



DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

501-07.00

TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

March 13, 2013

Release Number: 201333019

Release Date: 8/16/2013

LEGEND

ORG - Organization name

XX - Date Address - address

Taxpayer Identification Number:

Form:

Tax Year(s) Ended:

Person to Contact/ID Number:

Contact Number:

Group Manager Contact Number:

ORG  
ADDRESS

**CERTIFIED MAIL – RETURN RECEIPT REQUESTED**

Dear :

In a determination letter dated March 25, 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 letter with regard to your exempt status.

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 January 24, 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 are required to file Federal income tax returns for the for tax period(s) shown above. If you have not yet filed these returns, please file them 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.

Thank you for your cooperation.

Sincerely,

Nanette M. Downing  
Director, EO Examinations

Enclosure:  
Publication 892

**Internal Revenue Service**  
**Tax Exempt and Government Entities Division**  
Exempt Organizations: Examinations  
801 Tom Martin Drive  
Room 263  
Birmingham, AL 35211

**Department of the Treasury**

Date: November 30, 2012

Taxpayer Identification Number:  
Form:  
Tax Year(s) Ended:  
Person to Contact/ID Number:  
Contact Numbers:  
Telephone:  
Fax:

ORG  
ADDRESS

**Certified Mail – Return Receipt Requested**

Dear :

We have enclosed a copy of our report of examination explaining why we believe revocation 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-A, *Consent to Proposed Adverse Action*. We will then send you a final letter revoking your 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  
Director, EO Examinations

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

Form <b>886-A</b> (Rev. January 1994)	<b>EXPLANATIONS OF ITEMS</b>	Schedule number or exhibit  1
Name of taxpayer  ORG	Tax Identification Number  EIN	Year/Period ended Oct. XX-Sept. XX Oct. XX-Sept. XX

LEGEND

ORG - Organization name      EIN - ein      XX - Date      City - city      President -  
 president      Co-1 - 1<sup>st</sup> COMPANY

Issue:

1. Whether or not ORG will continue to qualify as an exempt organization under Internal Revenue Code (IRC) section 501(c)(7)?

Facts:

The ORG (ORG) was granted exemption as a social club exempt from Federal income tax under Internal Revenue Code section 501(c)(7) pursuant to a ruling issued on March 25, 19XX. Its purposes as stated in its Articles of Incorporation are: "provide for its members facilities and operating for them the sport commonly known as clay-bird shooting, in all of its aspect, and to that end the acquisition and maintenance and operation of the gun club and shooting grounds, and the equipment therefore, for clay-bird shooting; and the operation of local practice shoots, local registered shoots, state shoots, and any other shooting activities deemed by the Board of Directors to be in the interest of ORG."

ORG's principal activity is to encourage the sport of trapshooting and to provide the necessary facilities to its members. ORG holds specialty shoots and provides shooting lessons to both members and non-members. Skeet, trap, 5 stand non-members fees are \$, and \$ for members, sporting clays 100 are \$ for non-members and \$ for members.

In the fiscal year ending (FYE) September 30, 20XX, ORG derived most of its income from the sales of oil, gas, and mineral royalties. ORG received \$ from exempt function income and \$ from oil, gas and mineral royalties, \$ from advertising, and \$ from non-member use of the facility in FYE September 30, 20XX. There was a written contract provided for the oil, gas and mineral lease.

Board meeting minutes dated September 28, 20XX included a resolution of the board of directors stating: "Be it resolved by the board of directors of the ORG November 24, 20XX that President, President is hereby authorized to act on behalf of ORG and execute oil and gas leases whose terms are no less than \$ (dollars) per acre and % (percent) royalty." Oil, gas and mineral lease dated January 22, 20XX between the ORG, and CO-1 stated that the lessee may use the land for purposes of investigating, prospecting, drilling, mining and exploring (including exclusive rights to conduct geophysical/seismic operations and other related activities) for and producing oil, gas, and all other minerals, laying pipe lines, building drill sites, access roads, tanks, power stations, telephone lines, and other structures thereon to produce, save, take care of, treat, transport and own said products and for dredging and maintaining canals, constructing roads and bridges, and building houses for its employees, and, in general, for all appliances, structures, equipment, servitudes and privileges which may be necessary, useful or convenient to or in connection with any such operations conducted by Lessee thereon, or on any lands pooled therewith the following described land in City, to will:" The lease shall be for a term of 5 years and for a total amount of 48.30 acres of land. See the attached lease for more specific details.

During the examination, it was determined that ORG receives income from outside its membership and did not comply with the record-keeping requirements of Revenue Procedure 71-17, 1971-1 C.B. 683. Based on examination of ORG's Form 990 for the period ending September 30, 20XX, and 20XX, and Form 990-

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T for the period ending September 30, 20XX and 20XX and a review of their books and records, the percent of nonmember use of facilities exceeded % of its total gross receipts and more than % of its gross receipts are from non-member sources for the years under exam as well as the subsequent year. These receipts are noted in the following chart:

Year/Period Ended	% of gross receipts from nonmember use	% of gross receipts from investment income	Total % investment income / nonmember income
September 30, 20XX		0%	
September 30, 20XX		0%	

TABLE DELETED

**LAW:**

Organizations exempt from federal taxes as described in IRC Section 501(c)(7) include 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.

