



Department of the Treasury
Internal Revenue Service
P.O. Box 2508
Cincinnati, OH 45201

Release Number: **201706020**
Release Date: 2/10/2017
UIL Code: 501.07-00
501.07-05

Date: November 18, 2016

Employer ID number:

Contact person/ID number:

Contact telephone number:

Form you must file:

Tax years:

Dear _____ :

This letter is our final determination that you don't qualify for tax-exempt status under Section 501(c)(7) of the Internal Revenue Code (the Code). Recently, we sent you a proposed adverse determination in response to your application. The proposed adverse determination explained the facts, law, and basis for our conclusion, and it gave you 30 days to file a protest. Because we didn't receive a protest within the required 30 days, the proposed determination is now final.

You must file federal income tax returns for the tax years listed at the top of this letter using the required form (also listed at the top of this letter) within 30 days of this letter unless you request an extension of time to file.

We'll make this final adverse determination letter and the proposed adverse determination letter available for public inspection (as required under Section 6110 of the Code) after deleting certain identifying information. Please read the enclosed Notice 437, *Notice of Intention to Disclose*, and review the two attached letters that show our proposed deletions. If you disagree with our proposed deletions, follow the instructions in the Notice 437 on how to notify us. If you agree with our deletions, you don't need to take any further action.

If you have questions about this letter, you can contact the person listed at the top of this letter. If you have questions about your federal income tax status and responsibilities, call our customer service number at 1-800-829-1040 (TTY 1-800-829-4933 for deaf or hard of hearing) or customer service for businesses at 1-800-829-4933.

Sincerely,

Jeffrey I. Cooper
Director, Exempt Organizations
Rulings and Agreements

Enclosures:

Notice 437

Redacted Letter 4034, *Proposed Adverse Determination under IRC Section 501(a) Other Than 501(c)(3)*

Redacted Letter 4040, *Final Adverse Determination under IRC Section 501(a) Other Than 501(c)(3) - No Protest*



**Department of the Treasury
Internal Revenue Service**

P.O. Box 2508
Cincinnati, OH 45201

Date: September 30, 2016

Employer ID number:

Contact person/ID number:

Contact telephone number:

Contact fax number:

Legend:

B = State

C = Date of formation

F = City

w dollars = Amount

x dollars = Amount

UIL:

501.07-00

501.07-05

Dear _____ :

We considered your application for recognition of exemption from federal income tax under Section 501(a) of the Internal Revenue Code (the Code). Based on the information provided, we determined that you don't qualify for exemption under Section 501(c)(7) of the Code. This letter explains the basis for our conclusion. Please keep it for your records.

Issues

Do you qualify for exemption under Section 501(c)(7) of the Code? No, for the reasons stated below.

Facts

You are a nonprofit corporation formed in the state of B on C. You are formed for the social, literary, educational, musical, intellectual, athletic and physical development, improvement, benefit and amusement of members.

You own and operate a local golf course in the city of F. You maintain the course for the benefit of members and the public. You also operate a clubhouse for the benefit and convenience of members. The clubhouse is available for rent for various community functions. You are governed by a Board of Directors who has hired a clubhouse and course manager, as well as several seasonal part-time employees.

Your Articles of Incorporation state you will have stock that is non-assessable and non-dividend bearing, except as provided in your bylaws. Per your bylaws, you will have two classes of members, Stockholder Members and General Members. Stockholder Members are members who have purchased a share of your stock. The stock will be evidenced by a Certificate. Stockholder Members will be the only members who are qualified for a position on the Board of Directors, except for the role of President. They are also they only members who have voting rights for the Board of Directors, except the President who may vote in the case of a tie. In contravention to your bylaws, your Form 1024, *Application for Recognition of Exemption*, indicates that only members belonging to the Board of Directors have voting rights.

Shares of stock issued to Stockholder Members are not assignable or transferable. The holder of stock may apply to the Board of Directors for redemption of the stock. Per your Form 1024, you have over 100 shares of common stock, which is sold at w dollars per share. However, you later indicated that you have less than 70 members who hold shares and those shares have a value of x dollars. You do not pay any dividends.

General Members are all your other members who have paid annual dues. Anyone can be a member who has paid annual dues, with no limit to the number of members that can join. Members receive the benefit of unlimited golfing. You only have one annual event exclusively for your members. There are different membership rates for students, single members, couples, and families. Members receive membership cards and you maintain a membership list.

