Income from certain research grants or contracts may be exempt from the unrelated business income tax depending on the type of research. The following types of research are exempt:

- research performed for the US government or any agency or instrumentality of the US
- research performed by a college, university, or hospital “for any person”
- research performed for any person in the case of an organization operated primarily for purposes of carrying on “fundamental” research (as distinguished from “applied”), the results of which are freely made available to the general public

The regulations further limit these exclusions by providing that research does not include activities of a type ordinarily carried on as an incident to commercial or industrial operations. Ordinary testing and inspection of products or materials is not exempt. The term fundamental research doesn’t include research conducted for the primary purpose of commercial or industrial application.

**Sale of Research By-Products**

The sale of products resulting from research activities may or may not be exempt from UBTI. If the product is sold in substantially the same state it is in on completion of the research, the sale does not constitute unrelated business income. However, if further manufacture or processing of the product occurs, the gross income is considered unrelated, unless the manufacturing activities themselves contribute importantly to the accomplishment of the exempt purpose of the organization (i.e. education of students).

*Example.* An experimental dairy herd maintained for scientific purposes by a research organization produces milk and cream in the ordinary course of operation of the project. The sale of the milk and cream would not be gross income from conduct of unrelated trade or business. On the other hand, if the research organization were to utilize the milk and cream to produce ice cream, the gross income from the sale of such products would be from the conduct of unrelated trade or business (unless the educational purpose exception above applies).