



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

TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

Number: **202150032**  
Release Date: 12/17/2021

**Date: August 6, 2020**

**Taxpayer ID Number:**

**Form:**

**For Tax Period(s) Ending:**

**Person to Contact:**

**Identification Number:**

**Telephone Number:**

**Fax Number:**

**UIL: 501.07-00**

**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. Your determination letter dated August 9, 19XX is revoked.

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

You have not established that you are operated substantially for pleasure and recreation of its members or other non-profitable purposes and no part of the earnings inures to the benefit of private shareholder within the meaning of IRC Section 501(c)(7). You have made your recreational and social facilities available to the general public. You have exceeded the non-member income test for tax years ending January 31, 20XX and January 31, 20XX.

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](http://www.irs.gov).

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 20439

U. S. District Court for the District of Columbia  
333 Constitution Ave., N.W.  
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.

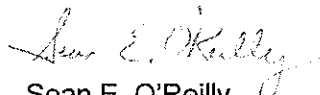
You may be eligible for help from the Taxpayer Advocate Service (TAS). TAS is an independent organization within the IRS that can help protect your taxpayer rights. TAS can offer you help if your tax problem is causing a hardship, or you've tried but haven't been able to resolve your problem with the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

Sincerely,



Sean E. O'Reilly  
Director, Exempt Organizations Examinations

Enclosures:  
Publication 892



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

Date:  
03/18/2020  
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 we propose to revoke your tax-exempt status as an organization described in Internal Revenue Code (IRC) Section 501(c)(7).

**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.

Letter 3618 (Rev. 8-2019)  
Catalog Number 34809F

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.

**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](http://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](http://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,

*Maria Hooke by m*

Maria Hooke

Director, Exempt Organizations Examinations

**Enclosures:**

Form 6018  
Form 4621-A  
Form 886-A  
Pub 892  
Pub 3498

Form <b>886A</b>	Department of the Treasury - Internal Revenue Service <b>Explanation of Items</b>	Schedule No. or Exhibit
Name of Taxpayer		Year/Period Ended 20XX- 20XX

**ISSUE:**

Whether ( ) continues to qualify for exemption as an organization described in the Internal Revenue Code (IRC) §501(c)(7).

**FACTS:**

was incorporated under the laws of the State of as a non-profit corporation on March 29, 19XX "(a) to promote and encourage social and fraternal relations among its members and to promote their educational, intellectual and cultural welfare; (b) to purchase, acquire, own and hold real property, both improved and unimproved, and thereon to maintain, operate and conduct a building or buildings and to furnish and equip same for the use of and occupation by of , Incorporated under the laws of the state of , as tenant or otherwise, and to sell, mortgage and/or encumber the same; (c) to acquire such property, including securities of other corporations and/or associations, as may be necessary, convenient or incidental to the foregoing purposes; (d) to promote the aims and objects of ; (e) this corporation shall have and exercise all rights and powers conferred or corporations under the laws of the State off , provided, however, that this corporation is not empowered to engage in any activity which in itself is not in furtherance of its purposes as set forth in subparagraphs(a), (b), (e) and (d) of this Article Four."

On August 9, 19XX, was recognized to be exempt from federal income tax as an organization described in IRC §501(c)(7).

is located at , Address reported on the return , is the Treasurer's personal residence, where books and records are kept.

Members of are initiated members, in good standing of of and other alumni who paid a one-time \$0.00 fee.

Directors of are President, Vice President, Secretary, Treasurer, and Parliamentarian.

exempt activities consist of an annual alumni reunion, 3 quarterly meetings which are conducted over the phone and a combined 4<sup>th</sup> quarter/annual meeting, conducted at a member's house. Outside of these meetings, it has no other social/pleasure activities.

does not carry out any social/pleasure activities at .

owns the property (lodge and attached parking lot) at .

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Name of Taxpayer		Year/Period Ended 20XX- 20XX

The building and the parking lot minus the spaces that are separately leased to the of ( ), are leased to ( ) fraternity under two, 0-years contracts, beginning in 08/01/20XX and 08/01/20XX. From 08/01/20XX, rental fee is \$0 per month for the first year and increases approximately 0% each subsequent year until 07/31/20XX. From 08/01/XX, rental fee is \$0 per month for the first year and increases approximately 0% each subsequent year until 7/31/20XX. puts down \$0 security deposit at the time of the signing of the lease. Contracts permit to sublease living quarters to two of its members. Currently, one of its members (a graduate student) is occupying a room in the building.

Fifteen parking spaces in the parking lot adjacent to the building are leased to . Contract with begins 06/01/20XX and lasts for 0 years. pays \$0 each year for the parking spaces.

Members of and are not members of . and are just other unaffiliated fraternities.

has an investment portfolio, actively managed by

In addition to capital gains from the selling of various securities in the investment portfolio, collects dividends from the portfolio and interest from a money market account.

Gross receipts reported on Form 990EZ for 20XX and 20XX:

	20XX	20XX	20XX	20XX
Membership dues and assessments	\$ -	\$ -	0%	0%
Rental income	\$ 0.00	\$ 0.00	0%	0%
Sales from investment portfolio	\$ 0.00	\$ 0.00	0%	0%
Interest	\$ 0.00	\$ 0.00	0%	0%
Dividends	\$ 0.00	\$ 0.00	0%	0%
	\$ 0.00	\$ 0.00	100%	100%

Books and records show \$0 was recorded as member dues for 20XX and nothing for 20XX.

fiscal year ends in January 31.