Your Board of Directors determines the initiation fee and dues payable. The amount is due annually and is the same for both Stockholder Members and General Members. A member may be suspended or terminated for cause, for ineligibility, or being in default of annual dues by vote of the Board of Directors.

You are open for public use. Non-members are allowed to golf on your course and patronize your clubhouse on a regular basis. You calculate that approximately 25% of your receipts are from non-member use of the club. There are no restrictions or additional benefits for being a member versus a public consumer. You have no special policies for guests of members.

Your sources of revenue include dues and membership, food and beverage sales, golf course green fees, cart rentals, space rentals, and clubhouse rentals. According to the financial data you provided, approximately 25% of your revenue is from membership dues. The other 75% is derived from the operation of the golf course and includes revenue from the bar, cart rentals, cart space rent, driving range, golf merchandise, green fees, insurance proceeds, machine income, as well as a few other minimal income sources. Your expenses are primarily operational expenses related to your activities.

Law

Section 501(c)(7) of the Code provides for the exemption from federal income tax of 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.

Treasury Regulation Section 1.501(c)(7)-1(a) states that the exemption provided by Section 501(a) of the Code for an organization described in Section 501(c)(7) of the Code 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 any part of 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.

Treas. Reg. Section 1.501(c)(7)-1(b) states that 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 the club 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.

Public Law 94-568, 1976-2 C.B. 596, provides that a social club may receive up to 35 percent of its gross receipts, including investment income from sources outside its membership, without losing exemption. 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 nonmembers so long as the latter do not represent more than 15 percent of the total receipts.

Rev. Rul. 58-588, 1958-3 C.B. 265, provides that an organization formed by several individuals to operate a health, recreational, and social club but whose predominant activity is the selling of services for profit to an unlimited number of so-called "members," who have no voice in the management of the club and whose only rights are to the use of the club's facilities upon the payment of specified fees is not a tax-exempt social club within the meaning of Section 501(c)(7) of the Code.

Rev. Rul. 58-589, 1958-2 C.B. 266, sets forth criteria or tests for determining whether an organization qualifies for exemption from federal income tax under Section 501(c)(7) of the Code. The ruling states that "...a club that makes its facilities open to the general public and the purpose is to increase its funds for enlarging its club facilities or for otherwise benefitting its members, it is evident that it is not operating as an exempt social club within the intentment of Section 501(c)(7) of the Code." There must be an established membership of individual, personal contacts and fellowship. A commingling of the members must play a material part in the life of the organization.

Rev. Rul. 60-324, 1960-2 CB 173, held that a social club that made its social facilities available to the general public through its member-sponsorship arrangement cannot be treated as being operated exclusively for pleasure, recreation, or other non-profitable purposes and no longer qualified for tax exemption under Section 501(c)(7) of the Code.

Rev. Rul. 69-219, 1969-1 C.B. 153, states that a social club that regularly holds its golf course open to the general public and charges established green fees that are used for maintenance and improvement of club facilities is not exempt under Section 501(c)(7) of the Code.

In Chattanooga Automobile Club v. Commissioner Warren Automobile Club, Inc. v. Commissioner, 182 F. 2d 551 (6th Cir. 1950), the United States Court of Appeals 6th Circuit held that to be exempt under the Act of Congress, a club must have been organized and operated exclusively for pleasure, recreation, and other non-profitable purposes. The court further specified that the words "other non-profitable purposes" must be construed as coming within the same classification as pleasure and recreation. In addition, there must be at least some sort of commingling of members to constitute a club. The court held that the two automobile clubs petitioning the court were not exempt under Section 101(9) of the Internal Revenue Code of 1939 as a social club because the members of these clubs did not commingle.

Application of law

You are not described under Section 501(c)(7) of the Code because you are not organized for pleasure, recreation, or other non-profitable purposes. You operate a golf course for members as well as for the general public. Per Treas. Reg. Sections 1.501(c)(7)-1(a) and 1.501(c)(7)-1(b), this exemption extends to social and recreational clubs which are supported by membership fees, dues and assessments and not for an organization that engages in business, such as making facilities available to the general public. While you do raise funds

through membership fees and assessments, you also are open to the public and raise a substantial amount of revenue from non-member sources. This demonstrates you are conducting commercial operations, rather than a social club for members.

