



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

Date: February 17, 2021

Taxpayer ID number:

Form:

Tax periods ended:

Release Number: **202221012**
Release Date: 5/27/2022
UIL: 501.07-00

Person to contact:
Name:
ID number:
Telephone:
Fax:

CERTIFIED MAIL - RETURN RECEIPT REQUESTED

Dear _____ :

Why we are sending you this letter

This is a final determination that you don't 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 periods above. Your determination letter dated February 18, 19____, 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 _____, and _____.

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.

What you must do if you disagree with this determination

If you want to contest our final determination, you have 90 days from the date this determination letter was mailed to you to file a petition or complaint in one of the three federal courts listed below.

How to file your action for declaratory judgment

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.

Please contact the clerk of the appropriate court for rules and the appropriate forms for filing an action for declaratory judgment by referring to the enclosed Publication 892, How to Appeal an IRS Determination on Tax-Exempt Status. 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.

Information about the IRS Taxpayer Advocate Service

The IRS office whose phone number appears at the top of the notice can best address and access your tax information and help get you answers. However, you may be eligible for free help from the Taxpayer Advocate Service (TAS) if you can't resolve your tax problem with the IRS, or you believe an IRS procedure just isn't working as it should. TAS is an independent organization within the IRS that helps taxpayers and protects taxpayer rights. Contact your local Taxpayer Advocate Office at:

Internal Revenue Service
Taxpayer Advocate Office

Or call TAS at 877 777 4778. For more information about TAS and your rights under the Taxpayer Bill of Rights, go to taxpayeradvocate.irs.gov. Do not send your federal court pleading to the TAS address listed above. Use the applicable federal court address provided earlier in the letter. Contacting TAS does not extend the time to file an action for declaratory judgment.

Where you can find more information

Enclosed are Publication 1, Your Rights as a Taxpayer, and Publication 594, The IRS Collection Process, for more comprehensive information.

Find tax forms or publications by visiting www.irs.gov/forms or calling 800-TAX-FORM (800-829-3676).

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

If you prefer to write, use the address shown at the top of this letter. Include your telephone number, the best time to call, and a copy of this letter.

Keep the original letter for your records.

Sincerely,



Sean E. O'Reilly

Director, Exempt Organizations Examinations

Enclosures:
Publication 1
Publication 594
Publication 892



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

Date: September 17, 2020
Taxpayer ID number:

Form:

Tax periods ended:

Person to contact:

Name:
ID number:
Telephone:
Fax:
Address:

Manager's contact information:

Name:
ID number:
Telephone:
Response due date:

CERTIFIED MAIL – Return Receipt Requested

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.

After we issue the final adverse determination letter, we'll announce that your organization is no longer eligible to receive tax deductible contributions under IRC Section 170.

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.

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.

For 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,

Sean O'Reilly by em

Sean E. O'Reilly
Director, Exempt Organizations
Examinations

Enclosures:
F 4621-A
Form 6018
Form 886-A
Pub 892
Pub 3498

| | | |
|---------------------------------|---------------------------------------------------------------------------------------|-------------------------------|
| 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>) XX-XXX | Year/Period ended |

ISSUE:

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

FACTS:

_____ articles of incorporation were filed in the state of _____ on September 12, 19xx. The exact legal name of the organization in the articles of incorporation is _____. The purpose stated in the articles of incorporation were to acquire and maintain a community house and grounds in the village of _____ for promoting and fostering the educational and religious purpose of the community.

The _____ Secretary of State website indicated, _____ was reinstated on July 18, 20xx, its principal office address is _____ entity status with the State is active and in good standing.

On August 23, 19____ the organization submitted form 1024, Application for Recognition of Exemption Under Section 501(a) and requested exemption as a social welfare organization exempt under section IRC 501 C 4. _____ stated its purpose was to provide swimming, tennis and basketball activities for its members. _____ was granted exemption as a social club and exempt under section IRC 501 C 7. The letter of exemption as a section IRC 501 C 7 social club was issued on Feb. 18, 19xx.

