



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

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Number: **202052024**
Release Date: 12/24/2020

UIL: 501-07.00

Date: April 24, 2020

Taxpayer ID Number:

Form:

For Tax Period(s) Ending:

Person to Contact:

Identification Number:

Telephone Number:

Fax Number:

CERTIFIED MAIL – Return Receipt Requested
LAST DAY FOR FILING A PETITION WITH THE TAX COURT:

Dear :

This is a final determination that you do not qualify for exemption from federal income tax under Internal Revenue Code (IRC) Section 501(a) as an organization described in IRC Section 501(c)(7) for the tax period(s) above.

In the future, if you believe your organization qualifies for tax-exempt status and would like to establish its status, you may request a determination letter from the Internal Revenue Service, you can request a determination by filing Form 1024, *Application for Recognition of Exemption Under Section 501(a)*, or Form 1024-A, *Application for Recognition of Exemption Under Section 501(c)(4) of the Internal Revenue Code* (as applicable) and paying the required user fee.

Our adverse determination as to your exempt status was made for the following reasons:

You have not established that you are organized and operated exclusively for an exempt purpose within the meaning of IRC Section 501(c)(7). You have not established that you are organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes, substantially all 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.

Organizations that are not exempt under IRC Section 501 generally are required to file federal income tax returns and pay tax, where applicable. For further instructions, forms, and information please visit www.irs.gov.

We previously provided you a report of examination explaining the proposed denial of your tax-exempt status. At that time, we informed you of your right to contact the Taxpayer Advocate, as well as your appeal rights. On December 13, 2019, you signed Form 6018, *Consent to Proposed Action – Section 7428*, in which you agreed to the denial of your tax exempt status as described under IRC 501(c)(7). This is a final determination letter with regards to your Federal tax-exempt status under Section 501(a).

If you decide to contest this determination, you may file an action for declaratory judgment under the provisions of IRC Section 7428 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 was mailed to you. Please contact the clerk of the appropriate court for rules and the appropriate forms for filing petitions for declaratory judgment by referring to the enclosed Publication 892. You may write to the courts at the following addresses:

United States Tax Court
400 Second Street, NW
Washington, DC 20217

U.S. Court of Federal
Claims 717 Madison Place, NW
Washington, DC 20005

U. S. District Court for the District of Columbia
333 Constitution Ave., NW
Washington, DC 20001

Processing of income tax returns and assessments of any taxes due will not be delayed if you file a petition for declaratory judgment under IRC Section 7428.

You may be eligible for help from the Taxpayer Advocate Service (TAS). TAS is an independent organization within the IRS that can help protect your taxpayer rights. TAS can offer you help if your tax problem is causing a hardship, or you've tried but haven't been able to resolve your problem with the IRS. If you qualify for TAS assistance, which is always free, TAS will do everything possible to help you. Visit www.taxpayeradvocate.irs.gov or call 1-877-777-4778.

Taxpayer Advocate assistance can't be used as substitute for established IRS procedures, formal appeals processes, etc. The Taxpayer Advocate is not able to reverse legal or technically correct tax determination, nor extend the time fixed by law that you have to file a petition in 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 can get any of the forms or publications mentioned in this letter by calling 800-TAX-FORM (800-829-3676) or visiting our website at www.irs.gov/forms-pubs.

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

Enclosures:
Publication 892

Sincerely,

Maria D. Hooke

Maria D. Hooke
Director, EO Examinations



Department of the Treasury
Internal Revenue Service
Tax Exempt and Government Entities

Date:
December 3, 2019

Taxpayer ID number:

Form:

Tax periods ended:

Person to contact:

Name:

ID number:

Telephone:

Fax:

Address:

CERTIFIED MAIL – Return Receipt Requested

Manager's contact information:

Name:

ID number:

Telephone:

Response due date:

Dear _____ :

Why you're receiving this letter

We enclosed a copy of our audit report, Form 886-A, Explanation of Items, explaining that your organization doesn't qualify as an organization described in Internal Revenue Code (IRC) Section 501(c)(7).

This letter is not a determination of your tax-exempt status under IRC Section 501 for any period other than the tax periods above.

If you agree

If you haven't already, please sign the enclosed Form 6018, Consent to Proposed Action, and return it to the contact person shown at the top of this letter. We'll issue a final adverse letter determining that you aren't an organization described in IRC Section 501(c)(7) for the periods above.

