

DEPARTMENT OF THE TREASURY

INTERNAL REVENUE SERVICE

TE/GE EO Examinations

1100 Commerce St.

Dallas, Texas 75242

501.07-00

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

March 12, 2010

Release Number: 201023063

Release Date: 6/11/10

LEGEND

ORG = Organization name XX = Date Address = address

**ORG
ADDRESS**

**Taxpayer Identification Number:
Form:
Tax Year(s) Ended:
Person to Contact/ID Number:
Contact Number:
Telephone:**

CERTIFIED MAIL – RETURN RECEIPT REQUESTED

Dear

In a determination letter dated November, 19XX, you were held to be exempt from Federal income tax under section 501(c)(7) of the Internal Revenue Code (the 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 01, 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 June 18, 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 1120, "US Corporation Income Tax Return", for the years ended June 30, 20XX and June 30, 20XX with us. 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 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,

Nanette M. Downing, Acting
Director, EO Examinations

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit 990, 990T
Name of Taxpayer ORG		Year/Period Ended 20XX06, 20XX06

LEGEND

ORG = Organization name XX = Date City = city State = state

ISSUE:

Whether the tax-exempt status of ORG should be revoked due to substantial non-member use of facility?

EXPLANATION OF FACTS

ORG ("Club" "Organization") was formed as a social club in City, State. They received exemption under IRC 501(c)(7) in November, 19XX. Analysis of the gross receipts generated by the organization for the two-year periods ending June 30, 20XX and June 30, 20XX has disclosed nonmember receipts to be at least 22% in 20XX06 and 18.77% in 20XX06. The nonmember receipts were received from sale of food, drinks and use of the organization's facilities for parties and events. In addition, the sales include reciprocal use of the club facilities by other clubs. The Form 990T reported part of the income received from non-members use of facility, but did not include non-member sales from other social clubs with which the organization have reciprocal arrangements.

The organization filed Form 990 and Form 990T for the period ending June 30, 20XX and June 30 20XX. We have examined the Form 990 for June 30, 20XX & 20XX and Form 990T for June 30, 20XX. Summary of examination findings and Form 990T returns are shown on the table below.

Non-Member Test	20XX06		20XX06	
	Per 990T	Per Exam	Per 990T	Per Exam
Total Gross Receipts				
Less Non-Traditional Income				
Less: Initiation fees				
Less: Unusual Income				
Adjusted gross receipts				
<u>Nonmember use of facilities:</u>				
Reciprocal club usage				
Nonmember parties				
Total Nonmember use of facilities				
Nonmember Use %	%	%	%	%
Limit		%		%
Result		Failed		Failed
Nonmember & Investment %		%		%

LAW

Internal Revenue Code (IRC) section 501(c)(7) exempts from Federal income tax: "Clubs organized for pleasure, recreation, and other non-profitable purposes, substantially all of the activities of which are for

such purposes and no part of the net earnings of which inures to the benefit of any private shareholder.”

Income Tax Regulation (ITR) 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 1971-1 C.B. 683 as amended by Public Law 94-568 sets forth guidelines for determining the effect of gross receipts derived from use of a social club’s facilities by the general public have on the club’s exemption under section 501(c)(7) of the Code. The revenue procedure states that where a club makes its facilities available to the general public to a substantial degree, the club is not operated exclusively for pleasure, recreation, or other non-profitable purposes. 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. If these standards are exceeded, a Social Club will not qualify for exemption pursuant to IRC section 501(c)(7).

The term “general public” as used in this procedure means persons other than members of a club, their dependents, or guests. “Total gross receipts” is defined as the receipts from normal and usual activities of the club including charges, admissions, membership fees, dues and assessments.

Revenue Ruling 66-149 provides that a social club is not exempt from Federal income tax as an organization described in section 501(c)(7) of the Code if it regularly derives a substantial part of its income from non-member sources.

Regulations Section 1.501(c)(7) -1(b) provides that a club which engages in business, such as making its social and recreational facilities available to the general public or by selling real estate, timber or other products, is not organized and operated exclusively for pleasure, recreation, and other non-profitable purposes, and is not exempt under section 501(a).

GOVERNMENT’S POSITION

As a result of our examination of your Form 990 return for periods ending June 30, 20XX and June 30 20XX we have determined that your organization no longer qualifies as an exempt social club described in Internal Revenue Code section 501(c)(7). Your non-member revenue consistently exceeds the percentage allowed by law. Your non-member income in 20XX06 and 20XX06 averaged 20% of total gross receipts, whereas Revenue Procedure 71-17 and Public Law 94-568 allow a maximum of 15%.

Because social clubs are primarily supported by their members’ payments, their tax exemption has the practical effect of allowing the membership to join together to provide themselves with recreational or social facilities without further tax consequences, when the club’s income is limited to membership receipts. This justification should not result in any tax advantage. By receiving such a large amount of nonmember income from the use of the facilities, the members do receive financial advantages.

CONCLUSION

Since the organization does not meet the requirements of 501(c)(7) because they received more than 15 percent of its income from non-members, the organization does not qualify for exemption under 501(c) (7). We propose a revocation of your exempt status under section 501(c)(7) effective July 01, 20XX. As a taxable entity, you are required to file Form 1120, U.S. Corporation Income Tax Return for the periods open under statute.

TAXPAYER’S POSITION

The organization agreed and signed Form 6018-A and also provided Form 1120 returns.