You do not qualify for exemption per Public Law 94-568, which states no more than 15% of receipts may be from the use of a social club's facilities or services provided to the general public. You reported your non-member income to be more than 25% of your total receipts, which is greater than 15%. The conduct of business activities, including the public use of your social and recreational facilities, is incompatible with exemption, so even if you were to meet the facts and circumstances non-member income test you would still fail to qualify for exemption under Section 501(c)(7) of the Code.

You have only one organized member event per year – a city golf tournament. You provided no evidence of regular commingling of members, material in the operation of a Section 501(c)(7) social club. Thus, as in Chattanooga Automobile Club and Rev. Rul. 58-589, you are not organized exclusively for the pleasure and recreation of your members because you are formed primarily to offer a facility and services to the public with an insignificant amount of commingling.

You are similar to Rev. Rul. 60-324 and 69-219 because you are making your golf course and clubhouse facilities available to the general public. Accordingly, you are not operated exclusively for pleasure, recreation or other non-profitable purposes.

You are also similar to the organization described in Rev. Rul. 58-588 because your social purposes are incidental to your purpose of providing a golf course to the general public. Members who choose not to purchase stock have no voting rights and only receive unlimited golfing in return for their dues. This is similar to what you offer the general public, who can use your facilities for a fee. You also have no limit to the number of your members, so your General Members are not distinguishable from the general public, except in the manner in which they pay for services. When membership requirements are so broad or vaguely stated or the initiation charges or dues are so low that one-time or transient use of the facility by the general public is encouraged, it is questionable if the organization can be viewed as a true club.

Conclusion

You are not formed exclusively for pleasure, recreation, and other non-profitable purposes as required by Section 501(c)(7) of the Code. Your facility is regularly open to the public and you receive a substantial amount of your income from non-member sources. Additionally, your operations do not require members to commingle. Accordingly, you do not qualify for recognition of exemption under Section 501(c)(7).

If you don't agree

You have a right to file a protest if you don't agree with our proposed adverse determination. To do so, you must send a statement to us within 30 days of the date of this letter. The statement must include:

- Your name, address, employer identification number (EIN), and a daytime phone number
- A copy of this letter highlighting the findings you disagree with

- An explanation of why you disagree, including any supporting documents
- The law or authority, if any, you are relying on
- The signature of an officer, director, trustee, or other official who is authorized to sign for the organization, or your authorized representative
- One of the following declarations:

For an officer, director, trustee, or other official who is authorized to sign for the organization:

Under penalties of perjury, I declare that I examined this protest statement, 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.

For authorized representatives:

Under penalties of perjury, I declare that I prepared this protest statement, 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.

Your representative (attorney, certified public accountant, or other individual enrolled to practice before the IRS) must file a Form 2848, *Power of Attorney and Declaration of Representative*, with us if he or she hasn't already done so. You can find more information about representation in Publication 947, *Practice Before the IRS and Power of Attorney*.

We'll review your protest statement and decide if you provided a basis for us to reconsider our determination. If so, we'll continue to process your case considering the information you provided. If you haven't provided a basis for reconsideration, we'll forward your case to the Office of Appeals and notify you. 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*.

If you don't file a protest within 30 days, you can't seek a declaratory judgment in court at a later date because the law requires that you use the IRS administrative process first (Section 7428(b)(2) of the Code).

Where to send your protest

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

U.S. mail:

Internal Revenue Service
EO Determinations Quality Assurance
Room 7-008
P.O. Box 2508
Cincinnati, OH 45201

Street address for delivery service:

Internal Revenue Service
EO Determinations Quality Assurance
550 Main Street, Room 7-008
Cincinnati, OH 45202

You can also fax your statement and supporting documents to the fax number listed at the top of this letter. If you fax your statement, please contact the person listed at the top of this letter to confirm that he or she received it.

If you agree

If you agree with our proposed adverse determination, you don't need to do anything. If we don't hear from you within 30 days, we'll issue a final adverse determination letter. That letter will provide information on your income tax filing requirements.

You can find all forms and publications mentioned in this letter on our website at www.irs.gov/formspubs. If you have questions, you can contact the person listed at the top of this letter.

Sincerely,

Jeffrey I. Cooper
Director, Exempt Organizations
Rulings and Agreements

Enclosure:
Publication 892