

Internal Revenue Service, Treasury

§ 1.512(a)-4

if a taxpayer wishes to rely on the rules stated therein for taxable years beginning before December 13, 1967, he may do so.

[T.D. 7392, 40 FR 58638, Dec. 18, 1975, as amended by T.D. 7438, 41 FR 44392, Oct. 8, 1976; T.D. 7935, 49 FR 1694, Jan. 13, 1984; T.D. 8991, 67 FR 20437, Apr. 25, 2002]

§ 1.512(a)-2 Definition applicable to taxable years beginning before December 13, 1967.

(a) *In general.* The unrelated business taxable income which is subject to the tax imposed by section 511 is the gross income, derived by any organization to which section 511 applies, from any unrelated trade or business regularly carried on by it, less the deductions allowed by chapter 1 of the Code which are directly connected with the carrying on of such trade or business, subject to certain exceptions, additions, and limitations referred to below. In the case of an organization which regularly carries on two or more unrelated businesses, its unrelated business taxable income is the aggregate of its gross income from all such unrelated businesses, less the aggregate of the deductions allowed with respect to all such unrelated businesses. For provisions generally applicable to the unrelated business tax, see § 1.511-3, and for rules applicable to the determination of the adjusted basis of property, see paragraph (a)(2) of § 1.514(a)-1.

(b) *Effective date.* Except as provided in paragraph (f) of § 1.512(a)-1, this section is applicable with respect to taxable years beginning before December 13, 1967.

[T.D. 6500, 25 FR 11737, Nov. 26, 1960, as amended by T.D. 6939, 32 FR 17660, Dec. 12, 1967]

§ 1.512(a)-3 [Reserved]

§ 1.512(a)-4 Special rules applicable to war veterans organizations.

(a) *In general.* For taxable years beginning after December 31, 1969, this section provides special rules for the determination of the unrelated business taxable income of an organization described in section 501(c)(19). In general, the rules contained in sections 511 through 514 which are applicable to any organization listed in section 501(c)

apply in determining the unrelated business taxable income of an organization described in section 501(c)(19). However, that amount which is paid by members to the organization for the purpose described in paragraph (b)(1) of this section, if set aside from other organizational monies and accounts in an insurance set aside, may be excluded from the unrelated business taxable income of the organization. The insurance set aside shall be used exclusively for providing insurance benefits, for the purposes specified in section 170(c)(4) of the Code, for the reasonable costs of administering the insurance program that are directly related to such set aside, or for the reasonable costs of distributing funds for section 170(c)(4) purposes. If an amount so set aside is used for any purposes other than those described in the preceding sentence, it shall be included in unrelated business taxable income without regard to any modifications provided by section 512(b), in the taxable year in which it is withdrawn from such set aside. Amounts will be considered to have been withdrawn from an insurance set aside if they are used in any manner inconsistent with providing insurance benefits, paying the reasonable costs of administering the insurance program for section 170(c)(4) purposes and for costs of distributing funds for section 170(c)(4) purposes. An example of a use of funds which would be considered a withdrawal would be the use of such funds as security for a loan.

(b) *Insurance set aside—(1) Purpose of payments by members.* Payments by members (including commissions on such payments earned by the set aside as agent for an insurance company) into an insurance set aside must be for the sole purpose of obtaining life, sick, accident or health insurance benefits from the organization or for the reasonable costs of administration of the insurance program, except that such purpose is not violated when excess funds from an experience gain are utilized for those purposes specified in section 170(c)(4) or the reasonable costs of distributing funds for such purposes. Funds for any other purpose may not be set aside in the insurance set aside.

(2) *Income from set aside.* In addition to the payments by members described

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in paragraph (b)(1) of this section, only income from amounts in the insurance set aside (including commissions earned as agent for an insurance company) may be so set aside. Moreover unless such income is used for providing insurance benefits, for those purposes specified in section 170(c)(4), or for reasonable costs of administration, such income must be set aside within the period described in paragraph (b)(3) of this section in order to avoid being included as an item of unrelated business taxable income under section 512(a)(4).

(3) *Time within which income must be set aside.* Income from amounts in the insurance set aside generally must be set aside in the taxable year in which it would be includible in gross income but for this section. However, income set aside on or before the date prescribed for filing the organization's return of unrelated business taxable income (whether or not it had such income) for the taxable year (including any extension of time) may, at the election of the organization, be treated as having been set aside in such taxable year.

(4) *Computation of income from set aside.* Income from amounts in the insurance set aside shall consist solely of items of investment income from, and other gains derived from dealings in, property in the set aside. The deductions allowed against such items of income or other gains are those amounts which are related to the production of such income or other gains. Only the amounts of income or other gain which are in excess of such deductions may be set aside in the insurance set aside.

(5) *Requirements for set aside.* An amount is not properly set aside if the organization commingles it with any amount which is not to be set aside. However, adequate records describing the amount set aside and indicating that it is to be used for the designated purpose are sufficient. Amounts that are set aside need not be permanently committed to such use either under state law or by contract. Thus, for example, it is not necessary that the organization place these funds in an irrevocable trust. Although set aside income may be accumulated, any accumulation which is unreasonable in

amount or duration is evidence that the income was not accumulated for the purposes set forth. For purposes of the preceding sentence, accumulations which are reasonably necessary for the purpose of providing life, sick, health, or accident insurance benefits on the basis of recognized mortality or morbidity tables and assumed rates of interest under an actuarially acceptable method would not be unreasonable even though such accumulations are quite large and the time between the receipt by the organization of such amounts and the date of payment of the benefits is quite long. For example, an accumulation of income for 20 years or longer which is determined to be reasonable necessary to pay life insurance benefits to members, their dependents or designated beneficiaries, generally would not be an unreasonable accumulation. Income which has been set aside may be invested, pending the action contemplated by the set aside, without being regarded as having been used for other purposes.

[T.D. 7438, 41 FR 44393, Oct. 8, 1976]

§ 1.512(a)-5T Questions and answers relating to the unrelated business taxable income of organizations described in paragraphs (9), (17) or (20) of Section 501(c) (temporary).

Q-1: What does section 512(a)(3), as amended by the Tax Reform Act of 1984 (Act), provide with respect to organizations described in paragraphs (9), (17) or (20) of section 501(c)?

A-1: In general, section 512(a)(3), as amended by section 511 of the Act, extends the rules for determining the unrelated business income tax of voluntary employees' beneficiary associations (VEBAs) to supplemental unemployment compensation benefit trusts (SUBs) and group legal service organizations (GLSOs). The section also restricts the amount of income that may be set aside by such organizations for exempt purposes.

Q-2: What is the effective date of the amendments to section 512(a)(3)?

A-2: The amendments to section 512(a)(3) will apply to income earned by VEBAs, SUBs or GLSOs after December 31, 1985, in the taxable years of such organizations ending after such date. For purposes of applying section 512(a)(3) to the first taxable year of such an organization ending after December 31, 1985, the income of the VEBA, SUB or GLSO earned after December 31, 1985, will be determined by allocating the total income earned