



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

501.19-00

Number: 201218020
Release Date: 5/4/2012

LEGEND

ORG - Organization name
XX - Date Address - address
CO-1 = 1ST COMPANY

ORG
ADDRESS

Date: December 1, 2011

Employer Identification Number:

Person to Contact/ID Number:

Contact Numbers:

Voice:

Fax:

CERTIFIED MAIL – RETURN RECEIPT REQUESTED

Dear :

In a determination letter dated November 16, 19XX you were held to be exempt from Federal income tax under section 501(c)(19) of the Internal Revenue Code (the "Code") as a subordinate organization to the CO-1. pursuant to a group ruling, Group Exemption Number 9509.

Based on recent information received, we have determined you have not operated in accordance with the provisions of section 501(c)(19) of the Code. Accordingly, your exemption from Federal income tax is revoked effective January 1, 20XX. This is a final adverse determination letter with regard to your status under section 501(c)(19) 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 April 26, 20XX, you signed Form 6018-A, *Consent to Proposed Action*, agreeing to the revocation of your exempt status under section 501(c)(19) of the Code.

As a taxable entity, you are required to file Form[s] 1120, *U.S. Corporate Income Tax Return*, 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:

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

Sincerely,

Nanette M. Downing
Director, EO Examinations



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY

Internal Revenue Service
1122 Town & Country Commons Drive
Attention:TE:GE:EO:7956AS
Chesterfield, MO 63017

April 2, 2010

ORG
ADDRESS

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.

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,

Nanette M. Downing
Acting Director, EO Examinations

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

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit: Form 6018-A
Name of Taxpayer ORG		Year/Period Ended 12/31/20XX 12/31/20XX

LEGEND

ORG - Organization name ORG-1 - DBA Organization name XX - Date
Address - address City - city State - state CO-1 & CO-2 - 1st & 2nd
COMPANIES President - president President-1 - president-1 Vice
President - vice president Secretary - secretary CPA - CPA BM-1,
BM-2 & BM-3 - 1ST, 2ND & 3RD BM

ISSUES

Issue 1

Whether ORG ("ORG"), doing business as "ORG-1", meets the requirements for exemption under section 501(c)(19) of the Internal Revenue Code ("IRC")

Issue 2

Whether ORG operated exclusively for purposes listed in Treas. Reg. § 1.501(c)(19)-1(c).

FACTS

Background Information

CO-1 is a veterans organization that holds a group exemption for veterans organizations described in I.R.C. § 501(c)(19). Hereinafter, CO-1 will be referred to as "CO-1". CO-1 web page states that its mission is to "unite veterans and their families by forming social clubs throughout the United States, which interact with other social veterans clubs."

CO-1 website lists several advantages to be included in its group exemption as a subordinate organization. These advantages include selling liquor, operating on Sundays, holding bingo games, and obtaining liquor licenses in dry counties. CO-1 website markets the CO-1 Organization and its group exemption to existing bars and restaurants located in State as a way to avoid restrictive local liquor laws and as a way to operate on a tax-exempt basis. CO-1 website states that it will assist in a club's formation and application for a liquor license. CO-1 refers to its subordinate organizations as "clubs."

CO-1 website requires that its clubs have at least 10 veteran members. It also requires its subordinate organizations to send it proof of all veteran affiliation. One question that appears on CO-1 web page is "do I have to be a member's only club?" The response is "[a]lthough the tax advantages of being a members only club are greater, we do not require you to limit your bar to members.....Your doors may be kept open. By incorporating separately, you keep control of your own club. It is your choice if you wish

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit: Form 6018-A
Name of Taxpayer ORG		Year/Period Ended 12/31/20XX 12/31/20XX

to keep your doors open or closed. We only ask that you honor members of other chapters.”

ORG's Formation and Purpose

ORG, doing business as “ORG-1”, was incorporated by BM-1, BM-2, and BM-3. According to ORG's Articles of Incorporation, dated April 10, 20XX, the corporation was formed to better the lives of all veterans and their families and any other powers permitted a general non-profit corporation. The Articles further provide ORG is a membership organization. The Articles provide that in the event of dissolution, “After paying all liabilities of the corporation, all assets will be given to other veterans' organizations covered under the same 501(c)(19).”