On May 1, 20xx, _____ filed form _____ and form _____ for the year ending _____ and reported the following revenues

1. Membership dues
2. Clubhouse rental
3. Tennis
4. Pool
5. Other

Total Revenues _____ \$

On March 5, 20xx, _____ was contacted by letter 3611, informing the organization that its form _____ for 20xx had been selected for examination. The organization was informed that the examination and request for documents was to verify the non-member usage of the club's facilities and the organization's continued qualification for exemption under section IRC 501 C 7 as a social club.

| | | |
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On August 04, 20xx, submitted the response to information document request. The organization submitted books, records and bank statements for the year ending December 31, 20xx.

On August 06, 20xx, the organization was informed that the examination would be expanded to include form for the year ending and the form for the years of 20xx and 20xx.

On August 19, 20xx, a telephone interview was conducted with the organization's treasurer, . As per the interview, owns its building in which its activities are conducted. operates a club house, swimming pool and tennis court. The sources of income are membership dues, club house rental, pool and tennis court usage.

The organization is governed by a board of directors. Different members of the board oversee the different club activities. Membership is for one year; membership dues is normally due in February. Memorial Day to Labor Day is the clubs busiest time. Tennis is year-round. The organization conducts movie nights and cook outs for members. Club house rental to nonmembers is year-round. The total number of members is between xxx to xxx. The members include an entire family as one member. The annual membership fees are based on the number in the family.

On August 19, 20xx, as per interview with the organization's treasurer, nonmembers/guests can use the pool and the tennis courts but must be accompanied by a member. For the pool use, member pay \$ per guest. For the tennis court use, members pay \$ per guest. The organization did not provide the substantiation to document the usage of the pool and the tennis courts by nonmembers/guest.

The organization also rents out its club house to non-members. The organization submitted journals and rental agreements with the nonmembers.

As per form , the organization reported nonmember or unrelated business income as follows:

| | | | | |
|---------------------------------|--|------|------|------|
| Form | | | | |
| Part VIII Statement of Revenues | | | | |
| | | 20XX | 20XX | 20XX |
| Line 2 g | | | | |
| Unrelated Business Revenue | | | | |
| Line 12 | | | | |
| Total Revenue | | | | |

| | | |
|---------------------------------|---------------------------------------------------------------------------------------|-------------------------------|
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As per examination of the organization's books, records and review of the forms and forms filed by the organization, the following is a computation of the organization total revenue and the nonmember percentage of the total revenue.

NONMEMBER INCOME PERCENTAGE OF TOTAL REVENUE

| 15% Test | Form | 20XX | 20XX | 20XX | |
|--------------------------------------|------|------|------|------|--|
| Total Nonmember Income | | | | | |
| Total Gross receipts | | | | | |
| Nonmember % cannot exceed 15% | | % | % | % | |

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.

Section 1.501(c)(7) of the Regulations provides that, in general, the exemption extends to social and recreation clubs supported solely by membership fees, dues and assessments. However, a club that engages in a business, such as making its social and recreational facilities open to the general public, is not organized and operated exclusively for pleasure, recreation and other non-profitable purposes, and is not exempt under section 501(a).

Prior to its amendment in 1976, IRC § 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 an IRC § 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 (Senate Report No. 94-1318 2d Session, 1976-2 C.B. 597) further states;

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(a) Within the 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.

(b) Thus, a social club may receive investment income up to the full 35 percent of its gross receipts if no income is derived from non-members' use of club facilities.

Revenue Ruling 66-149 holds a social club as not exempt as an organization described in IRC § 501(c)(7) where it derives a substantial part of its income from non-member sources.

Revenue Ruling 60-324 states by making its social facilities available to the general public the club cannot be treated as being operated exclusively for pleasure, recreation or other non-profitable purposes.

Revenue Procedure 71-17 sets forth the guidelines for determining the effect of gross receipts derived from the general public's use of a social club's facilities on exemption under IRC § 501(c)(7). Where nonmember income from the usage exceeds the standard as outlined in this Revenue procedure, the conclusion reached is that there is a non-exempt purpose and operating in this manner jeopardizes the organization's exempt status.

TAXPAYER POSITION

On September 11, 20xx, revenue agent spoke with organizations treasurer, treasurer agreed with determination

GOVERNMENT POSITION

The cited Code and Regulations above provide criteria for recognition of a tax-exempt organization under IRC 501(c)(7). Generally, an organization is to be organized and operated exclusively for pleasure, recreation, and other nonprofit purposes. In general, this exemption extends to social and recreation clubs which are supported solely by membership fees, dues, and assessments.

