

Sponsorship vs. Advertising: Know the Difference to Save Tax Dollars

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If you were to randomly poll a hundred people about the difference between a sponsorship and advertising, most would probably say they're the same. But in the world of nonprofit accounting, the difference could end up costing—or saving—an organization thousands of dollars in taxes.

Sponsorship vs. Advertising

If a business pays a nonprofit to have its logo, slogan, or other information displayed throughout the nonprofit organization's event, that money could be considered either sponsorship or advertising. There are several qualitative factors to consider, key of which is the concept of "substantial benefit." Did the business receive a substantial benefit for having its logo on display throughout the event? If the answer is "no," the organization would recognize sponsorship income, which is not subject to an unrelated business income tax (UBIT). If the answer is "yes," the organization would recognize advertising income, which is subject to UBIT.

So what qualifies as a substantial benefit? Like most tax-related questions, the IRS's answer is, "It depends." Some qualitative factors provide a substantial benefit, which renders the contribution of advertising-income subject to UBIT. If the message contains comparative price information, endorsements, or persuasive language to buy products, the IRS considers that a substantial benefit has been provided. On the other hand, payment to post only the business's logo, slogan, location, and/or contact information will most likely be considered as sponsorship income not subject to UBIT.

Real World Example

Consider the following hypothetical example:

- DEF Wellness Inc., a nonprofit healthcare organization, will throw a gala fundraising event to support its mission. The organization has explored the idea of allowing local businesses to sponsor different rooms at the event venue. Several businesses have contacted DEF Wellness with messages they'd like to display.
- KMC LLC, a local doctor's office, has submitted a potential sponsorship message for Room 1. The message, which will be posted on the door, is to contain the KMC logo and its slogan, "We care for our patients, so you don't lose your patience!" The message does not contain any competitive information or pricing information, nor does it make it appear that DEF endorses KMC's services. As a result, DEF would recognize the revenue as sponsorship revenue not subject to UBIT.

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- AMS Inc., a for-profit medical device manufacturer, has submitted a potential sponsorship message for Room 2. The message to be posted on the door of Room 2 contains the logo for AMS and a photo of the company's new product, an X-ray machine. Printed under photo of the machine is its price and the words: "More visible than our competitor's machines! Buy for your medical practice today!" The message clearly contains comparative or competitive information, pricing information, and persuasive language directed at potential customers. AMS thus expects a substantial benefit in return for its payment to DEF, and those dollars would be considered advertising income subject to UBIT.
- If DEF is looking to maximize sponsorship income without being subject to tax, the nonprofit should seek more sponsors like KMC LLC and fewer like AMS Inc.

Know the Difference

Management of a nonprofit organization should be cognizant of these nuances when it comes to planning their sponsored events. Knowing the subtle differences between sponsorships and advertising can save your nonprofit thousands of dollars in UBIT, allowing you to use those funds to support your mission and purpose.

ABOUT THE AUTHORS

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