



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: 202221015**  
**Release Date: 5/27/2022**  
**UIL Code: 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 December, 19\_\_\_\_, is revoked.

Our adverse determination as to your exempt status was made for the following reasons: During the tax year in question, you did not qualify for exemption as a social club described in IRC Section 501(c)(7) because your gross receipts have consistently exceeded the limitation of 35%, including investment income, from sources outside of your membership.

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).

### 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

Telephone:  
Fax:

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](http://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**

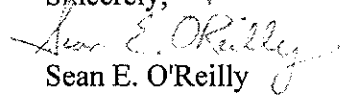
Enclosed are Publication 1, Your Rights as a Taxpayer, and Publication 594, The IRS Collection Process, for more comprehensive information.

Find tax forms or publications by visiting [www.irs.gov/forms](http://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:  
June 30, 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:

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](http://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](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,

Sean F. O'Reilly  
Director, Exempt Organizations  
Examinations

Enclosures:  
Form 886-A  
Form 6018  
Publication 892 and 3498

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

**ISSUE(S):**

Whether the \_\_\_\_\_ (“\_\_\_\_\_” or “organization”) continues to qualify for exemption from federal income tax under section 501(a) of the Internal Revenue Code (“Code”) as a social club described in Section 501(c)(7) of the Code.

**FACTS:**

\_\_\_\_\_ was incorporated under Section 402 of the Not-for-Profit Corporation Law in the State of \_\_\_\_\_ on October 10, 19\_\_\_\_\_.

The purpose of the club, as stated in the articles, is to:

- (a) Unite a group of men with the common purpose of promoting the civic, culture, intellectual, social, and charitable benefits of the community and its members.
- (b) Arrange social functions and take part in the educational activities for the teaching of the principles of brotherhood.
- (c) Promote and take part in such other social activities as will result in embracing the opportunity for social advancement and the benefit for all the members and to the organization, as like-corporations may do and in keeping with the laws provided for associations of this nature.

\_\_\_\_\_ corporate by-laws were adopted and approved by a majority vote on November 6, 19\_\_\_\_\_. No amendment has been made to the by-laws since then. Article III of the by-laws states that all members of the \_\_\_\_\_ (“\_\_\_\_\_”), in good financial standing, and those initiated after are considered members of \_\_\_\_\_.

Internal Revenue Service (“IRS”) records show that in June of 19\_\_\_\_\_, \_\_\_\_\_ filed Form 1024, Application for Recognition of Exemption under Section 501(a), requesting tax-exempt status as a social club pursuant to Section 501(c)(7) of the Code.

Per the 1024 application for recognition of Exemption, the specific purposes for which the organization was formed are as follows:

- 1) Operation of a hall used by \_\_\_\_\_ for social and business purposes;
  - 2) Rental of the hall for weddings-special functions;
  - 3) Operation of a bar for member \_\_\_\_\_;
  - 4) Collection of rent for adjacent property;
  - 5) Assisting needy of community; and
  - 6) Assembly area for \_\_\_\_\_.
- Based on the information contained in the Form 1024 application and the accompanying attachments, the IRS

<b>Form 886-A</b> (May 2017)	Department of the Treasury - Internal Revenue Service <b>Explanation of Items</b>	Schedule number or exhibit
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issued a favorable determination letter in December 19     which recognized the     as a tax-exempt social club as described in Section 501(c)(7) of the Code.

The Form 990 returns filed by     annually from 20     to 20     describe the organization's mission/purpose as "maintenance of the building and facilities of the     . Building used by members for meetings and program activities."

The examination revealed that     had owned real property that was maintained by for use by a related tax-exempt entity,     . According to     , the organization sold the real property in 20     at the behest of and to accommodate the local town which was developing a parcel of land as community green space. In exchange for selling that property,     was given a favorable lease on the property, now owned by the town.