Section 1.501(c)(7)-1 of the Income Tax Regulations, relating to the requirements of exemption of such clubs under section 501(a), reads in part as follows:

- (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 its net earnings inure 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 ORG 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.

Prior to its amendment in 1976, IRC Section 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 a section 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. The Committee Reports for Public Law 94-568 further state:

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- (a) Within this 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. These percentages supersede those provided in Revenue Ruling 71-17, 1971-1 C.B. 683.
- (b) Thus, a social club may receive investment income up to the full 35 percent of its gross receipts if no income is received from non-members' use of club facilities.
- (c) In addition, the Committee Reports state 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.
- (d) The Senate report also indicates that even though gross receipts from the general public exceed this standard, it does not necessarily establish that there is a nonexempt purpose. A conclusion that there is a nonexempt purpose will be based on all the facts and circumstances including, but not limited to, the gross receipts factor.

Revenue Ruling 58-589 sets forth the criteria for exemption under section 501(c)(7) of the Code, and provides that a club must have an established membership of individuals, personal contacts, and fellowship. It also provides that, while the regulations indicate that a club may lose its exemption if it makes its facilities available to the general public, this does not mean that any dealings with nonmembers will automatically cause a club to lose its exemption. A club may receive some income from the general public, that is, persons other than members and their bona fide guests, or permit the general public to participate in its affairs, provided that such participation is incidental to and in furtherance of ORG's exempt purposes, such dealings with the general public and the receipt of income therefrom does not indicate the existence of a club purpose to make a profit, and the income does not inure to club members.

Revenue Ruling 60-324 provides that a social club that made its social facilities available to the general public through its member-sponsorship arrangement can not be treated as being operated exclusively for pleasure, recreation, or other nonprofitable purposes and ORG no longer qualified for exemption under 501(c)(7) of the Code.

Revenue Ruling 66-149 provides that a social club is not exempt from federal income tax as an organization described in section 501(c)(7) of the code if it regularly derives a substantial part of its income from non-member sources such as, for example, dividends and interest on investments.

Revenue Ruling 68-119 provides that a club will not necessarily lose its exemption if it derives income from transactions with other than bona fide members and their guests, or if the general public on occasion is 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.

Revenue Procedure 71-17 sets forth guidelines for determining the effect of gross receipts derived from nonmember use of a social club's facilities on exemption under Internal Revenue Code Section 501(c)(7) and recordkeeping requirements. Failure to maintain such records or make them available to the Service

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for examination will preclude use of the minimum gross receipts standard and audit assumptions set forth in this Revenue Procedure.

If a club exceeds the 15/35% test, then it will maintain its exempt status only if it can show through facts and circumstances that "substantially all" of its activities are for "pleasure, recreation and other non-profitable purposes."

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):

- The actual percentage of nonmember receipts and/or investment income.
- Frequency of use of ORG 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 ORG's facilities were made available to nonmembers.
- Whether the nonmember income generates net profits for the organization. Profits derived from nonmembers, unless set aside, subsidize ORG's activities for members and result in inurement within the meaning of IRC 501(c)(7).

**TAXPAYER'S POSITION:**

The ORG Inc. will have an opportunity to respond once this report is received.

**GOVERNMENT'S POSITION:**

An organization exempt from federal income taxes as described in IRC section 501(c)(7) must meet the gross receipts test in order to maintain its exemption. In order to meet the gross receipts test, an organization can receive up to thirty-five percent (%) of its gross receipts, including investment income, from sources outside its membership without losing its tax exempt status. Within this 35% amount, not more than fifteen percent (%) of the gross receipts should be derived from the use of a social club's facilities or services by non-members.

ORG, has exceeded the % gross receipts standard for nonmember income on a continuous basis for at least two years. The nonmember receipts are earned throughout the year. During the fiscal year ending September 30, 20XX there was a single unusual event that occurred but even without the gas, oil, mineral lease ORG still exceeded the 15% threshold and therefore no longer qualifies for exemption as a 501(c)(7) organization.

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Based on the large percentages of gross nonmember income to total gross receipts of ORG, (i.e., % for 20XX09 and % 20XX09 as noted in the above table), which exceeds the limitation of % as set forth by IRC 501(c)(7) for each of these years and the fact that the organization is not keeping adequate records to account for non-member income and advertises the use of their facilities to the general public, it is the Government's position that ORG is no longer operated exclusively for the pleasure and recreation of it's members and is not exempt under section 501(c)(7).

**CONCLUSION:**

The IRC Section 501(c)(7) tax exempt status of ORG . should be revoked since the nonmember income received by ORG exceeded 15% of ORG's total gross receipts for the years under examination. Further, it advertises the use of their facilities to the general public reflecting evidence that ORG is engaged in a business and is not being "operated exclusively for pleasure, recreation, or social purposes."

ORG . no longer meets the requirements to qualify as exempt from federal income tax under IRC section 501(a) as described in section 501(c)(7). Therefore, your exempt status under 501(c)(7) of the Internal Revenue Code will be revoked effective October 1, 20XX.

As a taxable entity, the organization is required to file Form 1120, U.S. Corporation Income Tax Return for the periods open under statute. Under 6501(g) these periods include the years ending September 30, 20XX and subsequent tax years.

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