ORG became a subordinate organization of CO-1 effective April 20XX.

ORG's governing documents include the “CO-1 Constitution and By Laws” a governing instrument provided to it by CO-1.

According to Section III of the “Bylaws for CO-1 Corporations”, ORG's stated purpose is: “uniting fraternally, veterans and the families of veterans, in order to work together to better the lives of all veterans and their families and to assist with any difficulties encountered by them.” These purposes include, but are not limited, to the following:

- A. Helping fellow veterans and their families receive the benefits for which they are entitled;
- B. Finding employment for veterans and their families;
- C. Helping the homeless veterans find housing and re-adjust to civilian life;
- D. Carrying on programs to perpetuate the memory of deceased veterans and members of the armed forces, and to comfort their survivors;
- E. Sponsoring or participating in activities of a patriotic nature;
- F. Providing social and recreational activities for its members;
- G. Assisting the disabled and needy war veterans and their dependents;
- H. Promoting awareness of the prisoners of war and the missing in action issues;

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit: Form 6018-A
Name of Taxpayer ORG		Year/Period Ended 12/31/20XX 12/31/20XX

I. Promoting the general welfare and prosperity of all CO-1 corporations;
and

J. Presenting and supporting the purposes of CO-1 before the public and the government.

According to Corporate Annual Registration Reports filed by ORG between June 14, 20XX and August 29, 20XX with the State Secretary of State, Officers and Board Members of the corporation are as follows:

	20XX	20XX	20XX
President	President	President	President
Vice-President	Vice President	Vice President	Vice President
Secretary	Secretary	Secretary	Secretary
Treasurer	None Named	None Named	None Named
Board Member	Secretary	Secretary	Secretary
Board Member	President	President	President
Board Member	Vice President	Vice President	Vice President

The corporation's current registered agent is President, Address, City, State.

ORG's Business Operations, Business Activities, and Members

ORG d/b/a "ORG-1" is located at Address, City, State. ACCURINT provides and it has been confirmed during the opening conference that the building is owned by President, President and Commander of ORG.

Assets identified within the facility are three flatscreen 19" color televisions, a bar; 15 bar stools; 7 booths, and 5 tables with about four chairs each; two coin operated pool tables, a beer cooler, juke box, commercial cooler, cash register, and miscellaneous neon liquor signs. All of the assets are located in the bar area. There is a store room for inventory, and two restrooms. There are chips hanging behind the bar.

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit: Form 6018-A
Name of Taxpayer ORG		Year/Period Ended 12/31/20XX 12/31/20XX

Miscellaneous sports paraphernalia adorn the walls of the very clean, very neat establishment.

Business and liquor licenses are displayed behind the bar. A banner displaying the establishment's affiliation with CO-1 is draped across the entire front of the building. A small sign on the front door identifies the establishment as ORG. Entry into the building is not restricted, however just inside the building there is a sign in book on a podium. President advised that the banner and sign in book are new additions recently added to bring the establishment closer to compliance with the membership requirements.

An operational interview was conducted by correspondence, due to bad weather, with a follow-up field visit on August 25, 20XX. In attendance were President, President-1, CPA, and CPA of President-1's firm. President provided that she became affiliated with CO-1 as a means to attract patronage of the bar. She has been affiliated with CO-1 since 20XX, which is when she came to express interest in operating the establishment. As liquor licenses are only available where there is a full kitchen, and ORG has no food preparation facilities, it would not have been possible to get a license without being an exempt organization. She purchased the building in 20XX via "Quit Claim Deed".

The organization provided a list of its membership effective November 20XX. The list provides for 14 members. Copies of Department of Defense Form DD-214 were included for each member listed on the handwritten member roster attached.

She is in the process of trying to sell the building. She explained that she joined CO-1 in order to give her more power to attract Veterans to her facility, because as it stands, ORG is in direct competition with a CO-2 within a few blocks of ORG, and restaurant even closer than that. Both the restaurant and the CO-2 are older establishments. Most of the area Veterans are members of and frequent the CO-2, leaving the patronage of ORG to everyone else.

