

DEPARTMENT OF THE TREASURY

Internal Revenue Service
TEGE EO Examinations



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Date: May 20, 2009

Number: **201344010**

Release Date: 11/1/2013

UIL: 501.07-01

**Taxpayer Identification
Person to Contact:**

Legend:

ORG = Name of Organization

Address = Address of Organization

Year = xx

Telephone Number:

FAX Number:

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 October 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 February 17, 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, for the year[s] ended September 30, 20xx, 20xx & 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, 1-877-777-4778, and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

Taxpayer Advocate Service

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

Sincerely,

Sunita B. Lough
Director, EO Examinations



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
Internal Revenue Service

January 20, 2009

LEGEND:

ORG = Name of Organization
Address = Address of Organization
Year = xx

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,

Renee B. Wells
Acting Director, EO Examinations

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

Form 886-A	EXPLANATION OF ITEMS	Schedule No.
Name of Taxpayer ORG		Years/Period Ended

+

LEGEND:

ORG = Name of Organization

YEAR = xx

ISSUE:

Does the ORG continue to meet the qualifications of an organization described in Internal Revenue Code Section 501(c)(7)?

FACTS:

ORG received exemption as an organization described in IRC 501(c)(7) in 19xx. The records available for the organization for the periods ending September 30, 20xx and 20xx were examined. It was found that the club is not in compliance with Rev. Proc. 71-17. Nonmember events are carried on throughout the year. The organization receives nonmember revenue for use of its golf course, golf cart rental, pool and tennis court and from food and beverage sales to nonmembers. The exempt organization failed to file form 990T to report their nonmember income

Inspection of the returns filed by the Club for the prior years shows that the organization has not reported their nonmember income in excess of 15% on form 990T since 20xx.

Based on the amounts reported on the organizations income statement for tax year ending September 30, 20xx, the percent of gross receipts estimated from nonmember use of facilities exceeds the allowed 15%. Information regarding nonmember portion of proceeds for tax year ending September 30, 20xx was solicited but not provided.

Form 886-A	EXPLANATION OF ITEMS	Schedule No.
Name of Taxpayer ORG		Years/Period Ended

LAW AND DISCUSSION:

IRC Section 501(c) 7 states:

Internal Revenue Code section 501(c)(7) provides for the exemption from Federal income taxes for Social Clubs with these specifying attributes for exemption "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." "IRC 501(c) (7)

Treasury Regulation Section 1.501(c)7-1:

a) The exemption provided by section 501(a) for organizations described in section 501(c)(7) applies only to clubs which are organized and operated exclusively for pleasure, recreation, and other non profitable purposes, but does not apply to any club if any part of its net earnings inures to the benefit of any private shareholder. In general, this exemption extends to social and recreation clubs which are supported solely by membership fees, dues, and assessments. However, a club otherwise entitled to exemption will not be disqualified because it raises revenue from members through the use of club facilities or in connection with club activities.

(b) 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). Solicitation by advertisement or otherwise for public patronage of its facilities is prima facie evidence that the club is engaging in business and is not being operated exclusively for pleasure, recreation, or social purposes. However, an incidental sale of property will not deprive a club of its exemption.

Revenue Ruling 58-589, 1958-2 C.B. 266,

provides that operational costs covered by nonmember patronage, would be an indicator of inurement, provided the club's assets are distributable to club members upon dissolution. The effect of this Ruling is that a club can overall experience a loss in any

Form 886-A	EXPLANATION OF ITEMS	Schedule No.
Name of Taxpayer ORG		Years/Period Ended

given business year, but inurement can take the form of any excess of nonmember receipts over direct costs, covering expenses that the members of the club would have to bare if it were not for the income provided by nonmember patronage.

Revenue Ruling 1960-324, 1960-2 C.B. 173,

weighed the following factors in its findings that a club that makes its facilities available to the general public on a regular, recurring, basis should no longer be recognized under IRC Section 501(c)(7): percentage of nonmember gross receipts (ranged from 12-17% in this case), gross profit from the unrelated activities, net profit overall and the number of outside (unrelated) functions compared to total functions of the club. It was also indicated that internal analysis of the club showed that if these outside activities were discontinued, a substantial increase in the amount of annual dues from club members would be necessary.

Revenue Procedure 1971-17, 1971-1, CB 683,

sets forth the guidelines for determining the gross receipts from the use of a social club's facilities by the general public. The Revenue Procedure also provides that in situations 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. The definition of items includable in the gross receipts tests is established in this Revenue Procedure. Also contained in this Revenue Procedure are the rules under which the host-guest relationship will be established.

