

Raffles & Unrelated Business Income

Tax Issues that Affect Civil Air Patrol

What the IRS Says about UBI

- Unrelated Business Income (UBI) is revenue derived by a tax exempt organization from a regularly carried on trade or business which is not substantially related to the exempt purpose of the organization.
- Tax exempt organizations may be subject to taxes on UBI at corporate tax rates.
- Gaming open to the general public may result in Unrelated Business Income Tax (UBIT) for the tax exempt organization.
- Gaming or lotteries are not charitable activities. Using proceeds from these activities for charitable causes does not make the activities charitable.
- Tax exempt organizations can not conduct gaming as a primary activity.
- Any income derived from bingo games may be exempt from UBIT as long as the game is legal under state and local laws and not in direct competition with games conducted by for-profit organizations. If for-profit organizations can regularly carry on bingo games in any part of a jurisdiction, the exemption does not apply.
 - In order to qualify for the bingo exclusion, the wagers must be placed, winners determined, and prizes distributed in the presence of all persons placing wagers in that game.
- An exception may also be available if substantially all of the work in carrying on the activity is performed by volunteers. Tips, free drinks, and free food are considered compensation when determining whether the individuals carrying out the activity are volunteers.
 - If tips are even allowed, the volunteer labor does not qualify for the exception.
- Public entertainment activities are excluded from UBI if they are performed in conjunction with an international, national, state, regional, or local fair or exposition, and in accordance with state laws.
- The sale of advertising in a periodical of an exempt organization is UBI and is subject to UBIT.

RAFFLES

- Raffles are a form of gaming because they involve making wagers for the chance to win prizes.
 - Tax exempt organizations (under section 501 of the Internal Revenue Code) are required to report raffle prizes awarded if the fair market value of the prize less the wager is \$600 or more and at least 300 times the amount of the wager.
 - Form W-2G is used for reporting.
 - This form will be completed at CAP NHQ.
 - The Region, Wing, or Unit conducting the raffle is responsible for obtaining the information required to complete the Form W-2G and submitting this information to CAP NHQ.
 - Raffle prizes are subject to withholding tax if the fair market value of the prize less the wager exceeds \$5,000.
 - Taxes can be withheld from the winnings, if cash, or collected from the winner if non-cash.
 - $(\text{prize value} - \text{wager}) \times 25\% = \text{withholding tax}$
 - If this method is used, the Region, Wing, or Unit conducting the raffle is responsible for collecting the appropriate taxes from the winner.
 - Taxes can be paid on behalf of the winner by the organization.
 - $(\text{prize value} - \text{wager}) \times 33.33\% = \text{withholding tax}$
 - If this method is used, the Region, Wing, or Unit is responsible for the taxes.
 - Backup withholding of 28% may apply if the winner does not furnish a correct taxpayer identification number and 25% has not been withheld. This would mean that prizes not subject to the 25% withholding tax may be subject to backup withholding if the correct information is not obtained.
 - The Region, Wing or Unit conducting the raffle will be held responsible for collecting and/or paying these taxes.
 - It is important to note that all winnings may also be subject to state taxes.
 - Also note that wagers received can be taxable to CAP if the proceeds are used for the general operating expenses of the organization.

A Perfect Example

1. A Wing decides that it would like to conduct a raffle to raise needed funds for an upcoming event.
2. The Wing makes sure the raffle is allowable under state and local law and obtains the necessary approvals for holding the raffle.
3. The Wing contacts their WFA to go over the tax liability the raffle may cause. The Wing decides to collect the taxes from the winner at the time the prize is awarded.
4. The WFA notifies NHQ of the raffle.
5. The Wing sells raffle tickets for over a predetermined time period being sure to inform the ticket purchasers of their intent to collect taxes and the tax amount.
6. The Wing holds the drawing for the raffle prize. Once the winner is chosen, the Wing obtains all necessary information for the IRS Form W-2G and the money for the taxes.
7. The Wing notifies their WFA that the raffle is complete and the taxes have been collected.
8. The WFA notifies NHQ about the completion of the raffle.
9. NHQ completes all necessary IRS paperwork, processes the payment to the IRS electronically, and initiates a request to draw the funds back from the Wing.

Sources of Information

IRS Pub. 3079 Gaming Publication for Tax-Exempt Organizations

IRS Pub. 598 Tax on Unrelated Business Income of Exempt Organizations

IRS Notice 1335 Gaming Activities

IRS Notice 1340 Tax-Exempt Organizations and Raffle Prizes

Figure 1

Regular Gambling Withholding & Backup Withholding Chart		
GAME	REGULAR GAMBLING WITHHOLDING Required Prizes More Than	BACKUP WITHHOLDING Applies on Prizes Equal to or Exceeding
Bingo	No Withholding Required	\$1,200
Instant Bingo, Pull-Tabs, Raffles	\$5,000	\$600