

Internal Revenue Service

Appeals Office

100 First Street Suite 2000
San Francisco, CA 94105

Release Number: **201529013**

Release Date: 7/17/2015

Date: April 23, 2015

Department of the Treasury

Employer Identification Number:

Person to Contact:

Employee ID Number:

Tel:

Fax:

UIL: 0501 .35-00

Certified Mail

Dear

This is a final adverse determination regarding your exempt status under section 501(c)(3) of the Internal Revenue Code (the "Code"). It is determined that you do not qualify as exempt from Federal income tax under section 501(c)(3) of the Code.

Our adverse determination was made for the following reason(s):

You are not organized and operated exclusively for exempt purposes as described in section 501(c)(3). Under Treas. Reg. Section 1.501(c)(3)-1(c)(1), an organization will be regarded as operated exclusively for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in section 501(c)(3). More than an insubstantial part of your activities are the operation of a golf course, recreational facility and restaurant for members on a fee-for-service basis, which activities are not in furtherance of exempt purposes.

Contributions to your organization are not deductible under section 170 of the Code.

You are required to file Federal income tax returns on Forms 1120. File your return with the appropriate Internal Revenue Service Center per the instructions of the return. For further instructions, forms, and information please visit www.irs.gov.

Processing of income tax returns and assessments of any taxes due will not be delayed should a petition for declaratory judgment be filed under section 7428 of the Code.

We will make this letter and the proposed adverse determination letter available for public inspection under Code section 6110 after deleting certain identifying information. We have provided to you, in a separate mailing, Notice 437, *Notice of Intention to Disclose*. Please review the Notice 437 and the documents attached that show our proposed deletions. If you disagree with our proposed deletions, follow the instructions in Notice 437.

If you decide to contest this determination, you may file an action for declaratory judgment under the provisions of section 7428 of the Code 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 letter was mailed to you. Please contact the clerk of the appropriate court for rules for filing petitions for declaratory judgment. To secure a petition form from the United States Tax Court, write

to the United States Tax Court, 400 Second Street, N.W., Washington, D.C. 20217. See also Publication 892.

You also 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 matters that may not have been resolved through normal channels get prompt and proper handling. If you want Taxpayer Advocate assistance, please contact the Taxpayer Advocate for the IRS office that issued this letter. You may call toll-free, 1-877-777-4778, for the Taxpayer Advocate or visit www.irs.gov/advocate for more information.

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

Sincerely Yours,



Nan M. Shimizu
Appeals Team Manager

Enclosure: Publication 892 and/or 556



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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

Date: SEP 25 2014

Contact Person:

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

LEGEND

C= association
D = company
E= state
F= date
G= location
Q= company
R= company
S= association

U.I.L. Number

501.36-00
501.04-00
501.35-00

Dear /

We have considered your application for recognition of exemption from federal income tax under Internal Revenue Code section 501(a). Based on the information provided, we have concluded that you do not qualify for exemption under Code section 501(c)(3). The basis for our conclusion is set forth below.

Issues

Do you qualify for tax exemption under section 501(c)(3) of the Internal Revenue Code? No, for the reasons give below.

Facts

C, a local association of employees, is currently exempt under Internal Revenue Code 501(c)(4). C operates a facility and recreational park offering golf, basketball, volleyball, soccer, etc., as well as health initiatives and special outings for its members, who are current and retired employees of the companies of D. You incorporated a new

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Catalog Number 47630W

corporation in E on F, and applied for exemption under IRC 501(c)(3). With your application you provided minutes from a local zoning board meeting. These minutes discussed C's increased property tax on the property they own/operate, indicating C was 'in a bind' needing to increase revenue to keep the park. The city in which the park/facilities are located offered to buy the property from C and lease it back, however, C rejected this offer. The sale and lease were for each for \$1. Instead, you were formed by C who intended on transferring the aforementioned property to you once exemption under 501(c)(3) was secured.

The primary difference between you and C is that you will not restrict membership to only employees and retirees of D companies. You will open membership to the community and also expect to provide more to charitable causes including some free programs.

As stated in your Articles of Incorporation, you formed for the following purposes: (i) educate and promote amateur athletics (ii) promote health and wellness programs. (iii) promote facilities and services to the community, its members, and their families to promote good health.

In your Bylaws you stated the following purposes:

1. To foster the growth of quality recreational activities, sports programs, health and wellness programs, facilities and services to the community, its members, and their families.
2. The D park property, facilities, and all other assets owned by C will be gifted to you, as agreed by both R and C Membership. This transfer of asset and any liabilities shall thus become the responsibility of the newly formed organization (you).