In the case of the organization under examination, it was granted exemption in 19xx, as a social club under IRC 501(c)(7). IRC 501 c 7 organizations are limited to the amount of nonmember income that it can receive and still maintain its exempt status. The nonmember income limitation is 15% of the gross revenue received.

| | | |
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In the year of examination, nonmember income was % of the total income received. The facts provided about the organization under examination shows that for the years 20xx – 20xx, the entity exceeded the nonmember income limitation.

The has exceeded the 15% nonmember limitation in all of the identified years. The subject organization does not qualify for exemption under IRC 501 C 7. The exemption status should be changed and revoked.

CONCLUSION

Based on the above facts and circumstances, and considering the statutory law and rulings cited. The organization has exceeded the 15% nonmember income limitation. The organization does not qualify for tax-exemption under IRC §501(c)(7) and should be revoked. The proposed date of the revocation is January 1, 20xx.

Form 1120, U.S. Corporation Income Tax Return should be filed for 20xx and thereafter if the organization continues to be subject to income tax.

ALTERNATIVE POSITION

Issue

If the proposed revocation of exempt status is not upheld, the organization form should be adjusted to include nonmember income from the usage of the pool and tennis courts and nonmember income from the lease revenues from the cell tower.

Facts

The organization filed form and form for 20xx and 20xx timely. The organization reported a total of unrelated nonmember income on form in the amount of \$ for 20xx and \$ for 20xx.

As per interview with the treasurer on August 19, 20xx, the organization allows nonmembers to use their pool and tennis courts, the nonmember must be accompanied by a member. The member is required to pay \$ on behalf of their guest.

The organization received \$ for 20xx and \$ for 20xx for nonmember usage of the pool and tennis courts.

This amount was not reported on form .

| | | |
|---------------------------------|---------------------------------------------------------------------------------------|-------------------------------|
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The organization received income from leasing its cell tower in the amount of \$, this amount was not reported on form .

As per examination of books, records, bank and financial statements. The organization did not provide the required substantiation of Revenue Procedure 71-17 for social clubs to substantiate nonmember usage of the club's facilities.

LAW

IRC § 511(a)(1) imposes a tax on the unrelated business taxable income (UBTI) of organizations described in § 501(c).

IRC § 512(a)(3)(A) defines unrelated business taxable income for IRC 501(c)(7) social clubs as gross income excluding any exempt function income, less the deductions allowed that are directly connected with the production of the income.

IRC § 512(a)(3)(B) Exempt function income is defined as "gross income from dues, fees, charges, or similar amounts paid by members of the organization as consideration for providing such members or their dependents or guests goods, facilities, or services in furtherance of the purposes constituting the basis for the exemption of the organization to which such income is paid."

Revenue Procedure 71-17 sets forth the guidelines for determining the effect of gross receipts derived from the general public's use of a social club's facilities on exemption under IRC § 501(c)(7). Where nonmember income from the usage exceeds the standard as outlined in this Revenue procedure, the conclusion reached is that there is a non-exempt purpose and operating in this manner jeopardizes the organization's exempt status.

TAXPAYERS POSITION

On September 11, 20xx, discussed findings with organizations treasurer. Advised officer that the converted return form 1120, must include the adjustments to unrelated business income not reported on form .

GOVERNMENT POSITION

The organization received nonmember income for 20xx in the amount \$ and cell tower lease revenue in the amount of \$.

| | | |
|---------------------------------|---------------------------------------------------------------------------------------|-------------------------------|
| 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>) XX-XXX | Year/Period ended |

The organization received nonmember income in 20XX in the amount \$ _____ and cell tower lease revenue in the amount of \$ _____.

The organization did not provide the substantiation of nonmember income as required by revenue procedure 71-17, therefore nonmember usage of the pool and tennis court is determined to be unrelated business income and subject to tax.

The organizations form _____ for 20xx and 20xx should be adjusted and taxable income should be increased as follows:

Form Adjustment

| | 20XX | 20XX |
|--------------------------------|------|------|
| Form | | |
| Form | | |
| Difference | | |
| Cell Tower Lease Adjustment | | |
| | | |
| Tax Rate | % | % |
| | | |
| Tax Due | | |

CONCLUSION

If revocation is not upheld, the organization form _____ for 20xx and 20xx should be adjusted and the taxable income and tax liability increased.