

Three situations illustrate the application of certain concepts to be considered in determining the effect of the sale of property on the exempt status of a section 501(c)(7) social club.

Section 501(c)(7) of the Internal Revenue Code of 1954 provides for the exemption from Federal income tax of clubs organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder.

Section 1.501(c)(7)-1(b) of the Income Tax Regulations provides that a club which engages in business, such as selling real estate, is not organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes. However, an incidental sale of property will not deprive the club of its exemption.

Even though a profit is realized, the sale of property will not cause a social club to lose its exemption provided the sale is incidental in that it does not represent a departure from the club's exempt purposes. See *Anderson Country Club, Inc., v. Commissioner*, 2 T.C. 1238 (1943), acquiescence, C.B. 1944, 2. If, however, profit is the primary purpose of the sale, it will not be regarded as incidental. *Juniper Hunting Club, Inc. v. Commissioner*, 28 B.T.A. 525 (1933).

All the facts and circumstances of a sale will be considered in determining the club's primary purpose in making the sale. Included in the consideration will be: (1) the purpose of the club in purchasing the property; (2) the use the club makes of the property; (3) the reasons for the sale; and (4) the method used in making the sale.

The situations described below illustrate application of these concepts to organizations exempt from Federal income tax under section 501(c)(7) of the Code.

Situation 1

A club purchased the building and land that it had occupied under a lease for several years and continued to use the property for club purposes. Within a short time the members realized that ownership of the property was impractical, as the club's income was not sufficient to support its activities and the carrying charges on the property. For this reason the property was sold as a single unit. The club realized a profit from the sale. After the sale the club leased other facilities for its purposes. The proceeds from the sale were used to furnish and equip its new facilities.

It is held that the sale of the property under the circumstances described was incidental within the meaning of the regulations. The club originally purchased the property for social purposes. It could not have continued to operate for these purposes unless it sold the property. The facts indicate that the club sold the property primarily to be relieved of the financial burden imposed by ownership and not to derive a profit. Therefore, the sale did not jeopardize the exempt status of the club.

Situation 2

A club needed a site for a golf course, clubhouse, and other club facilities. In order to obtain the best site for the golf course, the club had to purchase a larger tract of land than it needed because the landowner refused to sell less than the entire property. After the golf course, the clubhouse, and other facilities were built, excess land remained. The club could have sold the property in a single unit. However, it decided to subdivide the land into building lots, make improvements on the lots, and offer them for sale. Sales of the lots were made over a period of years at substantial profits.

The club was not compelled to dispose of the excess land in the manner described. Its only purpose in electing to do so was to increase the profit to be derived from the sale of such land.

Under these circumstances, the purpose of the club in subdividing and improving the land was to produce a profit. Therefore, it is held that the disposition of the land was not an incidental sale of property within the meaning of the regulations. Accordingly, the club is not entitled to retain its exemption.

Situation 3

A golf club owned and occupied land in the suburbs of a large city. As the city expanded the club's property increased greatly in value. Taxes and maintenance costs also increased. Many of the club facilities had become antiquated and needed replacement. Most of the members had moved farther out in the suburbs so that the close-in location was no longer important. Consequently, the club sold the property to land developers at a profit. The club then used the proceeds to purchase land and build a more modern clubhouse and golf course farther out in the country.

It is held that this sale was incidental within the meaning of the regulations. The primary purpose of the sale was not to make a profit, but to lower the club's overhead and improve its facilities by moving to a more suitable location. There is no requirement in the law that a club must continue to occupy uneconomical and outdated premises in order to continue its exemption. Therefore, the sale did not adversely affect the exempt status of the club.