If you disagree

1. Request a meeting or telephone conference with the manager shown at the top of this letter.
2. Send any information you want us to consider.
3. File a protest with the IRS Appeals Office. If you request a meeting with the manager or send additional information as stated in 1 and 2, above, you'll still be able to file a protest with IRS Appeals Office after the meeting or after we consider the information.

The IRS Appeals Office is independent of the Exempt Organizations division and resolves most disputes informally. If you file a protest, the auditing agent may ask you to sign a consent to extend the period of limitations for assessing tax. This is to allow the IRS Appeals Office enough time to consider your case. For your protest to be valid, it must contain certain specific information, including a statement of the facts, applicable law, and arguments in support of your position. For specific information needed for a valid protest, refer to Publication 892, How to Appeal an IRS Determination on Tax-Exempt Status.

Fast Track Mediation (FTM) referred to in Publication 3498, The Examination Process, generally doesn't apply now that we've issued this letter.

4. Request technical advice from the Office of Associate Chief Counsel (Tax Exempt Government Entities) if you feel the issue hasn't been addressed in published precedent or has been treated inconsistently by the IRS.

If you're considering requesting technical advice, contact the person shown at the top of this letter. If you disagree with the technical advice decision, you will be able to appeal to the IRS Appeals Office, as explained above. A decision made in a technical advice memorandum, however, generally is final and binding on Appeals.

If we don't hear from you

If you don't respond to this proposal within 30 calendar days from the date of this letter, we'll issue a final adverse determination letter.

In the future, if you believe your organization qualifies for tax-exempt status and would like a status determination letter from the IRS, you can request a determination by filing Form 1024, Application for Recognition of Exemption Under Section 501(a), and paying the required user fee.

Contacting the Taxpayer Advocate Office is a taxpayer right

The Taxpayer Advocate Service (TAS) is an independent organization within the IRS that can help protect your taxpayer rights. TAS can offer you help if your tax problem is causing a hardship, or you've tried but haven't been able to resolve your problem with the IRS. If you qualify for TAS assistance, which is always free, TAS will do everything possible to help you. Visit www.taxpayeradvocate.irs.gov or call 877-777-4778.

Additional information

You can get any of the forms and publications mentioned in this letter by visiting our website at www.irs.gov/forms-pubs or by calling 800-TAX-FORM (800-829-3676).

If you have questions, you can contact the person shown at the top of this letter.

Sincerely,

Peter Jensen
for Maria Hooke

Director, Exempt Organizations Examinations

Enclosures:
Form 886-A
Form 6018

Form 886-A (May 2017)	Department of the Treasury – Internal Revenue Service Explanations of Items	Schedule number or exhibit
Name of taxpayer	Tax Identification Number (last 4 digits)	Year/Period ended 12/31/20XX

ISSUE:

Whether the tax-exempt status of _____ (_____), an IRC Section 501(c)(7) social club, should be disqualified.

FACTS:

The _____ Secretary of State website indicated, on April 10th, 19XX, _____ incorporated in _____ (the State); its principal office is located in _____ ; and, _____ entity status with the State is active and in good standing. The calendar year 20XX Form 990 indicated, _____ was incorporated for the purpose of promoting and extending fraternal, charitable, civic and social pursuits.

Our records do not indicate that _____ applied for tax-exemption status. Our records indicate prior to calendar year 20XX _____ filed Form 1120. In calendar year 20XX, _____ filed Form 990 and 990-T; thereby, self-declaring as a tax-exempt entity. _____ filed both Forms 990 and 990-T timely. On Form 990, Part VIII, line 2a, BAR/BANQUET FACILITY income was classified as unrelated trade or business income. BAR/BANQUET FACILITY represented _____ total income for calendar year 20XX. In addition, reported 0% of its total income and expenses on Form 990-T. On Form 990-T the specific deduction was not taken. Corporate tax rates were applied and paid.

_____ owns its building in which its activities are conducted. _____ operates _____ bars and an event scheduling service for its _____ halls. The sources of _____ 's income are: the sale of alcohol and snacks; various venues/events conducted in their halls; video gambling machines (keno and poker); annual banquet ticket sales; fundraising from mail solicitations; and, interest income.

