

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
Attn: Mandatory Review, MC 4920 DAL
1100 Commerce St.
Dallas, TX 75242

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Date: April 1, 2008

Number: 200829041

Release Date: 7/18/2008

LEGEND

ORG = Organization name XX = Date Address = address
UIL: 501.07-01

ORG
ADDRESS

**Employer Identification
Person to Contact/ID Number:**

Contact Numbers:
Voice
Fax

CERTIFIED MAIL – RETURN RECEIPT REQUESTED

Dear :

In a determination letter dated February 21, 19XX, you were held to be exempt from Federal income tax under section 501(c)(7) of the Internal Revenue Code.

Based on recent information received, we have determined you have not operated in accordance with the provisions of section 501(c)(7) of the Code. Accordingly, your exemption from Federal income tax is revoked effective July 1, 20XX. This is a final adverse determination letter with regard to your status under section 501(c)(7) of the Code.

We previously provided you a report of examination explaining why we believe revocation of your exempt status is necessary. At that time, we informed you of your right to contact the Taxpayer Advocate, as well as your appeal rights. On November 2, 20XX, you signed Form 6018-A, *Consent to Proposed Action*, agreeing to the revocation of your exempt status under section 501(c)(7) of the Code.

You have filed taxable returns on Form[s] 1120, *U.S. Corporation Income Tax Return*, for the year[s] ended June 30, 20XX and June 30, 20XX with us. For future periods, you are required to file Form 1120 with the appropriate service center indicated in the instructions for the return.

You have the right to contact the Office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal Appeals

process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling.

You may call toll-free, and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

If you have any questions, please contact the person whose name and telephone number are shown at the beginning of this letter.

Sincerely,

Marsha A. Ramirez
Director, EO Examinations



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY

Internal Revenue Service
Wells Fargo Place
30 East 7th Street - Suite 1130B
St. Paul, MN 55101

September 19, 2007

ORG
ADDRESS

Taxpayer Identification Number:

Form:

Tax Year(s) Ended:

Person to Contact/ID Number:

Contact Numbers:

Telephone:

Fax:

CERTIFIED MAIL – RETURN RECEIPT REQUESTED

Dear :

We have enclosed a copy of our report of examination explaining why we believe an adjustment of your organization's exempt status is necessary.

If you do not agree with our position you may appeal your case. The enclosed Publication 3498, *The Examination Process*, explains how to appeal an Internal Revenue Service (IRS) decision. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process.

If you request a conference, we will forward your written statement of protest to the Appeals Office and they will contact you. For your convenience, an envelope is enclosed.

If you and Appeals do not agree on some or all of the issues after your Appeals conference, or if you do not request an Appeals conference, you may file suit in United States Tax Court, the United States Court of Federal Claims, or United States District Court, after satisfying procedural and jurisdictional requirements as described in Publication 3498.

Letter 3610 (04-2002)
Catalog Number 34801V

You may also request that we refer this matter for technical advice as explained in Publication 892, *Exempt Organization Appeal Procedures for Unagreed Issues*. If a determination letter is issued to you based on technical advice, no further administrative appeal is available to you within the IRS on the issue that was the subject of the technical advice.

If you accept our findings, please sign and return the enclosed Form 6018, *Consent to Proposed Adverse Action*. We will then send you a final letter modifying or revoking exempt status. If we do not hear from you within 30 days from the date of this letter, we will process your case on the basis of the recommendations shown in the report of examination and this letter will become final. In that event, you will be required to file Federal income tax returns for the tax period(s) shown above. File these returns with the Ogden Service Center within 60 days from the date of this letter, unless a request for an extension of time is granted. File returns for later tax years with the appropriate service center indicated in the instructions for those returns.

You have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free 1-877-777-4778 and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

If you have any questions, please call the contact person at the telephone number shown in the heading of this letter. If you write, please provide a telephone number and the most convenient time to call if we need to contact you.

Thank you for your cooperation.

Sincerely,

Marsha A. Ramirez
Director, EO Examinations

Enclosures:
Publication 892
Publication 3498
Form 6018
Report of Examination
Envelope

Explanation of Items

Name of Taxpayer

ORG

| June 30, 20XX

Year/Period Ended

June 30, 20XX

LEGEND

ORG = Organization name

XX = Date

CO-1 = 1st companyCO-2 = 2nd company**ISSUE: REVOCATION OF EXEMPT STATUS****FACTS:**

ORG was organized to conduct social activities for the members of the CO-1. According to IRS records, the club was granted exemption from income tax as an organization described in IRC 501(c)(7) in 19 . The members are also members of the ORG. According to the Form 1024, the social activities which will be conducted consisted of golf outings, dances, fish fries and other social activities. The organization also conducted fundraising activities in the form of raffles. According to the taxpayer, receipts will principally be due from bar sales, rental of facilities, management fee from and Bingo. All activities were open to members and nonmembers, with the exception of the management fee. However, the organization did not keep record of the amount of member and nonmember income for the bar and pull-tab sales.

ORG conducted charitable gaming on-site and off-site. The bar was operated on-site, however, the off-site location for the operation of pull-tab sales were at the CO-2. All gambling and bar operations were reported on Form 990-T as unrelated business income. The organization has made its lawful expenditures donations.

The organization filed Forms 990 and 990-T for the years ending June 30, 20XX and June 30, 20XX.