President-1 provided that President had recently expressed to him an interest in dissolving the corporation altogether. In fact, he has already begun the application to the Secretary of State's office for the dissolution. President added that since CO-1 has had all of the problems with the IRS, and the subordinates such as her have all been targets of examinations, she feels she was misled with regard to how CO-1 really operated. She was unaware of all of the provisions of the law affiliated with the operation of an organization exempt under IRC § 501(c)(19) and provided that the organization's primary activity is in fact social and recreational, in that the primary activity is the operation of a bar that is open to the general public, and has always been the case. So, while she has provided documents and information to substantiate the revenue and expenses on the return, she can not provide information to show that the

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit: Form 6018-A
Name of Taxpayer ORG		Year/Period Ended 12/31/20XX 12/31/20XX

organization has a legitimate membership, or that the receipts of the organization came from such membership.

President stated that she realizes this puts the exempt status of the "club" in jeopardy, but she wants to be honest and would rather be shut down than be always worried about another visit from the IRS.

LAW AND ANALYSIS

Tax Exemption - Veterans Organizations

Prior to the enactment of I.R.C. § 501(c)(19) by Public Law 92-418, 1972-2 C.B. 675, many veterans organizations qualified for exemption from federal income tax under I.R.C. § 501(c)(4) because most of the traditional activities of these organizations were recognized by the IRS as primarily promoting social welfare. Staff of Joint Comm. on Taxation, 109th Cong., Historical Development and Present Law of the Federal Tax Exemption for Charities and Other Tax-Exempt Organizations, JCX-29-05 NO 8, (Comm. Print 20XX). The traditional activities of veterans organizations that were social welfare organizations included promoting patriotism, preserving the memory of those who died in war, and assisting veterans in need. *Id.* A veterans organization whose primary activity consisted of operating social facilities for its members was not able to qualify for exemption as a § 501(c)(4) social welfare organization, but it could qualify as a social club under § 501(c)(7). Rev. Rul. 66-150, 1966-1 C.B. 147; S. Rep. No. 1082, 92d Cong., 2d Sess. 2 (1972) reprinted in 1972-2 C.B. 713; H.R. Rep. No. 851, 92d Cong., 2d Sess. 1 (1972).

In 1972, Congress enacted I.R.C. § 501(c)(19) and I.R.C. § 512(a)(4) to address the concern that a veterans organization exempt under I.R.C. § 501(c)(4) or (7) may be subject to unrelated business income tax on the provision of insurance to its members. S. Rep. No. 1082, 92d Cong., 2d Sess. 2 (1972) reprinted in 1972-2 C.B. 713.¹ Section 512(a)(4) excludes amounts attributable to, or set aside by a §501(c)(19) veterans organization for the payment of life, sick, accident, or health insurance benefits for their members and their members' dependents. Public Law 92-418, 1972-2 C.B. 675.

The Section 501(c)(19) Exemption Requirements

* * * *

¹ "Before the enactment of the Tax Reform Act of 1969, there was no tax on the insurance activities of the veterans' organizations since the unrelated business income did not apply to social welfare organizations and social clubs. However, the 1969 Act extended the application of the unrelated business income tax to virtually all exempt organizations including social welfare organizations and social clubs." S. Rep. No.1082, 92d Cong., 2d Sess. 2 (1972) reprinted in 1972-2 C.B. 713.

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit: Form 6018-A
Name of Taxpayer ORG		Year/Period Ended 12/31/20XX 12/31/20XX

In General

Section 501(c)(19) of the Internal Revenue Code provides for the exemption from federal income tax of a post or organization of past or present members of the United States Armed Forces if it is:

- (a) organized in the United States or any of its possessions,
- (b) at least 75 percent of its members are past or present members of the Armed Forces of the United States,
- (c) substantially all of its other members are individuals who are cadets or are spouses, widows, widowers, ancestors or lineal descendants of past or present members of the Armed Forces of the United States or of cadets, and
- (d) no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Membership Requirements

Under I.R.C. § 501(c)(19), at least 75 percent of an organization's members must be past or present members of the Armed Forces of the United States ("veterans"). Section 501(c)(19) does not define the term "Armed Forces of the United States." The regulations under I.R.C. § 501(c)(19), likewise, do not define the term. Section 7701(a)(15) of the Code, however, defines "Armed Forces" to include all regular and reserve components of the uniformed services which are subject to the jurisdiction of the Secretary of Defense, the Secretary of the Army, the Secretary of the Navy, or the Secretary of the Air Force, and the Coast Guard.