On August 27, 20XX, AGENT _____ interviewed _____ (TREASURER) and _____ (ACCOUNTANT). _____ discussed that _____ does not have membership requirements; the club has been open to the general public since the "90s"; _____ sells package alcohol for off premises consumption; the club stopped paying their officers due to financial troubles; and, the club does not have members.

In addition, _____ and _____ discussed that they were not aware of Revenue Procedure 71-17 and Senate Report 94-1318; they were not able to provide a copy of the original application for tax exemption; and, in calendar year 20XX they decided to file Form 990 as the previous accountants were not knowledgeable about the proper filing requirements.

Form 886-A (May 2017)	Department of the Treasury – Internal Revenue Service Explanations of Items	Schedule number or exhibit
Name of taxpayer	Tax Identification Number (last 4 digits)	Year/Period ended 12/31/20XX

FACTS (continued):

On August 27, 20XX, AGENT conducted an examination of books and records. The scope of our examination is to schedule and analyze records to determine if records are in compliance with the record keeping requirements of Revenue Procedure 71-17; and, to determine if is organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes within the meaning of Public Law 94-568 (Senate Report 94-1318).

During the course of the examination, we scheduled and analyzed transactions and supporting documentation for the following sources of income: Sales – Beverages and Food (account #); Rental Income – Hall (account #); Merchandise Income (account #); Gambling Machine Income (account #); Income (account #); and, (account #).

Revenue Procedure 71-17 (Rev. Proc. 71-17) requires, Section 501(c)(7) organizations, to maintain adequate records to substantiate the gross receipts derived from nonmembers. Section 4 of Rev. Proc 71-17 provides the recordkeeping requirements that Section 501(c)(7) organizations are required to prepare and maintain. AGENT was not able to locate records prepared under the aforementioned recording keeping requirements. AGENT was not able to substantiate that sources of income were derived from members. Therefore, all sources of income were assumed to be derived from nonmembers.

books and records reported income from following sources:

Description	Sources of income	Amount
Beverages and Food	Nonmember	\$0
Rental income	Nonmember	\$0
income	Nonmember	\$0
Gambling machine income	Nonmember	\$0
donations	Nonmember	\$0
Merchandise income	Packaged alcohol for off premises consumption	\$0
Investment income and other income	Nonmember	\$0
Total income - Per Form 990, Part VIII, line 2a	Bar/Banquet Income	\$0

Form 886-A (May 2017)	Department of the Treasury – Internal Revenue Service Explanations of Items	Schedule number or exhibit
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Below are the results that were discovered during the examination or reported on Form 990.

Reporting Year	Total Income – (Per Form 990, Part I, line 7a)	Total nonmember income (Per examination or Form 990, Part V, line 10b)	Nonmember income % of total income	Net income / <Net loss> (Per Form 990, Part I, line 19)
20XX	\$0	\$0	0%	\$0
20XX	\$0	\$0	0%	\$0
20XX	\$0	\$0	0%	<\$0>
20XX	\$0	\$0	0%	\$0

Form 886-A (May 2017)	Department of the Treasury – Internal Revenue Service Explanations of Items	Schedule number or exhibit
Name of taxpayer	Tax Identification Number (last 4 digits)	Year/Period ended 12/31/20XX

LAW:

Treasury regulations:

Section 501(c)(7) of the Internal Revenue Code (the Code) provides for the exemption from federal income tax for clubs organized for pleasure, recreation, and other nonprofitable purposes, substantially all of the activities of which are for such purposes and no part of the net earnings of which inures to the benefit of any private shareholder.

Treasury Regulation Section 1.501(c)(7)-1(a) states that exemption provided by Section 501(a) of the Code for organizations described in Section 501(c)(7) of the Code applies only to clubs which are organized and operated exclusively for pleasure, recreation, and other nonprofitable 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. 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.

Treasury Regulation 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 nonprofitable purposes, and is not exemption under Section 501(a) of the Code. 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 purpose. However, an incidental sale of property will not deprive a club of its exemption.

Public Law 94-568, 1976-2 C.B. 896, 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 a club exempt from taxation described in Section 501(c)(7) is to be permitted to 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.

