



DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
1100 Commerce Street, MC 4920DAL  
Dallas, TX 75242

TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

UIL: 501.07-00

Number: 202110023  
Release Date: 3/12/2021

Date: 09/17/20

Taxpayer ID Number:

Form

For Tax Period(s) Ending:

Person to Contact:

Identification Number:

Telephone Number:

**CERTIFIED MAIL – Return Receipt Requested**  
**LAST DAY FOR FILING A PETITION WITH THE TAX COURT:**

Dear :

This is a final determination that you do not qualify for exemption from federal income tax under Internal Revenue Code (IRC) Section 501(a) as an organization described in IRC Section 501(c)(7) for the tax period(s) above.

Our adverse determination as to your exempt status was made for the following reasons:

You have not established that you are operated substantially for pleasure and recreation of its members or other non-profitable purposes and no part of the earnings inures to the benefit of private shareholder within the meaning of IRC Section 501(c)(7). You have made your recreational and social facilities available to the general public. You have exceeded the non-member income test for tax year ending August 31, 20XX.

Organizations that are not exempt under IRC Section 501 generally are required to file federal income tax returns and pay tax, where applicable. For further instructions, forms, and information please visit [www.irs.gov](http://www.irs.gov).

If you decide to contest this determination, you may file an action for declaratory judgment under the provisions of IRC Section 7428 in one of the following three venues: 1) United States Tax Court, 2) the United States Court of Federal Claims, or 3) the United States District Court for the

District of Columbia. A petition or complaint in one of these three courts must be filed within 90 days from the date this determination was mailed to you. Please contact the clerk of the appropriate court for rules and the appropriate forms for filing petitions for declaratory judgment by referring to the enclosed Publication 892. You may write to the courts at the following addresses:

United States Tax Court  
400 Second Street, NW  
Washington, DC 20217

U.S. Court of Federal Claims  
717 Madison Place, NW  
Washington, DC 20005

U. S. District Court for the District of  
Columbia 333 Constitution Ave., N.W.  
Washington, DC 20001

Processing of income tax returns and assessments of any taxes due will not be delayed if you file a petition for declaratory judgment under IRC Section 7428.

You may be eligible for help from the Taxpayer Advocate Service (TAS). TAS is an independent organization within the IRS that can help protect your taxpayer rights. TAS can offer you help if your tax problem is causing a hardship, or you've tried but haven't been able to resolve your problem with the IRS. If you qualify for TAS assistance, which is always free, TAS will do everything possible to help you. Visit [www.taxpayeradvocate.irs.gov](http://www.taxpayeradvocate.irs.gov) or call 1-877-777-4778.

Taxpayer Advocate assistance can't be used as substitute for established IRS procedures, formal appeals processes, etc. The Taxpayer Advocate is not able to reverse legal or technically correct tax determination, nor extend the time fixed by law that you have to file a petition in 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 can get any of the forms or publications mentioned in this letter by calling 800-TAX-FORM (800-829-3676) or visiting our website at [www.irs.gov/forms-pubs](http://www.irs.gov/forms-pubs).

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.

Sincerely,

Sean E. O'Reilly  
Director, Exempt Organizations Examinations

Enclosures:  
Publication 892



Department of the Treasury  
Internal Revenue Service  
Tax Exempt and Government Entities  
Exempt Organizations Examinations

Date:  
11/19/2019  
Taxpayer Identification Number:  
  
Form:  
  
Tax Year(s) Ended:  
  
Person to Contact:  
  
Employee ID:  
Telephone:  
Fax:  
Manager's Contact Information:  
  
Telephone:  
Response Due Date:

**CERTIFIED MAIL – Return Receipt Requested**

Dear \_\_\_\_\_ :

**Why you're receiving this letter**

We enclosed a copy of our audit report, Form 886-A, Explanation of Items, explaining that we propose to revoke your tax-exempt status as an organization described in Internal Revenue Code (IRC) Section 501(c)(7).

**If you agree**

If you haven't already, please sign the enclosed Form 6018, Consent to Proposed Action, and return it to the contact person shown at the top of this letter. We'll issue a final adverse letter determining that you aren't an organization described in IRC Section 501(c)(7) for the periods above.

