a draft revenue procedure authored by National Association of College and University Business Officers.

- g. Cost allocation methodology provided for lobbying activities in Treas. Reg. §§ 1.162-28.
7. We suggest three potential methods for allocating facility expenses based on the number of days the facility is used for unrelated activities.
- a. Method #1 is a simplified “safe harbor” method for use by an organization lacking detailed records to support the number of days the facility is actually used or available for use in all activities. The allocation ratio computation is as follows:

Number of days used for unrelated activities *divided by*
365 (or number of days in tax year if less)

- b. Method #2 is for use by an organization lacking detailed records to support the number of days the facility is actually used for all activities but which has records to support the number of days the facility was available for use. The allocation ratio computation is as follows:

Number of days used for unrelated activities *divided by*
Number of days available for use in all activities

- c. Method #3 is for use by an organization which has detailed records to support the number of days the facility is actually used for all activities. The allocation ratio computation is as follows:

Number of days used for unrelated activities *divided by*
Number of days actually used for all activities