Revenue rulings:

Revenue Ruling 66-149, 1966-1 C.B. 146, held that a social club is not exempt from Federal income tax as an organization described in Section 501(c)(7) of the Internal Revenue Code of 1954 where it regularly derives a substantial part of its income from nonmember sources such as, for example, dividends and interest on investments which it owns. However, a club's right to exemption under section 501(c)(7) of the Code is not affected by the fact that for a relatively short period a substantial part of its income is derived from investment of the proceeds of the sale of its former clubhouse pending the acquisition of a new home for the club.

Form 886-A (May 2017)	Department of the Treasury – Internal Revenue Service Explanations of Items	Schedule number or exhibit
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LAW (continued):

Revenue rulings (continued):

Revenue Ruling 69-219, 1969-1 C.B. 153, held 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 exemption under Section 501(c)(7) of the Code.

Revenue Ruling 60-324, 1960-2 C.B. 173, held that A social club which has been granted exemption from Federal income tax under Section 501(c)(7) of the Code of 1954 may lose its exemption if it makes its club facilities available to the general public on a regular, recurring, basis since it may then no longer be considered to be organized and operated exclusively for its exempt purpose.

Revenue Ruling 68-535, 1968-2 C.B. 219, held that a social club that regularly sells liquor to its members for consumption off its premises is not entitled to exemption under Section 501(c)(7).

Revenue Ruling 67-428, 1967-2 C.B. 204, held that a federation of clubs does not qualify for exemption from Federal income tax under section 501 (c) (7) of the Internal Revenue Code of 1954.

Revenue Ruling 58-589, 1958-2 C.B. 266, held that a social club must establish (1) that it is a club both organized and operated exclusively for pleasure, recreation and other nonprofitable purposes. To meet the first requirement, there must be an established membership of individuals, personal contracts and fellowship. A commingling of the members must play a material part in the life of the organization.

Court cases:

Pittsburgh Press Club v. USA, 536 F.2d 572, (1976) the Court held that while the reports mandate the application of a “facts and circumstances test” in the event that gross receipts from nonmember and/or investment income reach the prohibited levels, they do not specify any of the relevant facts and circumstances that should be considered. However, the Court of Appeals in this case has indicated some factors to consider in determining exempt status.

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LAW (continued):

Court cases (continued):

Factors to consider in applying this test include:

- The actual percentage of nonmember receipts and/or investment income.
- The frequency of nonmember's use of club facilities. (An unusual or single event (that is, non-recurrent on a year to year basis) that generates all the nonmember income should be viewed more favorably than nonmember income arising from frequent use by nonmembers).
- The number of years the percentage has been exceeded. (The record over a period of years is also relevant. The high percentage in one year, with the other years being within the permitted levels, should be viewed more favorably to the organization than a consistent pattern of exceeding the limits, even by relatively small amounts).
- The purposes for which the club'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 the club's activities for members and result in inurement within the meaning of IRC 501(c)(7).

In *Polish American Club Inc v. Commissioner* 33 T.C.M 925 (1974) the Court held that making club facilities available to the general public, for a fee, represented a substantial activity disqualifying the club from exemption under Section 501(c)(7) of the Code.

Revenue procedures:

Revenue. Procedure. 71-17, 1971 WL 26186, 1971-1 C.B. 683 sets forth guidelines for determining the effect gross receipts derived from use of a social club's facilities by the general public have on the club's exemption from federal income tax under section 501(c)(7) of the Code.

The club must maintain books and records of each such use and the amount derived therefrom. This requirement applies even though the member pays initially for such use. In each instance the record must contain the following information:

1. The date;
2. The total number in the party;
3. The number of nonmembers in the party;
4. The total charges;
5. The charges attributable to nonmembers;
6. The charges paid by nonmembers;
7. Where a member pays all or part of the charges attributable to nonmembers, a statement signed by the member indicating whether he has been or will be reimbursed for such nonmember use and, if so, the amount of the reimbursement;

Form 886-A (May 2017)	Department of the Treasury – Internal Revenue Service Explanations of Items	Schedule number or exhibit
Name of taxpayer	Tax Identification Number <i>(last 4 digits)</i>	Year/Period ended 12/31/20XX

LAW (continued):

Revenue procedures (continued):

8. Where the member's employer reimburses the member or makes direct payment to the club for the charges attributable to nonmembers, a statement signed by the member indicating the name of his employer; the amount of the payment attributable to the nonmember use; the nonmember's name and business or other relationship to the member; and the business, personal, or social purpose of the member served by the nonmember use; and,

9. Where a nonmember, other than the employer of the member, makes payment to the club or reimburses a member and a claim is made that the amount was paid gratuitously for the benefit of a member, a statement signed by the member indicating the donor's name and relationship to the member, and containing information to substantiate the gratuitous nature of the payments or reimbursement.