Years under examination are 20XX and 20XX.

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Name of Taxpayer		Year/Period Ended 20XX- 20XX

**LAW:**

IRC §501(c)(7) exempts from federal income tax clubs organized for pleasure, recreation, and other non-profitable purposes, substantially all of the activities of which are for such purposes and not part of the net earnings of which inures to the benefit of any private shareholder.

Treasury Regulation §1.501(c)(7)-1(a) states that the exemption provided by §501(a) for organizations described in §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 any part of its net earnings inures 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. §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 §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.

Public Law 94-568 provides that social clubs are permitted to receive up to 35% of their gross receipts from sources outside of their membership, including investment income, without losing their tax-exempt status. Within that 35%, not more than 15% of gross receipts should be derived from the use of a social club's facilities or services by the general public.

Rev. Rul. 58-589, 1958-2 C.B. 266, states that a business activity will defeat exemption, unless it is incidental, trivial or nonrecurrent. The Service has interpreted incidental, trivial or nonrecurrent to mean insubstantial for this purpose.

Rev. Rul. 66-149, 1966-1 CB 146, held that a social club was not exempt from federal income tax as an organization described in §501(c)(7) of the Code because it regularly derived a substantial part of its income from nonmember sources such as, for example, dividends and interest on investments.

Rev. Rul. 68-535, 1968-2 C.B. 219, held that a social club with regular sales of liquor to members for consumption off-site isn't exempt under IRC §501(c)(7).

In *Santa Barbara Club v. Commissioner*, 68 T.C. 200 (1974), the club sold liquor to its members for consumption away from the club's premises. The activity was conducted for over 40 years. The Court held the club was not exempt because the nontraditional

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activity did not further the club's social purposes, was recurrent, and the gross receipts were in excess of 25% of total gross receipts.

In *Polish American Club, Inc v Commissioner, TC Memo 1974-207 (1974)*, the court decided that the club is not qualified for exemption under §501(c)(7) of the Code because its non-member income was substantial, recurring and that it was not operated exclusively for pleasure, recreation and other nonprofit purposes.

In *Aviation Club of Utah v Commissioner of Internal Revenue Service*, 162 F.2d 984, the court held that the income received by the club from non-exempt activities is disproportionate compared to the income received from exempt purposes therefore, the club lost its exempt status.

**TAXPAYER'S POSITION:**

Unknown at this time.

**GOVERNMENT'S POSITION:**

does not operate exclusively for pleasure, recreation, and other non-profitable purposes described in Treasury Regulation §1.501(c)(7)-1(a).

receives 100% of its gross receipts from sources outside of its membership. reports no membership fees, dues, and assessments in 20XX and 20XX. Except for an immaterial amount of interest income, practically all its annual receipts come from a combination of rental payments from nonmembers and dividends plus realized gains from the investment portfolio.

The investment and rental activities represent substantial sources for nonexempt, unrelated business income because these activities are not incidental to exempt purposes, and the income derived from them are nontrivial and recurring. And as shown in Rev. Rul. 58-589, substantial business activities will defeat exemption.

Total gross income from the investment portfolio alone accounts for 0% in 20XX and 0% in 20XX of overall gross income. operates similarly to the club described in Rev. Rul. 66-149 where regular and substantial income from dividends and investment gains effectively preclude exemption.

Besides the investment income, gross rental receipts account for 0% in 20XX and 0% in 20XX of its overall gross income. These are substantial amounts derived from nontraditional activities. The long-term leasing of the parking spaces to along with the long-term leasing of the lodge and parking lot to , which includes a provision for sub-leasing of rooms as residential housing to members represent substantial nontraditional activities. These activities do not further exempt



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purposes even if they were conducted on membership basis and will jeopardize its exemption as demonstrated in *Santa Barbara Club v. Commissioner*.

As a result, total nonmember income well exceeds the 35% threshold set under P.L. 94-568 in both 20XX and 20XX.

Since derives 100% of its income from nonmember sources and nothing from membership dues, fees and assessments, this further illustrates a disproportionate amount of nonexempt income relative to its exempt income. A significant percentage of nonexempt income like the amount shown in this case has been proven as a basis for revoking exemption, for example, in *Aviation Club of Utah v. Commissioner of Internal Revenue Service*.

Additionally, because annual nonmember income is substantial and recurring, thus proving that it is not operated exclusively for pleasure, recreation and other nonprofit purposes as established in *Polish American Club, Inc. v. Commissioner*.

**CONCLUSION:**

is not operated exclusively for pleasure, recreation and other nonprofit purposes required under Treasury Regulation §1.501(c)(7)-1(a) because 100% of its income is derived from nonexempt activities in each year under examination. These nonexempt activities are nontrivial, recurring and do not further exempt purposes. annual nonexempt income is disproportionately larger than its exempt income and far surpasses the maximum level of 35% of total gross receipts allowed under P.L. 94-568. Consequently, exemption under IRC 501(c)(7) should be revoked as of February 1, 20XX. must file Form 1120, *U.S. Corporation Income Tax Return* instead of Form 990, *Return of Organization Exempt From Income Tax* beginning with tax year 20XX going forward.