The transfer of such assets will include all property, buildings, equipment, and materials at D park in E. Also to be transferred will be any such liabilities, including the existing mortgage held by the D credit union.

You will provide recreational programs and services, and maintain facilities and grounds needed to accomplish the objectives aforementioned. Your activities will include those conducted by C, specifically:

- 18 hole executive golf course
- Equipment rental
- Driving range
- Putting greens
- Clubhouse

- Restaurant
- Pro shop
- Golf lessons from pros
- Recreation center, with basketball and volleyball courts
- Banquet/wedding facilities
- Catering for events
- Lounge with food/refreshments
- Picnic areas
- Shelters
- Play areas
- Softball diamond
- Horseshoe and corn hole areas
- Equipment

Of your activities, you estimated 34% was spent on golf. You also provided forms submitted for rental of your facilities for various events such as golf outings, group picnics, restaurant reservation, and volleyball and basketball league and court rentals. Rates for these rentals varied between members or guests.

You also offer lessons in golf and volleyball, for hourly fees, and strength training and fitness programs, payable per sessions. Health seminars are offered at no cost.

Your facility consists of a clubhouse, restaurant and golf course. The clubhouse is a multi-use building for meetings, seminars, and banquets, offers food and houses the golf administrative offices. The restaurant provides food/beverage for patrons including employees and guests for all programs offered. The golf course includes practice areas, the course, and a program for instruction. You offer your golf facilities to local school teams and sponsor some regional tournaments.

Your members will continue to consist of D employees, D retirees, and their families. You offer affiliate membership to spouses or children of deceased D employees, former D employees or C members, military personnel working at D, and other contracted personnel working at D. Associate membership is offered to surrounding community residents, league participants, and designated business personnel. A look at your membership shows recent totals of around 1200 members who were D employees, retirees or family members, and around 150 who were non-employee or associate members. You expect to broaden membership once you opened to the public. You stated those in need may be offered free participation but offered no further elaboration on criteria for this evaluation and no mention of reduced membership fees is indicated on your membership brochure.

You charge annual fees for each member varying on their status and membership level. Non-employees of D are charged higher membership fees. While you have indicated anyone from the community may become a member, you have not defined what that community would consist of – the entire community is welcome to membership.

You have stated that you plan on having only one class of membership, whereas previously members could only be employees of D. However, the membership brochure you provided continues to show four types of members, D employee, D retiree, D affiliate and associate, and distinguishes those who are affiliated with D companies with those who are non-D employees from the community.

You will advertise your new open facility primarily via your web site and through email. You also expect to advertise through the local paper, TV and other news media, and to hold an open house.

All classes of membership shall be entitled to one vote in your affairs. Membership application shall be made on the prescribed forms. Initiation fees, annual membership dues, reinstatement fees, penalties, and means of collection shall be as specified in the membership application and/or the Bylaws.

Your sources of revenue will be: golf (greens fees, cart, range fees), lessons/merchandise, restaurant (food/refreshments), rentals, sports programs, outings/picnics and membership fees. Your largest source of revenue is from golf, and varies dependent on the event, holes played, whether equipment is rented, and whether participants are members or not. Income from your restaurant and rentals is also significant. A contract from a restaurant rental shows guests paying \$200 more, provides for a minimum rental fee, and stipulates all food and alcohol be purchased from your restaurant. You have filed Form 990T for three consecutive years and projected UBI will make up around 22% of your total income for the current year, generated from your snack bar and restaurant operation, whereas grants and donations are projected to make up 12% of your total income.

Your expenses consist primarily of salaries, occupancy and facility depreciation. Your breakdown of program service expenses consist of supplies, services and cost of goods sold for golf, the restaurant and the rec center, as well as program related equipment and supplies. You also provided a letter regarding a particular D employee group outing reflecting a payment of more than \$20000 for one year with a request for a similar amount for a subsequent year.

Law

Section 1.501(c)(3)-1(a)(1) of the Income Tax Regulations (regulations) states that to be tax exempt, an organization must be both organized and operated exclusively for one or

more exempt purposes specified in section 501(c)(3) of the Code. If an organization fails to meet either the organizational test or the operational test, it is not exempt.