U.S. Court of Appeals:

Pittsburgh Press Club v. USA, 536 F.2d 572, (1976).

Case stated there are factors to be considered when considering the effects of a social club's nonmember receipts, including the percentage of gross receipts from nonmembers, profit from non-member receipts, the purpose for which a social club's facilities are made available to nonmember groups, and the frequency of use of club facilities made by nonmembers.

Public Law -PL 94-568(October 20, 1976):

This Public Law defines limitations of nonmember gross receipts as 15% of total gross receipts.

Form 886-A	EXPLANATION OF ITEMS	Schedule No.
Name of Taxpayer ORG		Years/Period Ended

The following are important facts and circumstances to take into account to determine whether a club may maintain its exemption under IRC 501(c)(7):

- Frequency of use of the club facilities or services by nonmembers. An unusual or single event (that is, nonrecurring on a year to year basis) that generates all the nonmember income is viewed more favorably than nonmember income arising from frequent use by nonmembers.
- Record of nonmember use over a period of years. A high percentage in one year by nonmembers, with the other years being within permitted levels, is viewed more favorably than a consistent pattern of exceeding the limits, even by relatively small amounts. (See S. Rept. 94-1318, 2d Sess., 1976-2 C.B. 597,599).
- Purposes for which the club's facilities were made available to nonmembers.
- Whether the nonmember income generates net profits for the organization.

TAXPAYER'S POSITION:

The taxpayer has indicated that they are in agreement with this decision. However, I do not have a signed form 6018.

GOVERNMENT'S POSITION:

Social Clubs are required to follow Revenue Procedure 1971-17. This Procedure provides guidelines Social Clubs should follow when they engage in business with non-members. One of the requirements that this Procedure mandates is that Social Clubs document their levels of non-member income in various situations. Social Club did not follow this required Procedure which is why the analysis had to be performed based on organization's own partial estimation. It is unclear whether or not the organization has the records available to provide an estimation of non-member receipts.

Form 886-A	EXPLANATION OF ITEMS	Schedule No.
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The 15% limitation is, however a threshold. The facts and circumstances are also required to be examined when reviewing the exempt status of an organization exempt under IRC Section 501(c)(7).

In the terms of the facts and circumstances tests described in Revenue Rulings 1960-324 and Pittsburgh Press Club v. USA, the organization exceeding the gross receipts tests by either percentage is unfavorable. In Revenue Ruling 1960-324, the club in that case only exceeded the percentage by two percent at the most (12-17% of nonmember income over several years). The Social Club described in Revenue Ruling 1960-324 had their exemption revoked.

Based on the data that has been provided the green fees and cart rentals are an on-going activities and the organization has been operating without deficit for the years in question. The analysis shows that the Gross Receipts from non-members subsidizes the club, and has helped the organization cover expenditures that the members would have to bear alone.

Overall neither the facts and circumstances nor the Gross Receipts Test fall to the benefit of the Social Club. The primary factor is the Gross Receipts Test. The percentage, coupled with the fact that there are other areas that would make this percentage higher, is far outside the range that was intended for even the facts and circumstances to come into play.

ORG has exceeded 15% the permissible levels of non-member income to a substantial degree on a continuous basis. The nonmember receipts are earned throughout the year. There was no one single or unusual event that caused the club to exceed the 15% threshold.

Social Clubs receiving more then 15% of their receipts, per PL 94-568 and Revenue Procedure 1971-17, from nonmember usage of facilities are not operating in an exempt fashion per the rules and regulations governing organizations exempt under IRC Section 501(c)(7), with limited exceptions. No precedent was noted that discussed facts and circumstances of a Social Club's continued exemption, where nonmember patronage was not within a few percentage points of 15%. It has thus been determined that the organization has not met the requirements for continued exemption

EXPLANATION OF ITEMSName of Taxpayer
ORG

Years/Period Ended

as a 501(c) (7) organization. These rules are provided to Social Clubs when they received their exemption, as evidenced by the Social Club's determination letter which was issued to them.

Revocation of its tax-exempt status is warranted, effective October 1, 20xx.

As a taxable entity, the organization is required to file Form 1120, U.S. Corporation Income Tax Return the tax periods ending on or after September 30, 20xx and all subsequent years.

Additionally, the organization is reminded of the provisions of IRC 277 concerning membership organizations which are not exempt organizations.