



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

Date: May 28, 2021

Taxpayer ID number:

Form:

Tax periods ended:

Person to contact:

Name:

ID number:

Telephone:

Fax:

Number: 202238012
Release Date: 9/23/2022

UIL: 501.07-00

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 , 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 your members or other non-profitable purposes and no part of the earnings inures to the benefit of any 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 year ending .

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:
11/12/2020
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

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.

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,

Sean O'Reilly by lm

Sean O'Reilly

Director, Exempt Organizations Examinations

Enclosures:

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

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

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 "t

was given exemption under IRC §501(c)(7) as of

currently () has members. Annual due is \$.

operates a , a and a small shop.

operates several events throughout the year such as , Halloween Party, etc... where nonmembers are allowed to participate.

has a lease agreement with two individuals (who are also members) to let them run the independently as a for profit business. Contract started as a temporary trial before . However, according to (finance director), this has been implemented as a permanent contract since then.

\$ /month for upper level of the kitchen/dining area/balcony/restrooms and storage areas in lower level. Due is on each month.

Utilities are split % clubhouse facility at and % According to during initial interview, pays all utilities upfront and is reimbursed by .

pays the commissions for selling from the because the doesn't have license.

The terms of the contract with are as follow:

operates and manages % of the lower , which is used for special events scheduled by otherwise it is blocked off. will hire and pay staff and receives % of proceeds.

changed its status to " " so that the public can order w/o purchasing membership.

The upper level of the is operated by in conjunction with their in which

Serves Provides wait for patrons.

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

Stocks and supplies.
Maintains/cleans area.

manages the including:

Recordkeeping.

Depositing receipts.

Purchasing/reordering and supplies.

Paying wages for t from until closing on days the is open.

is responsible for maintaining the inside and outside the facility (including), landscaping, insurance, taxes and equipment owned by such as the ice machine, grill, fryer, A/C, carpet, plumbing etc...

may serve meals to participants during tournaments using the dining and area.

operates the dining and area during Nights.

provides catering for specials occasions such as Weddings/receptions/dances.

collects dues/green fees/cart rental fees for

is responsible for hiring/managing its employees, and mutually agree on the hiring of is responsible for wages for the bar from until closing on days the is open.

and share gross receipts of the , but sharing percentages left blank in contract.

and signed for
and signed for

According to , nonmembers receipts account for about % of all gross revenue.

had a small interest income from the checking accounts (\$ as reported on return for).

did not keep any records as required under Rev. Proc. 71-17 regarding nonmembers and guests use of its facility and services.

According to , does not keep separate records for transactions with nonmembers at all.

did not file Form for any income received from nonmember sources in .

has not filed its Form for .

On its return, reported \$ in member dues and \$ from all other activities.

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

Below is gross income as reported on its Form :

	<u>Per Return</u>
Member Dues	\$
Tournaments	\$
Assessments	\$
Green Fees	\$
Rental Income	\$
Investment	\$
Gross sales of inventory	\$
Reimbursement from	\$
	<u> </u>
	\$

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.

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

Rev. Proc. 71-17 describes the record-keeping requirements for social clubs exempt under IRC 501(c)(7) with respect to nonmember use of their facilities; it sets forth guidelines for determining the effect gross receipts derived by the general public have on a club's exemption from Federal Income Tax under section 501(c)(7) of the Internal Revenue Code. Revenue Procedure 71-17 also describes the records a club must maintain when nonmembers use a club's facilities and the circumstances under which a host guest relationship will be assumed, which are relevant both for purposes of determining adherence to the exemption requirements and for computing exempt function income under section 512(a)(3) of the Code.

Section 3 of Revenue Procedure 71-17 provides a set of assumptions as to the status of nonmembers using club facilities. If nonmember use can be classified into one of the assumptions listed in Revenue Procedure 71-17, then the income derived from these individuals will be income from guests and treated as if from members and therefore be classified as exempt function income. Clubs are required to provide detailed records of nonmember use to substantiate the assumptions.

Section 4 of Revenue Procedure 71-17 describes the records that a social club must maintain with respect to the assumption listed in section 3. Section 4.03 of Revenue Procedure 71-17 describes the books and records that must be maintained when the assumptions contained in Section 3.03 do not apply.

Section 4.04 of Revenue Procedure 71-17 states that failure to maintain such records or make them available to the Service for inspection will preclude use of the minimum gross receipts standard and audit assumptions set forth in this Revenue Procedure.

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 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*, T.C. 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.

TAXPAYER'S POSITION:

was given the option either to continue with exemption and file Form for all its unrelated business income beginning with going forward or to give up its exemption and file form if complying with all exemption requirements seems unfeasible for future tax years. According to the POA, , has decided to give up its exemption and will file form beginning with tax year .

GOVERNMENT'S POSITION:

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

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

Outside of membership dues, [redacted] has substantial financial transactions with nonmembers in all of its activities. [redacted] receives monthly rental income from [redacted] derives income indirectly from the sales of its inventory to nonmembers through [redacted] also receives income from nonmembers via its retail shop, the lower [redacted] and access to its [redacted] and events.

Even though there is a significant amount of evidence to indicate that nonmembers involve in practically all of [redacted] activities, yet it does not keep adequate books & records as required under Rev. Proc. 71-17. In fact, [redacted] has no books and records to substantiate any host-guest relationship and does not even keep separate receipts from nonmembers. Failure to keep adequate records under Rev. Proc. 71-17 means income derived from activities that involved nonmembers are treated as nonexempt function income. In this case, except for member dues of \$ [redacted] all of its other receipts, \$ [redacted] can be considered nonmember income.

Although unverifiable, even if [redacted] claims that about [redacted] % of [redacted] receipts comes from nonmember is accurate, this amount is still well above the [redacted] % limit under Public Law 94-568. Substantial and recurring income received from nonmember sources show that [redacted] is not operated exclusively for pleasure, recreation and other nonprofit purposes.

CONCLUSION:

[redacted] is not operated exclusively for pleasure, recreation and other nonprofit purposes required under Treasury Regulation §1.501(c)(7)-1(a) because a significant portion of its income is derived from nonmembers use of its facility and services. Income from nonmember sources is substantial, recurring and do not further [redacted] exempt purposes. Even by its own estimate, annual nonmember income surpasses the maximum level of 15% of total gross receipts allowed under P.L. 94-568. Consequently, [redacted] exemption under IRC 501(c)(7) should be revoked as of [redacted] must file Form 1120 , *U.S. Corporation Income Tax Return* instead of [redacted] beginning with tax year [redacted] going forward.

According to the POA, [redacted] has agreed to give up its exemption voluntarily and will file Form [redacted] to report its income for [redacted] and all future years.