After we issue the final adverse determination letter, we'll announce that your organization is no longer eligible to receive tax deductible contributions under IRC Section 170.

**If you disagree**

1. Request a meeting or telephone conference with the manager shown at the top of this letter.
2. Send any information you want us to consider.
3. File a protest with the IRS Appeals Office. If you request a meeting with the manager or send additional information as stated in 1 and 2, above, you'll still be able to file a protest with IRS Appeals Office after the meeting or after we consider the information.

The IRS Appeals Office is independent of the Exempt Organizations division and resolves most disputes informally. If you file a protest, the auditing agent may ask you to sign a consent to extend the period of limitations for assessing tax. This is to allow the

IRS Appeals Office enough time to consider your case. For your protest to be valid, it must contain certain specific information, including a statement of the facts, applicable law, and arguments in support of your position. For specific information needed for a valid protest, refer to Publication 892, How to Appeal an IRS Determination on Tax-Exempt Status.

Fast Track Mediation (FTM) referred to in Publication 3498, The Examination Process, generally doesn't apply now that we've issued this letter.

4. Request technical advice from the Office of Associate Chief Counsel (Tax Exempt Government Entities) if you feel the issue hasn't been addressed in published precedent or has been treated inconsistently by the IRS.

If you're considering requesting technical advice, contact the person shown at the top of this letter. If you disagree with the technical advice decision, you will be able to appeal to the IRS Appeals Office, as explained above. A decision made in a technical advice memorandum, however, generally is final and binding on Appeals.

**If we don't hear from you**

If you don't respond to this proposal within 30 calendar days from the date of this letter, we'll issue a final adverse determination letter.

**Contacting the Taxpayer Advocate Office is a taxpayer right**

The Taxpayer Advocate Service (TAS) is an independent organization within the IRS that can help protect your taxpayer rights. TAS can offer you help if your tax problem is causing a hardship, or you've tried but haven't been able to resolve your problem with the IRS. If you qualify for TAS assistance, which is always free, TAS will do everything possible to help you. Visit [www.taxpayeradvocate.irs.gov](http://www.taxpayeradvocate.irs.gov) or call 877-777-4778.

**For additional information**

You can get any of the forms and publications mentioned in this letter by visiting our website at [www.irs.gov/forms-pubs](http://www.irs.gov/forms-pubs) or by calling 800-TAX-FORM (800-829-3676).

If you have questions, you can contact the person shown at the top of this letter.

Sincerely,



Joseph Colletti for Maria Hooke  
Director, Exempt Organizations  
Examinations

Enclosures:  
Form 886-A  
Form 6018

Form <b>886-A</b> (Rev. January 1994)	<b>EXPLANATIONS OF ITEMS</b>	Schedule number or exhibit
Name of taxpayer	Tax Identification Number	Year/Period ended 20XX

**Issue(s):**

- 1) Should \_\_\_\_\_ (hereafter "EO") continue to qualify as an organization described in Section 501(c)(7) of the Internal Revenue Code?

**Facts:**

EO was exempt from income tax under Internal Revenue Code Section 501(c)(7), effective date of exemption is July 23, 19XX.

In their Articles of Association, EO was formed for the "purpose of operating a club and social or lodge for the general good of the members by promoting literary, social and educational advantages in the culture, as well as English, and to promote an educational program for the purpose of interesting and assisting \_\_\_\_\_ people or people of \_\_\_\_\_. The Articles further state EO shall have social events and other activities for the purpose of assisting or enabling the carrying out of the purposes aforementioned.

According to the President, \_\_\_\_\_, anyone can join the club during the year of audit and they don't have to be of \_\_\_\_\_ descend.

EO has a member's area for all the member activities, a hall with 0 round tables, and another hall that is substantially large compare to the club's total space. Both halls are open to the public during bingo and dinner events.

EO operated gaming throughout the year under audit. EO conducted bingo on a weekly basis, and they sold pull tabs tickets (progressive bingo) during the bingo nights. The organization advertised Bingo to the public, on EO's website, in local newspaper, and on their club's sign visible from the street. The agent confirmed, with the organization, that the public can play Bingo with the only restriction of access to the member's area.

