



TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

DEPARTMENT OF THE TREASURY  
Internal Revenue Service

May 14, 2007

Release Number: **200732024**

Release Date: 8/10/2007

UIL: 501.07-01

Org

Taxpayer Identification Number:

Form:

990 & 990-T

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:

Local Office

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,

Marsha A. Ramirez  
Director of EO

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

Legend:

ORG = Name of Organization

UIL: 501.07-01

NUM= EIN Number

Date1= Effective Date

Date2= Year End of the Year of Revocation

Date: May 14, 2007

ORG

Person to Contact:

Identification Number:

Contact Telephone Number:

Attention: Board of Directors

In Reply Refer to: TE/GE Review Staff

Dear Sir or Madam:

This is a Final Adverse Determination as to your exempt status under section 501(c)(7) of the Internal Revenue Code.

Our adverse determination was made for the following reasons:

ORG fails to meet the requirement for exemption under IRC 501(c)(7). IRC 501(c)(7), as changed by the Tax Reform Act of 1969 provides for the exemption of clubs organized and operated for pleasure, recreation, and other nonprofitable 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.

Public Law 94-568 amended IRC 501 to reflect a twofold change under IRC 501(c)(7). First, it makes it clear that a social club may receive some investment income without losing its exempt status. Second, it permits a higher level of income from nonmember use of club facilities than was previously allowed.

In addition, Public Law 94-568 defines gross receipts as those receipts from normal and usual activities of a club including charges, admissions, membership fees, dues, assessments, investment income, and normal recurring capital gains on investments, but excluding initiation fees and capital contributions. Public Law 94-568 also states that it is intended that social clubs should be permitted to receive up to 35 percent of their gross receipts, including investment income, from sources outside of their membership without losing their exempt status. Within this 35 percent amount, not more than 15 percent of the gross receipts should be derived from the use of the social club's facilities or services by the general public. Thus, a social club may receive investment income up to the full 35 percent amount of gross receipts. If a club receives unusual amounts, of income, such as from the sale of its clubhouse or similar facility, that income is not to be included in the 35 percent formula; that is, unusual income is not to be included in the gross receipts of the club.

Your organization has exceeded the safe harbor limitations on non-member income as outlined in Public Law 94-568. As a result, it has been determined that you are not operating as a social club within the meaning of section 501(c)(7).

Based on the above, we are revoking your organization's exemption from Federal income tax under section 501(c)(7) of the Internal Revenue Code effective Date1.

You are required to file Federal income tax returns on Form 1120. These returns should be filed with the appropriate Service Center for all years beginning after Date2, if you have not already done so. You have executed the Form 6018 agreeing to this revocation.

You are required to file Form 1120, U.S. Corporation Income Tax Return. Form 1120 must be filed by the 15<sup>th</sup> day of the third month after the end of your annual accounting period. A penalty of \$20 a day is charged when a return is filed late, unless there is reasonable cause for the delay. However, the maximum penalty charged cannot exceed \$10,000 or 5 percent of your gross receipts for the year, whichever is less. This penalty may also be charged if a return is not complete, so please be sure your return is complete before you file it.

You have the right to contact the office of the Taxpayer Advocate. However, you should first contact the person whose name and telephone number are shown above since this person can access your tax information and can help you get answers. You can call 1-877-777-4778 and ask for Taxpayer Advocate assistance. Or you can contact the Taxpayer Advocate from the site where the tax deficiency was determined by writing to: Local Taxpayer Advocate, Local Office. Taxpayer Advocate assistance cannot be used as a substitute for established IRS Procedures, formal appeals processes, etc. The Taxpayer Advocate is not able to reverse legal or technically correct tax determinations, nor extend the time fixed by law that you have to file a petition in the United States Tax 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.

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

Sincerely yours,

Marsha A. Ramirez  
Director, EO Examinations

Form <b>886A</b>	Department of the Treasury - Internal Revenue Service <b>Explanation of Items</b>	Schedule No. or Exhibit
Name of Taxpayer  Org		Year/Period Ended

Legend:

ORG= Name of Organization

TAX PERIODS= xxx xx, xxxx

**Issue #1** Does an organization that receives more than 15% of its income from non-members on a continuous and recurring basis continue to qualify for exemption as an organization described in 501c7 of the Internal revenue Code?

Facts:

The ORG was granted exemption in April as an organization described in section 501c7 of the Internal Revenue Code. The club was organized for social and recreational purposes. Its principal function was to hold dinner, meetings and enjoy social functions at participating clubs. However, recently per a review of Form 990 as well as a review of the activities the primary purpose of the organization has changed and the principal function is to provide a restaurant that operates in a commercial manner.

During tax periods ending xxx xx, xxxx and xxx-xx-xxxx, and xxx-xx-xxxx the ORG received \$ , \$ and \$ respectively from restaurant sales, sales of cookbooks and other sales which has been reflected on Part VII of Form 990. It was determined that the organization exceeded the 15% non-member threshold by a substantial amount which amounted to 19% 21% and 26% respectively during this three year period.

During a previous audit, it was brought to the organization's attention that the amount of non-member income received by the organization needed to be lowered in order to comply with the requirements outlined in public law bulletin 94-568

Law:

Section 501c7 of the Code provides for exemption from Federal income tax of clubs organized and operated exclusively for pleasure, recreational, and other non-profitable purposes providing no part of the net earnings inures to the benefit of any private shareholder.

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

Also, public law 94-568 was intended to permit organizations to receive up to 15% of its gross receipts from the use of social club facilities or services by the general public without jeopardizing its exempt status. Gross receipts are defined for this purpose as those receipts from normal

Form <b>886A</b>	Department of the Treasury - Internal Revenue Service <b>Explanation of Items</b>	Schedule No. or Exhibit
Name of Taxpayer  Org		Year/Period Ended

and usual activities of the club including charges, admissions, membership fees, dues and assessments and investment income and dividends.

In addition per Revenue Procedure 71-17 all organizations are required to maintain records reflecting the involvement of non-member use of the club. These records must contain the following information, date, the number of members in the party as well as the total charges.

Taxpayer's Position

Your organization has agreed to revocation of your organization's exempt status as indicated based on signed Form 6018.

Governments Position

Based on completing a three year income analysis during tax periods ending Xxx xx,xxxx and xxx xx ,xxxx, and xxx xx , xxxx, ORG has exceeded the 15% threshold as outlined in public law bulletin 94-569.

Conclusion

An organization that receives more than 15% of its gross income from non-members on a continuous and recurring basis does not continue to qualify for exemption.