In addition, I.R.C. § 501(c)(19)(B) requires that substantially all other members of an organization be cadets or spouses, widows, widowers, ancestors, or lineal descendants of veterans or cadets. According to the Senate Report accompanying the legislation, "substantially all" means 90 percent. See S. Rep. No. 1082, 92nd Cong. 2d Sess. 5 (1972), reprinted in 1972-2 C.B. 713, 715. Therefore, of the 25 percent of the members that do not have to be veterans, 90 percent must be cadets, or spouses, etc. Consequently, no more than 2.5 percent (10% x 25%) of an I.R.C. § 501(c)(19) organization's total membership may consist of individuals not mentioned in the statute.²

* * * *

² Prior to 20XX, ancestors and lineal descendent were not included in the statutory list of persons permitted to be members. In 20XX, Congress amended I.R.C. § 501(c)(19) to include ancestors or lineal
footnote continues next page

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit: Form 6018-A
Name of Taxpayer ORG		Year/Period Ended 12/31/20XX 12/31/20XX

Neither, I.R.C. § 501(c)(19), its legislative history, nor the regulations under I.R.C. § 501(c)(19) define what it means to be a member of a veterans organization. However, whatever the organization requires for one to become a member, the organization must maintain records tracking who its members are and the proportions in the various categories of membership permitted under I.R.C. § 501(c)(19)(B) (member of armed forces, cadet, relative, etc.) to substantiate that its members are veterans or other permitted members. See I.R.C. § 6001 and Treas. Reg. § 1.6001-1(c).³

Operational Test

Section 1.501(c)(19)-1(c) of the regulations provides that an organization exempt under I.R.C. § 501(c)(19) must be operated exclusively for one or more of the following purposes:

- 1) To promote the social welfare of the community as defined in section 1.501(c)(4)-1(a)(2) of the regulations,
- 2) To assist disabled and needy war veterans and members of the United States Armed Forces and their dependents and widows and orphans of deceased veterans,
- 3) To provide entertainment, care, and assistance to hospitalized veterans or members of the Armed Forces of the United States,
- 4) To carry on programs to perpetuate the memory of deceased veterans and members of the Armed Forces and to comfort their survivors,

continued footnote

descendants of present or former members of the United States Armed Forces or cadets in the statutory list of individuals who may be members of an organization. The regulations have not been updated to reflect this change nor do they reflect the 1982 statutory change eliminating a requirement that veterans be veterans of war.

³ Section 6001 of the Code provides that every person liable for any tax imposed by the Code, or for the collection thereof, shall keep adequate records as the Secretary of the Treasury or his delegate may from time to time proscribe. Every organization exempt from tax under § 501(a) and subject to the unrelated business income tax, including veterans organizations, must keep such records. Treas. Reg. § 1.6001-1(a). These books and records are required to be available for inspection by the Service. Treas. Reg. § 1.6001-1(a). In addition, veterans organizations are required to keep books and records to substantiate information reported on their information return. See I.R.C. § 6033 and Treas. Reg. § 1.6001-1(c). They are also required to submit additional information to the Service for the purpose of enabling the Service to inquire further into its exempt status.

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit: Form 6018-A
Name of Taxpayer ORG		Year/Period Ended 12/31/20XX 12/31/20XX

- 5) To conduct programs for religious, charitable, scientific, literary, or educational purposes,
- 6) To sponsor or participate in activities of a patriotic nature,
- 7) To provide insurance benefits for their members or the dependents of their members or both, or
- 8) To provide social and recreational activities for their members.

Treas. Reg. § 1.501(c)(19).