EO also operated many dinner events for the year under audit, and is evident that dinner nights are currently ongoing through their website. Similar to the bingo nights, these events were open to the public with the same restriction. *Please see EXHIBIT A for reference to these events, according on EO's website.*

The organization leased a portion of land to a for profit company. The for profit entity used land and installed solar panels to generate electricity. The contract, reviewed, stated that the lease's term is 0 years with option to extend. According to the organization's General Ledger, Account 0 – reported a total of \$0 for the year under audit.

EO had a lot of events open to the public, including rental income and investment income. These activities were active in the audit year, as well as in 20XX thru 20XX, according to the Form 990-T filed. EO acknowledged these types of income constituted unrelated business income, and filed Form 990-T to report these income. The following table depicts the total unrelated business gross receipts for the reported year, according to the Form 990-T filed. Additionally, the table shows the total revenue reported on Form 990 for the respective year, the percentage of non member gross receipts to the total gross receipts, and the percentage of investment income to total gross receipts.

Form <b>886-A</b> (Rev. January 1994)	<b>EXPLANATIONS OF ITEMS</b>	Schedule number or exhibit
Name of taxpayer	Tax Identification Number	Year/Period ended 20XX

EO reported bingo income of \$0 in their books and records for the year under audit. Bingo is advertised on the newspaper, street signs, and is open to the public. Agent audited bingo income and the determined reported amount is not correct. Agent aggregated the revenues reported on the Bingo reports (filed to the State of ) to determine the accuracy of the income reported on the P&L. Audit procedures conclude that this bingo income is reported as net, not gross. The total gross revenue for Bingo sales is \$0 as audited.

Data taken from Form 990 and Form 990-T filed:

Income Reported on Form 990 and Form 990-T					
Tax Period					
PERCENTAGE NON MEMBER INCOME					
	8/31/20XX	8/31/20XX	8/31/20XX	8/31/20XX	8/31/20XX
Gross Receipts Reported Form 990-T	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Total Gross Receipts Reported on Form 990	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
% Unrelated Business Income/ Total Gross Receipts	0%	0%	0%	0%	0%
PERCENTAGE OF INVESTMENT INCOME					
	8/31/20XX	8/31/20XX	8/31/20XX	8/31/20XX	8/31/20XX
Investment Income Reported for the Year	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
% of Investment Income / Total Gross Receipts	0%	0%	0%	0%	0%

Please reference EXHIBIT B for copies of Form 990 and Form 990-T filed, except for Form 990 with period ending 20XX. RA used the Service's record to compute the total gross receipts for 20XX. This table is unadjusted for the audited bingo income. With the inclusion of the audited bingo income that was open for the public, the percentage of unrelated business income / total receipts for 20XX tax period would be 0%.

**Laws:**

Internal Revenue Code § 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 not part of the net earnings of which inures to the benefit of any private shareholder."

Section 1.501(c)(7) of the Income Tax Regulations provides that, in general, the exemption extends to social and recreation clubs supported solely by membership fees, dues and assessments. However, a club that engages in a business, such as making its social and recreational facilities open to the general public, is not organized and operated exclusively for pleasure, recreation and other non-profitable purposes, and is not exempt under section 501(a).

Prior to its amendment in 1976, IRC § 501(c)(7) required that social clubs be operated exclusively for pleasure, recreation and other non-profitable purposes. Public Law 94-568 amended the "exclusive" provision to read "substantially" in order to allow an IRC § 501(c)(7) organization to receive up to 35 percent of its gross receipts, including investment income, from sources outside its membership without losing its tax exempt status.

Form <b>886-A</b> (Rev. January 1994)	<b>EXPLANATIONS OF ITEMS</b>	Schedule number or exhibit
Name of taxpayer	Tax Identification Number	Year/Period ended 20XX

The Committee Reports for Public Law 94-568 (Senate Report No. 94-1318 2d Session, 1976-2 C.B. 597) further states:

(a) Within the 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 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.

(b) Thus, a social club may receive investment income up to the full 35 percent of its gross receipts if no income is derived from non-members' use of club facilities.

(c) In addition, the Committee Report states that where a club receives unusual amounts of income, such as from the sale of its clubhouse or similar facilities, that income is not to be included in the 35 percent formula.

