



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

Number: **201204020**
Release Date: 1/27/2012

Date: November 2, 2011

Contact Person:

Identification Number:

Contact Number:

Employer Identification Number:

Form Required To Be Filed:

Tax Years:

UIL: 501.03-05; 501.03-19; 501.33-00

Dear _____ :

This is our final determination that you do not qualify for exemption from Federal income tax as an organization described in Internal Revenue Code section 501(c)(3). Recently, we sent you a letter in response to your application that proposed an adverse determination. The letter explained the facts, law and rationale, and gave you 30 days to file a protest. Since we did not receive a protest within the requisite 30 days, the proposed adverse determination is now final.

Since you do not qualify for exemption as an organization described in Code section 501(c)(3), donors may not deduct contributions to you under Code section 170. You must file Federal income tax returns on the form and for the years listed above within 30 days of this letter, unless you request an extension of time to file.

We will make this letter and our proposed adverse determination letter available for public inspection under Code section 6110, after deleting certain identifying information. Please read the enclosed Notice 437, *Notice of Intention to Disclose*, and review the two attached letters that show our proposed deletions. If you disagree with our proposed deletions, you should follow the instructions in Notice 437. If you agree with our deletions, you do not need to take any further action.

In accordance with Code section 6104(c), we will notify the appropriate State officials of our determination by sending them a copy of this final letter and the proposed adverse letter. You should contact your State officials if you have any questions about how this determination may affect your State responsibilities and requirements.

Letter 4038 (CG) (11-2005)
Catalog Number 47632S

If you have any questions about this letter, please contact the person whose name and telephone number are shown in the heading of this letter. If you have any questions about your Federal income tax status and responsibilities, please contact IRS Customer Service at 1-800-829-1040 or the IRS Customer Service number for businesses, 1-800-829-4933. The IRS Customer Service number for people with hearing impairments is 1-800-829-4059.

Sincerely,

Lois Lerner
Director, Exempt Organizations

Enclosure
Notice 437
Redacted Proposed Adverse Determination Letter
Redacted Final Adverse Determination Letter



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Date: September 13, 2011

Contact Person:

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

LEGEND:

UIL:

501.03-05
501.03-19
501.33-00

L = Applicant
M = Subdivision
N = Specific blocks in subdivision
O = Organization
P = Village
Q = Date
V = Lake
W = State

Dear :

We have considered your application for recognition of exemption from federal income tax under section 501(a) of the Internal Revenue Code. Based on the information provided, we have concluded that you do not qualify for exemption under section 501(c)(3) of the Code. The basis for our conclusion is set forth below.

Issues

1. Do you meet the organizational test under section 501(c)(3) of the Code? No, for the reasons described below.
2. Do you meet the operational test under section 501(c)(3) of the Code? No, for the reasons described below.

Letter 4036 (CG) (11-2005)
Catalog Number 47630W

Facts

You, L, were incorporated under the laws of the State of W on Q. Your purpose as described in your amended Articles of Incorporation states in pertinent part "The specific purpose of this organization is to strengthen, improve and protect the unique character, livability, and social fabric of our neighborhood and to preserve its lake front history, natural beauty, diverse character and unique ambiance; to encourage more personal and social interaction between neighbors and among other community entities." Your bylaws also declare identical purposes.

You own beachfront land on V. The land provides space for the organization to hold events open to your community.

Your application, Form 1023, provides you will have activities that offer opportunities for those in the neighborhood who may be less social to participate, interact and get to know others in the community. Activities include block parties, boat parades, volleyball games and offering boat docks on the lake for rent.

Your block party is an annual event held in July that has various social games and activities for your community. You stated "Approximately 150 people from the neighborhood have the possibility to attend this party and to have some good time." You continued by saying, all residents within our neighborhood area benefit from the activity. You get permission from P to close the streets on the day of the event. Funding for the event comes from admission fees, membership fees, and donations. You indicated 50% of the organization's time and money are devoted to this event.

Your boat parade is held each July 4th. The organization participates in the parade by assisting another organization, O, with arranging for the entries and coordinating activities at the event. You state "The event is a parade of boats that are moored on V... Anyone with access to a boat can decorate as he sees fit and be a participant of the parade." You annually participate and enter an average of four boats per year with five individuals per boat. "Approximately 150 people attend from the immediate neighborhood and view the parade." "Signage is used throughout the neighborhood to promote the program". You indicated 10% of the organizations time and resources are used for this event.

You coordinate a volleyball activity for your members and community. Equipment, such as nets and balls are supplied by the club. Food and beverages are served at events. "Open invitation is extended to the entire neighborhood to play water volleyball at L on every Tuesday, starting Memorial Day Weekend through the end of September. On average, 5 to 10 families usually participate." Events are advertised through emails and signage. You indicated 30% of the organization's time and money are used for this activity.