The proceeds derived by     from the sale of its property was invested with a brokerage firm to earn investment income.     did not identify or declare this income as set aside income to be used for religious, charitable, scientific, literary, educational and other purposes specified in Section 170(c)(4) of the Code. The investment income derived from the proceeds were commingled with other funds which were not set aside.

filed Form 990-T, Exempt Organization Business Income Tax Return, with the IRS. However, the Form 990-T only reported the income or loss attributable to its interest in certain publicly traded limited partnerships. The organization did not report interest or dividends generated from stocks, bonds and other traditional investments held in the brokerage account. Based on the investment income reported on the June 30, 20     Form 990 return, the IRS initiated an examination of the Form 990 return from the prior year.

Form <b>886-A</b> (May 2017)	Department of the Treasury - Internal Revenue Service <b>Explanation of Items</b>		Schedule number or exhibit
	Name of taxpayer	Tax Identification Number (last 4 digits)  XX-XXX	Year/Period ended

The following is a summary of the revenue reported by \_\_\_\_\_ on the Form \_\_\_\_\_ and \_\_\_\_\_ returns filed with the IRS and under exam for fiscal years ending \_\_\_\_\_ and \_\_\_\_\_, respectively:

Membership Dues	\$	\$
Other Income (Bar Sales) <sup>1</sup>	\$	\$
Investment Income:	\$	\$
Interest and Dividends	\$	\$
Capital Gain <sup>2</sup>	\$	\$
Partnership (K-1 Ordinary Income/Loss) <sup>3</sup>	\$	\$
Partnership (K-1 Rents)	\$	\$
<b>Gross Receipts</b>	\$	\$
Percentage of Non-member Income	%	%

**LAW:**

Section 501(c)(7) of the Code provides for federal income tax exemption for clubs organized for pleasure, recreation, and other non-profitable purposes, or for clubs where substantially all the activities are for such purposes and no part of the net earnings inures to the benefit of any private shareholder.

The enactment of Public Law 94-568 in 1976 changed the term "exclusively" to "substantially all". This change allows for an insubstantial amount of a club's income to come from activities that do not further the club's exempt purposes. Activities which constitute an unrelated trade or business would not further the club's exempt purposes, and they include the use of the club facilities by the general public ("Non-Members").

1 For the purpose of this report, the bar sales reported by \_\_\_\_\_ is deemed to constitute member income.

2 \_\_\_\_\_ reported a gain from the sale of assets (other than inventory) on the 20 \_\_\_\_\_ fiscal year Form \_\_\_\_\_ return. During the 20 \_\_\_\_\_ fiscal year, \_\_\_\_\_ sold certain investments in securities with a gross sales price of \$ \_\_\_\_\_. However, \_\_\_\_\_ reported a loss on the sale in the amount of \$ \_\_\_\_\_. In general, capital losses from investment activities can only be used to offset capital gains from investment activities in determining nonmember income for a section 501(c)(7) social club.

3 The partnerships reported \_\_\_\_\_ unrelated business taxable income (loss) separately in section 20 (Other Information) of Schedule(s) K-1. Separately stated items of interest reported by the partnerships are included in the Interest and Dividends line shown above.

<b>Form 886-A</b> (May 2017)	Department of the Treasury - Internal Revenue Service <b>Explanation of Items</b>	Schedule number or exhibit
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Senate Report No. 94-1318 (1976), 2d Session, 1976-2 C.B. 597, at page 599 defines "substantially all." It specifies that a social club may not receive more than 35% of its gross receipts, including investment income, from sources outside of its membership in order to maintain its tax-exempt status. It also states that 35% is the overall limit and included in the 35% not more than 15% of the gross receipts can be derived from the use of a social club's facilities or services by Non-Members. The Senate Report defines the term "gross receipts" as those receipts from the traditional, normal, and usual activities of the club. Gross receipts include membership fees, dues, and assessments; charges, admissions, investment income (such as interest, dividends, rents and similar receipts) and normal recurring gains on investments.