Section 1.501(c)(3)-1(c)(1) of the regulations provides that an organization will be regarded as "operated exclusively" for one or more exempt only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in section 501(c)(3) of the Code. An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(d)(1)(ii) of the Regulations provides that an organization is not organized or operated exclusively for charitable purposes unless it serves a public rather than a private interest.

Section 501(c)(4) of the Code provides that civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare, or local associations of employees, the membership of which is limited to the employees of a designated person or persons in a particular municipality, and the net earnings of which are devoted exclusively to charitable, educational, or recreational purposes and no part of the net earnings of such entity inures to the benefit of any private shareholder or individual may be exempt from federal income tax.

Section 501(c)(7) exempts from federal income tax social clubs organized for pleasure, recreation, and other nonprofit 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. Social clubs are membership organizations.

Revenue Ruling 59-310, 1959-2 C.B. 146 describes an organization organized for the purpose of establishing, maintaining and operating a public swimming pool for the benefit of low-income groups and supported in part by public contributions may qualify for exemption as a charitable organization described in section 501(c)(3) of the Code. Residents of the community making use of such facilities consist principally of low-income groups who are unable to pay the cost of privately sponsored recreation facilities for themselves and their children.

Revenue Ruling 65-2, 1965-1 C.B. 227 describes an organization that qualified for exemption under Section 501(c)(3). It was organized and operated for the purpose of teaching a particular sport to children by holding clinics conducted by qualified instructors in schools, playgrounds, and parks, and by providing free instruction, equipment, and facilities.

Revenue Ruling 67-109, 1967-7 C.B. 136 describes an organization organized and operated solely for the purpose of establishing and maintaining a roller skating rink as a

recreational facility in cooperation with a county government, in a building provided rent free by a county, is an organization described in section 501(c)(4) of the Code where the rink is open to all the people of a county upon the payment of such nominal dues and admissions charges as are needed to defray operating expenses.

Revenue Ruling 74-281, 1974-1 C.B. 133 states that for purposes of IRC 501(c)(4), the term "employees" includes retired employees who were members of the employees' association at the time of retirement

Revenue Ruling 79-360, 1979-2 C.B. 237 holds that a health club facilities that operates in part in a commercial manner. Whose purpose is to provide for the welfare of young people, constitutes unrelated trade or business under section 513.

Better Business Bureau of Washington, D.C. v. United States, 326 U.S. 279, 283 (1945), the Court stated that "the presence of a single...[nonexempt] purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly...[exempt] purpose."

Schoger Foundation v. Commissioner, 76 T.C. 380 (1981) it was held that if an activity serves a substantial nonexempt purpose, the organization does not qualify for exemption even if the activity also furthers an exempt purpose.

Application of law

Section 1.501(c)(3)-1(a)(1) of the Income Tax Regulations (regulations) states that to be tax exempt, an organization must be both organized and operated exclusively for one or more exempt purposes specified in section 501(c)(3) of the Code. If an organization fails to meet either the organizational test or the operational test, it is not exempt. Section 1.501(c)(3)-1(c)(1) of the regulations provides that an organization will be regarded as "operated exclusively" for one or more exempt only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in section 501(c)(3). More than an insubstantial amount of your time is spent towards recreational activities for your members. Although your membership is open, membership fees restrict the extent to which the general public may participate. You provided no details on how you alleviate any dues payments for charitable purposes. For these reasons you are not operating exclusively under IRC 501(c)(3) for educational or charitable purposes.

Section 1.501(c)(3)-1(d)(1)(ii) of the Regulations provides that an organization is not organized or operated exclusively for charitable purposes unless it serves a public rather than a private interest. Accordingly, the Regulations provide, 'it is necessary for an organization to establish that it is not organized or operated for the benefit of private interests such as designated individuals, the creator or his family, shareholders of the

organizations, or persons controlled, directly or indirectly, by such private interests. While you have indicated the facility is for the community benefit, it is only for those able to pay the required membership fee. Despite opening up the facilities to the general public the majority of your members remain employees of D and its subsidiaries.

You are distinguishable from the organization described in Rev. Ruling 59-310, which describes an organization organized for the purpose of establishing, maintaining and operating a public swimming pool, playground and other recreation facilities for the children and other residents of a community. Most of your programs are for members that are employees of D and its subsidiary companies. The largest portion of your activities and income are related to your golf course and its greens fees. You provided no details on programs available to individuals unable to pay your membership and program fees. You have not distinguished your operations from a for profit recreational facility or social club described in 501(c)(7)

You are distinguished from the organization that received exemption under 501(c)(3) in Revenue Ruling 65-2. While you have instructional classes you have submitted no documentation you are providing any free of charge. Your classes are available only to paid members, are not directed primarily towards children, and while you provide some instructional clinics, your facility is structured more as a recreational center for individual participation in selected sports such as golf, aerobics or strength training.