Social and Recreational Activities for Members

While Treas. Reg. §1.501(c)(19)-1(c)(8) does not address what it means to “exclusively” provide social and recreational activities for members it is similar to the exempt purpose contained in I.R.C. § 501(c)(7), as both provisions permit an exempt organization to operate social and recreational facilities for its members. In fact, prior to the enactment of I.R.C. § 501(c)(19), a veterans organization whose primary activity consisted of operating a bar or restaurant for the benefit of its members would have to qualify as §501(c)(7) social club to be tax-exempt. See Rev. Rul. 60-324 and Rev. Rul. 69-219.⁴ These organizations, prior to 1976, were required to operate “exclusively” for the pleasure and recreation of its members. See I.R.C. § 501(c)(7) (1975). Thus, the rulings and case law under I.R.C. § 501(c)(7) are useful for purposes of determining whether an I.R.C. § 501(c)(19) veterans organization is providing social and recreational activities exclusively for its members.

Treas. Reg. § 1.501(c)(7)-1(b) provides that a club that engages in business, such as making its social and recreational facilities available to the general public is not organized and operated exclusively for pleasure, recreation, and other nonprofit purposes, and is not exempt under I.R.C. § 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.

* * * *

⁴ In 1976, Congress amended § 501(c)(7) replacing “exclusively” with “substantially all.” This change was effected to establish that social clubs will not jeopardize their exempt status if they receive 35% of their gross receipts from non-membership sources. Only 15% of their gross receipts, however, may be derived from nonmembers’ use of club facilities or services. Pub. L. No. 92-568, S. Rep. 1318, 94 Cong., 2d Sess. (1976).

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit: Form 6018-A
Name of Taxpayer ORG		Year/Period Ended 12/31/20XX 12/31/20XX

In West Side Tennis Club v. Commissioner, 111 F.2d 6 (2nd Cir. 1940), cert. denied, 311 U.S. 674 (1940), the Second Circuit upheld the board of tax appeals determination that a social club was not exempt because a substantial amount of its income was received from the general public. West Side Tennis Club was organized to provide tennis facilities for the use and enjoyment of its members. The facilities were only available to members for most of the year; the club hosted annual national championship tennis matches, however, that were open to the general public. The club shared in the ticket proceeds from these matches. The Second Circuit upheld the board of tax appeals determination that the national championship matches were a substantial and profitable business which jeopardized the club's exemption. West Side Tennis Club, 111 F.2d at p. 7.⁵

In Rev. Rul. 60-324, 1960-2 C.B. 173 and Rev. Rul. 69-219, 1969-1 C.B. 153, the Service held that a § 501(c)(7) social club is not operated exclusively for the pleasure or recreation of its members if it makes its facilities available to the general public to a substantial degree. Id. However, this does not mean that all dealings with the general public are necessarily inconsistent with the club's exempt purposes. For instance, in Rev. Rul. 60-324, 1960-2 C.B. 173, the Service stated that:

[w]hile [the] regulations indicate that a club may lose its exempt status if it makes its facilities available to the general public, [it] does not mean that any dealings with outsiders will automatically cause a club to lose its exemption. A club will not lose its exemption merely because it receives some income from the general public, that is, persons other than members and their bona fide guests, or because the general public may occasionally be permitted to participate in its affairs, provided such participation is incidental to and in furtherance of its general club purposes and the income therefrom does not inure to members.

In 1971, the Service issued Revenue Procedure 71-17, 1971-1 C.B. 683, which contains guidelines for determining the impact of an organization's nonmember gross receipts on its exempt status under I.R.C. § 501(c)(7). The revenue procedure provides that "[a] significant factor reflecting the existence of a nonexempt purpose is the amount of gross receipts derived from use of a club's facilities by the general public." The

* * * *

⁵ In 1976, Congress amended § 501(c)(7) replacing "exclusively" with "substantially all." This change was effected to establish that social clubs will not jeopardize their exempt status if they receive 35% of their gross receipts from non-membership sources. Only 15% of their gross receipts, however, may be derived from nonmembers' use of club facilities or services. Pub. L. No. 92-568, S. Rep. 1318, 94 Cong., 2d Sess. (1976).

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit: Form 6018-A
Name of Taxpayer ORG		Year/Period Ended 12/31/20XX 12/31/20XX

revenue procedure went on to provide a safe harbor for organizations serving the general public:

As an audit standard, [the gross receipts derived from the general public] alone will not be relied upon by the Service if annual gross receipts from the general public for [use of the club's facility] is \$2,500 or less or, if more than \$2,500, where gross receipts from the general public for use is five percent or less of total gross receipts of the organization.