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

Revenue Ruling 58-589, C.B. 1958-2, 266 sets forth the criteria for exemption under Section 501(c)(7) of the Code and provides 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. In this respect, statewide or nationwide organizations made up of individuals but broken up into local groups, satisfy the requirement if fellowship constitutes a material part of the activities of each local group. The requirement of individual membership derives from the requirement of personal contacts and fellowship between members. It is evident that fellowship between members cannot play a material part in the activities of an organization composed of artificial entities.

Revenue Ruling 56-305, 1956-2 C.B. 307 provides that an organization that owns and operates a building and conducts club activities for the benefit of a tax-exempt lodge may itself be exempt as a social club.

Revenue Ruling 66-149, 1966-1 C.B. 146 provides that a social club is not exempt from federal income tax under Section 501(c)(7) of the Code if it regularly derives a substantial part of its income from nonmember sources such as, for example, dividends and interest on investments which the club 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.



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Revenue Procedure 71-17, 1971 WL 26186, 1971-1 C.B. 683 sets forth guidelines for determining the effect of gross receipts derived from use of a social club's facilities by the general public 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.

While the Senate 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, in *Pittsburgh Press Club v. U.S.*, 536 F.2d 572, (1976); the Court noted certain factors to consider in determining exempt status.

Factors to consider in applying this test include:

- The actual percentage of nonmember receipts and/or investment income.
- The frequency of nonmember 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).

**TAXPAYER'S POSITION:**

agrees with the IRS position regarding the proposed revocation of the organization's tax-exempt status.

**GOVERNMENT'S POSITION:**

The facts show that was organized as a social club and has been recognized by the IRS as exempt from federal income tax under Section 501(c)(7) of the Code since . The organization was formed to own real property and operate a meeting place for the local . See Rev. Rul. 56-305.

The examination of 20 and the 20 fiscal year Form returns reveals that the organization derives no revenue from membership dues, assessments, or similar types of income. As noted above, sold real property in 20 and the proceeds were invested in

<b>Form 886-A</b> (May 2017)	Department of the Treasury - Internal Revenue Service <b>Explanation of Items</b>	Schedule number or exhibit
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stocks and securities rather than used to purchase a new clubhouse facility or set aside for charitable or other purposes specified in Section 170(c)(4) of the Code. The Form return data shows that the organization is supported primarily by investment income generated on investments in stocks, bonds, and certain publicly traded limited partnerships.

As a section 501(c)(7) social club, can receive up to 35% of its gross receipts, including investment income, from sources outside the membership without jeopardizing the organization's exempt status and not more than 15% of the total gross receipts may be derived from the use of facilities or services by Non-Members. See Senate Report No. 94-1318 (1976), 2d Session, 1976-2 C.B. 597.

To determine whether exceeded the limitation on Non-Member income one looks at investment income in proportion to gross receipts. Based on the source of income data summarized above, the IRS determined that investment income was % of gross receipts in the 20 fiscal tax year and % of gross receipts in the 20 fiscal tax year.

The investment income earned by is substantial, recurring, and routinely exceeds the non-member income limitations imposed on social clubs exempt under section 501(c)(7) of the Code. See Rev. Proc. 71-17; *Pittsburgh Press Club*, 536 F.2d 572; see also Rev. Rul. 66-149. Furthermore, the investment income effectively inures to the benefit of private members because it enables the organization to finance the organization's operations without imposing dues, fees, or other assessments on its members.

Based on the application of the law to the facts presented herein, it is the Government's position that no longer qualifies for exemption as a social club per Section 501(c)(7) of the Code.

**CONCLUSION:**

For the reasons stated above, the IRS has determined that no longer qualifies for exemption from federal income tax under section 501(c)(7) of the Code. The IRS proposes to revoke the tax-exempt status of effective July 1, 20 , the first day of the 20 fiscal tax year under examination.

Please refer to the attached 30-day letter and IRS publications for the options available to the organization including appeal rights.