Revenue Ruling 66-149 holds a social club as not exempt as an organization described in Internal Revenue Code § 501(c)(7) where it derives a substantial part of its income from non-member sources.

Revenue Procedure 71-17 sets forth the guidelines for determining the effect of gross receipts derived from the general public's use of a social club's facilities on exemption under Internal Revenue Code § 501(c)(7). Where nonmember income from the usage exceeds the standard as outlined in this Revenue procedure, the conclusion reached is that there is a non-exempt purpose and operating in this manner jeopardizes the organization's exempt status

Internal Revenue Code Section 512(a)(3)(B) states that for purposes of subparagraph (A), the term "exempt function income" means the gross income from dues, fees, charges, or similar amounts paid by members of the organization as consideration for providing such members or their dependents or guests goods, facilities, or services in furtherance of the purposes constituting the basis for the exemption of the organization to which such income is paid. Such term also means all income (other than an amount equal to the gross income derived from any unrelated trade or business regularly carried on by such organization computed as if the organization were subject to paragraph (1)), which is set aside for a purpose specified in section 170(c)(4).

**Government's Position:**

Based on the examination, the organization does not qualify for exemption as a social club described in IRC § 501 (c)(7) and Treas. Reg. § 1.501 (c)(7) which provides that in general, this exemption extends to social and recreation clubs which are supported solely by membership fees, dues, and assessments.

Revenue Ruling 66-149 and 60-324 support this position stating that a social club that opens to the public and derives a substantial part of its income from non-member sources is not exempt as an organization described in 501(c)(7).

The organization permits use of its facilities and attendance at its events by the general public. Records show that it had exceeded the 35% investment & non-member income as well as 15% non-member income threshold as outlined in Public Law 94-568, on a recurring basis for the previous 0 years.

Form <b>886-A</b> (Rev. January 1994)	<b>EXPLANATIONS OF ITEMS</b>	Schedule number or exhibit
Name of taxpayer	Tax Identification Number	Year/Period ended <b>20XX</b>

EO provided documentation to claim that their nonmember income is only 0%, opposed to the 0% reported on their 990-T, as originally filed. The responses received on June 28, 20XX and subsequently on August 12, 20XX support their 0% nonmember allocation. However, this number is unaccounted for the actual bingo income. Furthermore, the 0% is still over the allowed 15% nonmember receipt requirement for 501(c)(7) organization. In addition to that, the records provided, just circles on the weekly cash out sheet to determine non member function do not conform with the requirement set forth by the IRS – spelled out in Revenue Ruling 71-17. Even if the IRS accepts this substantiation, the organization is well over its allowed non member income limit. Because of that, RA did not address the legitimacy of the records produced by the organization.

Accordingly, it is proposed that the organization's tax-exempt status be revoked effective September 1, 20XX.

**Taxpayer's Position:**

On June 28, 20XX, Agent received a 0 pages fax response from EO's representative. EO claimed they kept calendar records for the dinner nights. This distinguish between member and non member income ratio for the 990-T allocation. RA discussed this response with CPA \_\_\_\_\_ on July 25, 20XX. CPA maintains that the nonmember income is 0% per their calculation.

On August 12, 20XX, Agent received a 0 pages fax response to substantiate the nonmember and member income ration. In the response, EO circled the nonmember events, indicating that those events were open to the public. The events that were not circled were determined for member's purposes. The nonmember income ratio is still 0% as previously claimed by the organization.

On August 21, 20XX and October 22<sup>nd</sup>, 20XX, discussions with the organization's representative suggested that EO agrees with the nonmember income threshold being too high for a 501(c)(7) organization. However, formal agreement has not been secured by the CPA.

**Conclusion:**

The organization no longer qualifies for exemption under § 501(c)(7) of the Code as your investment and non-member income has exceeded the 35% threshold as well as nonmember income exceeded 15% threshold on a continuing basis. Therefore, we proposed to revoke your exempt status under § 501(c)(7) of the Code effective September 1, 20XX.

Form 1120 Corporation Income Tax Return should be filed starting with tax periods ending August 31, 20XX and thereafter as long as you continue to be subject to income tax.