You are similar to an organization described in Rev. Ruling 67-109. You are providing a facility open to the community for recreational purpose and charging a fee for the use of those facilities. That organization was found to be exempt under 501(c)(4) and distinguished for the organization in Revenue Ruling 59-310.

As stated in Better Business Bureau of Washington, a single non-exempt purpose, if substantial, will preclude tax exemption under section 501(c)(3) of the code. You are operating a member only recreational facility including a golf course charging greens fees as well as fees for golf instruction as a substantial portion of your activities. Also, more than 20% of your income will be generated from unrelated business income from your on-site restaurant and snack facilities.

You are similar to an organization described in section 501(c)(4) which is a local association of employees. Although you are opening up your membership to the community most of your members will still be employees of D. You also include retired members of D, which meets the definition of a local employee per Revenue Ruling 74-281. You are operating similar to C, which is currently exempt under 501(c)(4).

You are also similar to an organization exempt under 501(c)(7). Those types of organizations are member oriented and are primarily social and recreational in nature.

You offer recreational and social activities and facilities that are restricted to members.

Conclusion

You fail the operational test by conducting non-501(c)(3) activities that are more than insubstantial. You are also operating for the benefit of a private membership rather than the general public. Therefore, you do not qualify for exemption under section 501(c)(3) of the Code.

You have the right to file a protest if you believe this determination is incorrect. To protest, you must submit a statement of why you disagree. Your protest statement must be filed within 30 days of the date of this letter and should include:

- a. Your organization's name, address, EIN number and a daytime phone number.
- b. A statement that the organization wants to protest the proposed determination.
- c. A copy of this letter showing the findings that you disagree with (or the date and IRS office symbols from the letter).
- d. An explanation of your reasons for disagreeing including any supporting documents.
- e. The law or authority if any, on which you are relying.

The protest statement may be signed by one of your officers or your representative. We will consider your statement and decide if the information affects our determination. If your statement does not provide a basis to reconsider our determination, we will forward your case to our Appeals Office. You can find more information about the role of the Appeals Office in Publication 892, *How to Appeal an IRS Decision on Tax-Exempt Status*.

The protest statement should also include the following declaration.

"Under penalties of perjury, I declare that I have examined this protest including accompanying documents and, to the best of my knowledge and belief, the statement contains all relevant facts, and such facts are true, correct, and complete."

The declaration must be signed by an officer or trustee of the organization who has personal knowledge of the facts.

Your protest will be considered incomplete without this statement.

If an organization's representative signs and submits the protest, a substitute declaration must be included stating that the representative prepared the protest and

any accompanying documents; and whether the representative personally knows (or does not know) that the statement of facts in the protest and any accompanying documents are true, correct.

An attorney, certified public accountant, or an individual enrolled to practice before the Internal Revenue Service may represent you during the appeal process. If you want representation during the appeal process, you must file a proper power of attorney, Form 2848, *Power of Attorney and Declaration of Representative*, if you have not already done so. You can find more information about representation in Publication 947, *Practice Before the IRS and Power of Attorney*. All forms and publications mentioned in this letter can be found at www.irs.gov, Forms and Publications.

If you do not file a protest within 30 days, you will not be able to file a suit for declaratory judgment in court because the Internal Revenue Service (IRS) will consider the failure to appeal as a failure to exhaust available administrative remedies. Code section 7428(b)(2) provides, in part, that a declaratory judgment or decree shall not be issued in any proceeding unless the Tax Court, the United States Court of Federal Claims, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted all of the administrative remedies available to it within the IRS.

If you do not intend to protest this determination, you do not need to take any further action. If we do not hear from you within 30 days, we will issue a final adverse determination letter. That letter will provide information about filing tax returns and other matters.

Please send your protest statement, Form 2848, and any supporting documents to the applicable address:

Mail to:

Internal Revenue Service
EO Determinations Quality Assurance

Deliver to:

Internal Revenue Service
EO Determinations Quality Assurance

You may fax your statement using the fax number shown in the heading of this letter. If you fax your statement, please call the person identified in the heading of this letter to confirm that he or she received your fax.