Rev. Proc. 71-17, 1971-1 C.B. 683 at § 3.01.

The term "general public" is defined as persons other than members or their dependents or guests. *Id.* at § 2.01. Section 3.03 of Rev. Proc. 71-17 provides four instances in which nonmembers are assumed to be the guests of the members. The assumptions include:

Where a group of eight or fewer individuals, at least one of whom is a member, uses club facilities, it will be assumed for audit purposes that the nonmembers are the guests of the member, provided payment for such use is received by the club directly from the member or the member's employer.

Where 75 percent or more of a group using club facilities are members, it will likewise be assumed for audit purposes that the nonmembers in the group are guests of members, provided payment for such use is received by the club directly from one or more of the members or the member's employer.

Rev. Proc. 71-17, Section 3.03.

In Pittsburgh Press Club v. United States, 615 F.2d 600 (3rd Cir. 1980), the Third Circuit upheld the Commissioner's determination that a social club failed to qualify for exemption from income tax as a §501(c)(7) organization because it was operated for business and not for the pleasure and recreation of its members. The Pittsburgh Press Club was organized for the purpose of providing a professional and social meeting place for its members. During the years under exam, however, the Pittsburgh Press Club hosted several functions for nonmember outside groups, although each such group had been member sponsored. Based on the amount of nonmember revenues (\$281,000 of nonmember receipts), as well as the percentage of those revenues (11 to 17 percent of gross receipts), the Third Circuit upheld the revocation stating that the exemption from Federal income tax for §501(c)(7) organizations "is to be strictly

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit: Form 6018-A
Name of Taxpayer ORG		Year/Period Ended 12/31/20XX 12/31/20XX

construed." Pittsburgh Press Club, 615 F.2d at 606. The Court stated that such strict construction cannot be reconciled with the fact that a substantial amount of the Club's activities and income consisted of nonmember functions and nonmember income. Therefore, the Court held "revocation of its exemption was proper." Id.

Recordkeeping and Reporting Requirements

Every person liable for any tax imposed by the Code, or for the collection thereof, shall keep adequate records as the Secretary of the Treasury or his delegate may from time to time prescribe. See I.R.C. § 6001. Every organization exempt from tax under I.R.C. § 501(a), and subject to the tax imposed by I.R.C. § 511 on its unrelated business income, must keep such permanent books or accounts or records, including inventories, as are sufficient to establish the amount of gross income, deduction, credits, or other matters required to be shown by such person in any return of such tax. Such organization shall also keep such books and records as are required to substantiate the information required by §6033. See Treas. Reg. §§ 1.6001-1(a) and 1.6001-1(c). The books or records required by section 1.6001-1 shall be kept at all times available for inspection by authorized internal revenue officers or employees, and shall be retained so long as the contents thereof may become material in the administration of any internal revenue law. See Treas. Reg. §1.6001-1(e). Except as provided, every organization exempt from tax under I.R.C. § 501(a) shall file an annual return, stating specifically the items of gross income, receipts and disbursements, and such other information for the purposes of carrying out the internal revenue laws as the Secretary may by forms or regulations prescribe, and keep such records, render under oath such statements, make such other returns, and comply with such rules and regulations as the Secretary may from time to time prescribe. See I.R.C. § 6033(a)(1).

Every organization which is exempt from tax, whether or not it is required to file an annual information return, shall submit such additional information as may be required by the Service for the purpose of inquiring into its exempt status and administering the provisions of subchapter F (i.e., I.R.C. § 501 and following), chapter 1 of subtitle A of the Code, I.R.C. § 6033, and chapter 42 of subtitle D of the Code. See Treas. Reg. §1.6033-2(i)(2). See also, I.R.C. § 6001, Treas. Reg. §1.6001-1.