Exceptions to these record keeping requirements are:

1. 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.
2. 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.
3. Solely for purposes of 1 and 2, above, payment by a member's employer will be assumed to be for a use that serves a direct business objective of the employee-member.

Form 886-A (May 2017)	Department of the Treasury – Internal Revenue Service Explanations of Items	Schedule number or exhibit
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GOVERNMENT’S POSITION/ANALYSIS:

The Pittsburgh Press Club v. USA court case indicate that when nonmember income reaches a prohibited level the following facts and circumstances should be considered:

- The frequency of nonmember’s use of club facilities. (An unusual or single event (that is, non-recurrent on a year to year basis) that generates all the nonmember income should be viewed more favorably than nonmember income arising from frequent use by nonmembers).
- The number of years the percentage has been exceeded. (The record over a period of years is also relevant. The high percentage in one year, with the other years being within the permitted levels, should be viewed more favorably to the organization than a consistent pattern of exceeding the limits, even by relatively small amounts).
- The purposes for which the club’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 the club’s activities for members and result in inurement within the meaning of IRC 501(c)(7).

Based upon the aforementioned facts, activities, including but not limited to the sale of alcohol for off-premises consumption, which derive gross receipts solely from nonmembers, are substantial and recurring. In addition, does not have a membership of individuals. Therefore, does not qualify for exemption as a social club described in Section 501(c)(7) of the Code; Treasury Regulation Section 1.501(c)(7)-1(a); and, Treasury Regulation Section 1.501(c)(7)-1(b) as is not organized and operated exclusively for pleasure, recreation, and other nonprofit purposes.

Revenue Rulings 67-428 and 58-589 stated that a club must have a membership of individuals, personal contacts, and fellowship. A commingling of members must play a material part in the activities of the organization. Although fellowship need not be present between each member and every other member of the club, it must constitute a material part of the organization's activities. Therefore, the aforementioned revenue rulings support the position that an organization must have membership with individuals to qualify under Section 501(c)(7).

Form 886-A (May 2017)	Department of the Treasury – Internal Revenue Service Explanations of Items	Schedule number or exhibit
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GOVERNMENT’S POSITION/ANALYSIS (continued):

Revenue Rulings 66-149, 69-219, and, 60-324 supports the position that a social club described in Section 501(c)(7) of the Code which regularly derives a substantial part of its income from nonmember sources is not exempt from Federal income tax.

Revenue Ruling 68-535 supports the position that the sale of alcohol for consumption off the club’s premises does not constitute the raising of income from members using the club’s facility. Neither is it income from the sale of merchandise to members through the operations of a bar. The regular sale of liquor for off premises consumption is not in furtherance of the social club’s exempt purposes. This activity is neither recreation nor social. Therefore, regularly conducting this activity and deriving substantial amounts of income from it will disqualify the club’s exemption from Federal income tax.

Public Law 94-568, 1976-2 C.B. 896, quantitatively defines substantial amounts of income from nonmembers. The law supports the position that a social club, which is open to the general public, shall not derive more than 15 percent of its total gross receipts from sources outside of membership without losing exemption from Federal income tax. It appears from calendar year 20XX to 20XX activities exceeded these limitations.

In Polish American Club Inc v. Commissioner, the courts’ decision supports the position that a social club described in Section 501(c)(7) of the Code which regularly derives a substantial part of its income from nonmember sources, on a recurring basis, is not exempt from Federal income tax.

TAXPAYER’S POSITION

On November 5, 20XX, the power of attorney (POA) and the taxpayer was offered a closing conference via telephone call. The POA and the taxpayer did not make a decision.

CONCLUSION

did not qualify, during the year 20XX, for exemption, under Section 501(c)(7) of the Code as your nonmember income has exceeded the 15% limit set by Congress in Public Law 94-568. Therefore, it is proposed that your exempt status under Section 501(c)(7) of the Code be disqualified for the yearend December 31st, 20XX.