Your other activities include quarterly member meetings, public relations to widen your support base, environmental cleaning and monitoring, instructions on boat safety and managing the beach property and related boat docks owned and operated by you on behalf of your members. You own a quarter mile portion of a square mile sized lake. The boat docks have been built on your land to accommodate mooring for members' boats. You indicated 10% of the organizations time is devoted to these activities.

Your bylaws state that maintaining and operating a bathing beach facility and activities related thereto are for private members use and that each member has one vote in issues before the club.

Seven board members are elected at an annual membership meeting for a five year term. None of these individuals are compensated. Advisory directors may be added in the future.

The organization receives revenue from admission fees from events and solicitations of members and the public at large.

Members were defined in your initial bylaws as owners, their heirs, executors of assigns of lots in M and N in P, W. You amended your bylaws to state membership is open to all with the appropriate application and approval by the board of directors of the organization. Article 5, Section 1, of your amended by-laws states "Application for voting membership shall be open to all. Membership is granted after completion and receipt of a membership application. All memberships shall be granted upon a majority vote of the Board of Directors".

Advertising for events is done throughout your community with temporary signs placed beside the road. Pictures of signs beside the road were provided for examples of how residents are informed of meetings and events. Also meeting minutes and emails are distributed to residents and members.

Law

Section 501(c)(3) of the Code provides for the exemption from federal income tax of corporations organized and operated exclusively for charitable or educational purposes, provided no part of the net earnings inures to the benefit of any private shareholder or individual.

Section 1.501(c)(3)-1(a)(1) of the Income Tax Regulations provides that in order to be exempt as an organization described in section 501(c)(3) of the Code, an organization must be both organized and operated exclusively for one or more purposes specified in such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt.

Section 1.501(c)(3)-1(b)(1)(i) of the Income Tax Regulations provides that in order to meet the organizational test an organization must be organized exclusively for one or more exempt purposes.

Section 1.501(c)(3)-1(c)(1) of the Income Tax Regulations provides that an organization operates exclusively for exempt purposes if it engages primarily in activities that accomplish exempt purposes specified in section 501(c)(3) of the Code. An organization must not engage in substantial activities that fail to further an exempt purpose.

Section 1.501(c)(3)-1(d)(1)(ii) of the Income Tax Regulations provides that an organization is not organized and operated exclusively for exempt purposes unless it serves a public rather than a private interest. Thus, to meet this requirement it is necessary for an organization to establish that it is not organized and operated for the benefit of private interests.

Revenue Ruling 59-310 granted exemption under section 501(c)(3) to an organization that was formed to establish, maintain and operate a public swimming pool, playground and other recreation facilities for the children and other residents of the community. Its funds were principally raised by public subscription. The income derived from charges for admission to the swimming pool was nominal and such charges were purely incidental to the orderly operation of the pool. Since the property and its uses are dedicated to members of the general public of the community and are charitable in that they serve a generally recognized public purpose which tends to lessen the burdens of government, it is concluded that the instant organization is exclusively charitable within the meaning of section 501(c)(3) of the Code.

Revenue Ruling 68-224 granted exemption under section 501(c)(4), not 501(c)(3) to an organization of which their primary purpose was to conduct an annual festival that depicts regional customs and traditions. In a typical year, it features a banquet or barbecue, a parade, various contests, and a rodeo. At the banquet or barbecue the winners of the various contests are announced. The parade is made up of school bands, local riding clubs, and floats built by local organizations. Contests relate to dress and costumes concerning the traditions of the area. Floats generally depict the community history and customs. The festival is climaxed on the final day with the rodeo. The ruling stated, "In carrying on the activities described, the organization provides recreation for the community, publicizes the community and attracts persons to it, promotes community growth, and provides a means whereby citizens may express their interest in local history, customs, and traditions. These activities promote the common good and general welfare of the people of the community and bring about civic betterments and social improvements. Accordingly, the organization qualifies for exemption from Federal income tax under section 501(c)(4) of the Code.

Revenue Ruling 70-186 discusses an organization that improved and sustained a lake used for public purposes. The organization improved the condition of the water in the lake to enhance its recreational features for public benefit. The organization's principal activity was to treat the water, to remove algae, and to otherwise improve the condition of the water for recreational purposes for the public. The organization was found to be exempt under section 501(c)(3) of the Code.

In Better Business Bureau of Washington, D.C., Inc. v. United States, 326 U.S. 279, the Supreme Court held that the presence of a single non-exempt purpose, if substantial in nature, will destroy a claim for exemption regardless of the number or importance of truly exempt purposes.