An organization's failure or inability to file required information returns or otherwise to comply with the provisions of I.R.C. § 6033 and the regulations which implement it, may result in the termination of the organization's exempt status based on the grounds that the organization has not established that it is observing the conditions that are required for the continuation of its exempt status. See Rev. Rul. 59-95. These conditions require the filing of a complete and accurate annual information return (and other

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit: Form 6018-A
Name of Taxpayer ORG		Year/Period Ended 12/31/20XX 12/31/20XX

required federal tax forms) and the retention of records sufficient to determine whether the organization is operated for the purposes for which it was granted tax-exempt status and to determine its liability for any unrelated business income tax. Id.

Rev. Rul. 59-95, 1959-1 C.B. 627, concerns an exempt organization that was requested to produce a financial statement and statement of its operations for a certain year. Its records were so incomplete, however, that the organization was unable to furnish such statements. The Internal Revenue Service held that the organization's failure or inability to file the required information return or otherwise to comply with the provision of section 6033 of the Code and the regulations which implement it, may result in the termination of the exempt status of an organization previously held exempt, on the grounds that the organization has not established that it is observing the conditions required for the continuation of its exempt status.

Government's Position and Conclusions

Issue 1. ORG has not established it meets the membership requirements of IRC 501(c)(19).

The IRC provides that an exempt Veterans organization must meet certain membership requirements to maintain its exempt status. At least % of the members must be past or present members of the Armed Forces of the United States (veterans). Substantially all, which the IRC defines as %, of all other members must be cadets or spouses, widows, or widowers of veterans or cadets. Specifically, of the % of the organization's members that are not Veterans, % must be cadets, spouses, etc. Only % of the organizations total membership may consist of individuals who are not veterans, cadets or spouses, widows or widowers of these individuals.

An organization failing to meet the membership requirements will no longer qualify for exemption.

To illustrate, where a Veterans organization consists of 100 members, at least 75 must be Veterans. Of the 25 remaining members, 90% (23) must be cadets or spouses, widows, or widowers of veterans or cadets. The remaining 2 people may be members who are not veterans, cadets, spouses, etc. (75 + 23 + 2 = 100)

The instruction offered by CO-1 to its subordinates, ORG among them, is that it requires only ten members and the proof of the veteran status of such members; and "[a]lthough the tax advantages of being a members only club are greater, it does not require it subordinates to limit their bar to members.

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit: Form 6018-A
Name of Taxpayer ORG		Year/Period Ended 12/31/20XX 12/31/20XX

The tax advantages of being a members only club *are* greater for an organization exempt under IRC § 501(c)(19) because as the statute clearly provides it is the organizational requirement for such exempt status. An organization that does not meet the membership requirements is not exempt.

The statutes as cited above, further provide that in order that it may be clear that such membership exists, the organization must maintain records tracking who its members are and the proportions in the various categories of membership permitted (members of the armed forces, cadets, spouses, etc.) to substantiate that its members are veterans or other permitted members.

ORG provided information for 14 Veterans claiming to be members. However, based on the oral testimony of President and her Accountants, the organization does not have a membership application process, nor has it taken any steps to secure additional members. During the August 25, 20XX interview, President provided that the Veterans are not legitimate members, in fact the organization does not have members, as it is open to the general public. The organization therefore does not meet the membership requirements under IRC § 501(c)(19) for Veterans organizations.

Issue 2. ORG has not established that it operates exclusively for exempt purposes listed in Treas. Reg. § 1.501(c)(19)-1(c).

As is discussed more fully above, an organization described in I.R.C. § 501(c)(19) carries out activities in furtherance of its exempt purposes only when such activities are carried out exclusively in furtherance of the purposes listed in Treas. Reg. § 1.501(c)(19)-1(c). Among these purposes is the provision of social and recreational activities for its members. Accordingly, when a veterans organization described in I.R.C. § 501(c)(19) provides social and recreational activities for its members, or for guests whose expenses are paid by members, the organization is engaged in activities in furtherance of its exempt purposes. If such an organization makes its facilities available to the general public to a substantial degree, and/or a significant amount of the organization's income is received from the general public, the organization may lose its tax exemption.

The statute is clear that an organization recognized as exempt under IRC § 501(c)(19) is a *membership* organization. Patronage of the facility and the participation in the activities of an organization so exempt is limited to the exclusively to the organization's membership and guests.