LAW:

Internal Revenue Code IRC section 501(c)(7) provides for the exemption from Federal income taxes for Social Clubs. Income Tax Regulation section 1.501(c)(7)-1 states that if a Social Club makes its social and recreational facilities available to the general public it will not qualify for tax-exempt status. However, Revenue Procedure 71-17 as amended by Public Law 94-568 provides certain gross receipts safe harbors; i.e. Social Clubs may receive up to 35% of their total gross receipts, including investment income, from sources outside of their membership without jeopardizing their tax-exempt status. Within this 35% limit, no more than 15% of a club's gross receipts may be derived from nonmember use of the club's facilities and/or services or from other activities not furthering social or recreational purposes for members. If these standards are exceeded, a Social Club will not qualify for exemption pursuant to IRC section 501(c)(7).

The Committee Reports for Public Law 94-568 (Senate Report No. 94-1318 2d Session, 1976-2 C.B. 597) state that it is intended that social clubs should be permitted to receive up to 35 percent of their gross receipts, including investment income, from sources outside of their memberships without losing their exempt status. Within this 35 percent amount, not more than 15 percent of the gross receipts should be derived from the use of a social club's facilities or services by the general public. This means that an exempt social club may receive

Explanation of Items

Name of Taxpayer

ORG

| June 30, 20XX

|Year/Period Ended

June 30, 20XX

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up to 35 percent of its gross receipts from a combination of investment income and receipts from non-members, so long as the latter do not represent more than 15 percent of total receipts.

Additionally, activities conducted by a social club need to further its exempt purposes. Traditional business activities are those activities that further a social club even if conducted solely on a membership basis. Activities that are not in furtherance of a social club's exempt purpose are referred to as nontraditional business activities. A social club is prohibited from conducting more than an insubstantial amount of nontraditional business activities. The prohibition against the conduct of nontraditional business activities applies equally to business with member and nonmembers.

GOVERNMENT'S POSITION

It was determined the gambling activity carried on off-site at the CO-2 by _____ is a nontraditional business activity. The selling of pull-tabs at a location separate from the facility where the social and recreational activities are carried out does not promote the social and recreational purposes of the club.

During the examination, the following were noted:

		<u>20XX</u>		<u>20XX</u>
CO-2 receipts	\$		\$	
(off-site)	\$		\$	
Total Gross Receipts		<u>34%</u>		<u>21%</u>
Percentage				

Since the sales from the CO-2 were unable to be traced to members, all sales will be treated as sales from non-members. As a result, the organization had a non-member percentage of 34% for 20XX and 21% for 20XX for off-site gambling. These percentages are more than the allowed 15% percentage from non-members.

Additionally, activities conducted by a social club need to further its exempt purposes. Traditional business activities are those activities that further a social club even if conducted solely on a membership basis. Activities that are not in furtherance of a social club's exempt purpose are referred to as nontraditional business activities. A social club is prohibited from conducting more than an insubstantial amount of nontraditional business activities. The prohibition against the conduct of nontraditional business activities applies equally to business with member and nonmembers.

During the examination, the following were noted:

Explanation of Items

Name of Taxpayer

ORG

| June 30, 20XX

Year/Period Ended

June 30, 20XX

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	<u>20XX</u>	<u>20XX</u>
CO-2 receipts (off-site)	\$	\$
On-site gambling - non-member	\$	\$
On-site bar, concessions, hall rentals - non-member	\$	\$
Total Gross Receipts from UBI	\$	\$
Total Gross Receipts Percentage	<u>48%</u>	<u>37%</u>

Thus, gambling activities are more than insubstantial and also the club consistently exceeds the permitted threshold of receiving up to 35 percent of their gross receipts, including investment income from sources outside of their memberships without losing their exempt status. Within this 35 percent amount, not more than 15 percent of the gross receipts should be derived from the use of a social club's facilities or services by the general public.

Thus, nontraditional business activities are more than insubstantial and also the club consistently exceeds the 15% of gross receipts from nonmember sources.

Additionally, the organization kept no contemporaneous records of nonmember use of its facility and activities.

ORG operated the bar. There were no contemporaneous records of these events were available.

Pull-tab sales and hall rentals were open to nonmembers as well as members and no records of nonmember income were kept.

Due to the substantial amount of nontraditional income and because the club consistently receives more than 35% of its gross receipts from sources outside the membership, no longer meets the requirements of IRC 501(c)(7). The taxpayer's exempt status should be revoked, effective July 1, 20XX.

As a taxable entity, the organization is required to file *Form 1120, U.S. Corporation Income Tax Return* for the periods open under statute. Under 6501(g) these periods include the years ending June 30, 20XX and June 30, 20XX.

Explanation of Items

Name of Taxpayer

ORG

| June 30, 20XX

Year/Period Ended

June 30, 20XX

LEGEND

ORG = Organization name

XX = Date

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The taxpayer's position is unknown. The taxpayer will be given 30 days to respond to the proposed change.

CONCLUSION

If you agree, an officer should sign and return the Form 6018-A to me along with Forms 1120 for the years ending June 30, 20XX and June 30, 20XX.

If you disagree, please let me know and we can arrange a meeting with the Group Manager.

Based upon the information noted above, it is proposed the exempt status of the organization be revoked as of the fiscal year ending June 30, 20XX. *Form 1120, U.S. Corporation Income Tax Return* should be obtained for the fiscal years June 30, 20XX to the present.

If the proposed revocation becomes final, appropriate State officials will be notified of such action in accordance with Internal Revenue Code of 6104(c).

The organization may re-apply for tax exemption under IRC 501(c)(7), as long as it can be determined their activities further their exempt purpose.

Please keep in mind Forms 1120 needs to be prepared so that they comply with IRC 277. I have attached a worksheet to demonstrate the allocation between member and nonmember income and deductions.

277(a) GENERAL RULE. —

In the case of a social club or other membership organization which is operated primarily to furnish services or goods to members and which is not exempt from taxation, deductions for the taxable year attributable to furnishing services, insurance, goods, or other items of value to members shall be allowed only to the extent of income derived during such year from members or transactions with members