Old Dominion Box Co. v. United States, 477 F. 2d 340 (4th Cir. 1973), cert. denied 413 U.S. 910 (1973). held that operating for the benefit of private parties constitutes a substantial nonexempt purpose.

Application of Law

You are not described under section 501(c)(3) of the Code or Section 1.501(c)(3)-1(a)(1) of the Income Tax Regulations because you do not meet the organizational or operational tests.

To demonstrate that it is organized exclusively for exempt purposes, thus satisfying the organizational test, an organization must have a valid purpose clause (section 1.501(c)(3)-1(b)(1)(i) of the regulations). Your amended Articles of Incorporation states that your specific purpose is "to strengthen, improve and protect the unique character, livability, and social fabric of (your) neighborhood and preserve its lake front history, natural beauty, diverse character and unique ambiance; to encourage more personal and social interaction between neighbors and among other community entities." These purposes, specifically encouraging personal and social interaction between neighbors, is not an exempt purpose describe under section 501(c)(3) of the Code or corresponding regulations. Therefore, you do not meet the organizational test.

You also do not meet the operational test. You indicated 90% of your time is for social and recreational events held for members and neighborhood residents. Social and recreational events are not considered exempt activities under section 1.501(c)(3)-1(c)(1) of the regulations. Furthermore, a substantial portion of your activities serves the private interests of your members, and not the public as a whole. Your beach is advertised and promoted as a private beach. Boat docks are provided by the organization for use only to benefit members mooring their personal boats. These activities do not benefit the public and are not sufficient to meet the requirements of section 1.501(c)(3)-1(c)(1) and 1.501(c)(3)-1(d)(1)(ii) of the Regulations.

Your activity is not like that described in Revenue Ruling 59-310 where a public pool and other recreational facilities were operated by an exempt organization. Swimming was offered to the public at large including all local residents without discrimination. Most of the individuals using the pool were low income and therefore could not afford the cost of privately sponsored recreational facilities. You are distinguished from this ruling because you are not simply maintaining a recreational facility for the general public in a manner that lessens the burdens of the government. Unlike the organization described in the ruling, you are actively involved in the conduct of social and recreational activities such as volleyball tournaments with the purpose of encouraging social interaction between neighbors. Social events are not considered charitable or educational purposes under section 501(c)(3) of the Code.

You are similar to the organization described in Revenue Ruling 68-224 that received exemption under section 501(c)(4), and not 501(c)(3). Like the organization in this ruling you conduct block parties, annual festivals, and a boat parade. As stated in the revenue ruling, these activities "provide recreation for the community, publicize the community and attracts persons to it, promotes community growth, and provides a means whereby citizens may express their interest in local history, customs, and traditions. These activities promote the common good and general welfare of the people of the community and bring about civic betterments and social improvements." These activities are not exclusively charitable or educational as defined in section 501(c)(3) of the Code.

You are not like the organization described in Revenue Ruling 70-186. The organization discussed in that ruling improved and maintained the lake, by improving the water quality for use by the public. Unlike that organization, a substantial portion of your activities is dedicated to conducting social and recreational activities, and not simply improving a lake for public use.

Private benefit has both qualitative and quantitative connotations. In the qualitative sense, to be incidental, the private benefit must be a necessary concomitant of the activity that benefits the activity at large, i.e., the benefit to the public cannot be achieved without necessarily benefiting private individuals. Revenue Ruling 70-186 above found that it would be impossible to accomplish the organization's charitable purposes of cleaning and maintaining a lake without providing benefit to certain property owners. You indicated that you will maintain beach property/boat docks and arrange social and recreational activities for the use of your members, which are not necessary to carry out your exempt activities. In quantitative sense, to be incidental, the private interests must not be substantial in the context of the overall public benefit conferred by the activity. In your case, you spend 40% of time and resources on managing your boat docks/beach property and arranging social and recreational activities for members which offer a direct benefit to your members.

Your operations are similar to those described in the court case Old Dominion Box Co. v

United States, 477 F2d 344 (4th Cir. 1973) cert. denied 413 U.S. 910 (1973) in that a substantial portion of your activities are for private interests. This is substantiated by the fact that your beach and dock are private and the lake "is private in terms of boat access". You further indicated "our beach is not advertised as a public beach, nor do we have the authority to open it up as one". The W Parks and Recreation website indicates the lake is a private lake. As such, a substantial portion of your activities benefits private interests, which is a substantial non-exempt purpose.

Like the organization in Better Business Bureau v. United States, 326 U.S. 278 (1945), you have a substantial non-exempt purpose. The fact that 90% of your activities are social and recreational precludes exemption under 501(c)(3). Even if some of your activities and purposes are described in section 501(c)(3), a single non-exempt purpose, if substantial in nature, will destroy a claim for exemption regardless of the number or importance of truly exempt purposes.

Applicant's Position

You cited Revenue Ruling 70-186 as an organization that was operating in a similar manner to you. You stated recreational activities are primarily to help drive volunteers to conduct the environmental cleaning, monitoring and safety and health fitness training. You also stated you are similar to Revenue Ruling 59-310 because you offer swimming to the community.

Service's Response to Applicant's Position

As described above, your activities substantially differ from both of these rulings. Based on your stated purpose and the activities you conduct, it is obvious you have a substantial purpose of providing social and recreational activities for your members and members of the community. Even if you have some activities that are similar to the organizations in these rulings, the overall facts and circumstances involved show you have a substantial non-exempt purpose of conducting social and recreational activities.

Conclusion

Based on the facts and information submitted, you are not organized and operated exclusively for exempt purposes. You do not meet the organizational test because your organizing document does not properly limit your purposes to those described in section 501(c)(3). Likewise, you do not meet the operational test because you conduct substantial social and recreational activities and you have not established that your activities do not substantially benefit private interests.

Accordingly, you do not qualify for exemption under section 501(c)(3) of the Code and you must file federal income tax returns. Contributions to you are not deductible under section 170 of the Code.

We have not considered whether you qualify for exemption under section 501(c)(4) of the Code. We asked if you would like to apply for exemption under this section instead, but you declined to do so.

You have the right to file a protest if you believe this determination is incorrect. To protest, you must submit a statement of your views and fully explain your reasoning. You must submit the statement, signed by one of your officers, within 30 days from the date of this letter. We will consider your statement and decide if the information affects our determination. If your statement does not provide a basis to reconsider our determination, we will forward your case to our Appeals Office. You can find more information about the role of the Appeals Office in Publication 892, *Exempt Organization Appeal Procedures for Unagreed Issues*.

Types of information that should be included in your appeal can be found on page 2 of Publication 892, these items include:

1. The organization's name, address, and employer identification number;
2. A statement that the organization wants to appeal the determination;
3. The date and symbols on the determination letter;
4. A statement of facts supporting the organization's position in any contested factual issue;
5. A statement outlining the law or other authority the organization is relying on; and
6. A statement as to whether a hearing is desired.

The statement of facts (item 4) must be declared true under penalties of perjury. This may be done by adding to the appeal the following signed declaration:

"Under penalties of perjury, I declare that I have examined the statement of facts presented in this appeal and in any accompanying schedules and statements and, to the best of my knowledge and belief, they are true, correct, and complete."

Your appeal will be considered incomplete without this statement.

If an organization's representative submits the appeal, a substitute declaration must be included stating that the representative prepared the appeal and accompanying documents; and whether the representative knows personally that the statements of facts contained in the appeal and accompanying documents are true and correct.

An attorney, certified public accountant, or an individual enrolled to practice before the Internal Revenue Service may represent you during the appeal process. If you want representation during the appeal process, you must file a proper power of attorney, Form 2848, *Power of Attorney and Declaration of Representative*, if you have not already done so. You can find more information about representation in Publication

947, *Practice Before the IRS and Power of Attorney*. All forms and publications mentioned in this letter can be found at www.irs.gov, Forms and Publications.

If you do not file a protest within 30 days, you will not be able to file a suit for declaratory judgment in court because the Internal Revenue Service (IRS) will consider the failure to appeal as a failure to exhaust available administrative remedies. Code section 7428(b)(2) provides, in part, that a declaratory judgment or decree shall not be issued in any proceeding unless the Tax Court, the United States Court of Federal Claims, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted all of the administrative remedies available to it within the IRS.

If you do not intend to protest this determination, you do not need to take any further action. If we do not hear from you within 30 days, we will issue a final adverse determination letter. That letter will provide information about filing tax returns and other matters.

Please send your protest statement, Form 2848, and any supporting documents to the applicable address:

Mail to:

Internal Revenue Service
EOD Quality Assurance
P.O. Box 2508 Room 7-008
Cincinnati, OH 45201

Deliver to:

Internal Revenue Service
EOD Quality Assurance
550 Main Street, Room 7-008
Cincinnati, OH 45202

You may fax your statement using the fax number shown in the heading of this letter. If you fax your statement, please call the person identified in the heading of this letter to confirm that he or she received your fax.

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

Sincerely,

Lois G. Lerner
Director, Exempt Organizations

Enclosure, Publication 892