



Department of the Treasury Internal  
Revenue Service  
Tax Exempt and Government Entities  
PO Box 2508  
Cincinnati, OH 4520

Date:  
02/27/2023  
Employer ID number:

Form you must file:  
Form 1120  
Tax years:  
All  
Person to contact:

Release Number: 202321015  
Release Date: 5/26/2023  
UIL Code: 501.04-00,  
501.04-07

Dear :

This letter is our 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)(4). Recently, we sent you a proposed adverse determination in response to your application. The proposed adverse determination explained the facts, law, and basis for our conclusion, and it gave you 30 days to file a protest. Because we didn't receive a protest within the required 30 days, the proposed determination is now final.

You must file the federal income tax forms for the tax years shown above within **30 days** from the date of this letter unless you request an extension of time to file. For further instructions, forms, and information, visit [www.irs.gov](http://www.irs.gov).

We'll make this final adverse determination letter and the proposed adverse determination letter available for public inspection after deleting certain identifying information, as required by IRC Section 6110. Read the enclosed Letter 437, Notice of Intention to Disclose - Rulings, and review the two attached letters that show our proposed deletions. If you disagree with our proposed deletions, follow the instructions in the Letter 437 on how to notify us. If you agree with our deletions, you don't need to take any further action.

If you have questions about this letter, you can call the contact person shown above. If you have questions about your federal income tax status and responsibilities, call our customer service number at 800-829-1040 (TTY 800-829-4933 for deaf or hard of hearing) or customer service for businesses at 800-829-4933.

Sincerely,

Stephen A. Martin  
Director, Exempt Organizations  
Rulings and Agreements

Enclosures:  
Letter 437  
Redacted Letter 4034  
Redacted Letter 4038



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

**Date:** September 6, 2022

**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](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,

Lynn A. Brinkley  
Acting Director, Exempt Organizations  
Examinations

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

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

**ISSUE**

Whether the \_\_\_\_\_ qualifies for exemption under IRC § 501(c)(7)?

**FACTS**

The \_\_\_\_\_ is currently recognized as an exempt organization described in IRC § 501(c)(7) to provide social, recreational and other activities to its members. The benefits provided to the members include, but are not limited to, the following activities as reported by the organization:

- During the interview:
  
- In written statement sent as IDR response:

On the original Articles of Incorporation filed on \_\_\_\_\_, with the \_\_\_\_\_, the purpose was as follows:

"The specific purpose of this corporation is to provide activities for the recreation and pleasures of senior citizens, and other related activities under Revenue and Taxation Code Section 23701g and Internal Revenue Code Section 501 (c) (7)."

Later the organization's purpose was amended on \_\_\_\_\_, to include:

"This corporation is a nonprofit mutual benefit corporation organized under the Nonprofit Mutual Benefit Corporation Law. The purpose of this corporation is to engage in any lawful act or activity for which a corporation may be organized under such law."

The \_\_\_\_\_ received its determination letter providing the organization tax exemption on \_\_\_\_\_, based on the information on the Form 1024. The letter stated the requirements for maintaining that tax exemption as a section 501(c)(7) entity.

The organization reported the following sources and amounts of revenue on \_\_\_\_\_ for the year ending \_\_\_\_\_:

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End of Year

**Gross Receipts**

Membership Dues and Assessments

Interest on savings and investments

Other Revenue

**Total Nonmember & Investment Income**

**Total Income**

\_\_\_\_\_ .  
=====

**Member Gross Receipts from Dues or Member Revenue**

%

**Nonmember Gross Receipts**

%

While reviewing the \_\_\_\_\_ and internal documents provided by the organization, such as monthly bank statements, answers during the interview held on \_\_\_\_\_, and written answers provided on \_\_\_\_\_ via fax, it has been noted that the organization did not provide a break down between member and nonmember income. The nonmember income has not been recorded in the \_\_\_\_\_. There were no accounting records provided - only the monthly bank statements. The monthly bank statements provided by the Organization for the calendar year of \_\_\_\_\_ came from this bank account:

The account number shows the same on all documents provided as seen above with the x's and the last four digits of the account. The organization did not provide the full account number, but the banking statements looked as if they came from the original documents the organization received from the bank on a monthly basis.

From a written answer, in an answer to IDR #2 on a fax on \_\_\_\_\_ :

"No membership fee collected. No actual or particular members. People cannot afford those. They just want a place to gather and "gossip".

"

Income came in from the use the facilities for gatherings such as \_\_\_\_\_

There are no records as to what income came from members and what income came from non-members. There was no membership roster provided. During the interview the organization stated that senior members typically visiting the facility were in the range between \_\_\_\_\_ to \_\_\_\_\_ in number of people that consistently visited the facilities. The organization also stated during the interview some of the "members" had passed away, so group became smaller since inception in \_\_\_\_\_.

There are three facts for this organization:

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- 1) The organization does not have revenue coming from members because it does not collect either membership fees or any membership assessments. No membership roster was provided by the organization for the exam year or the current year.
- 2) The organization did not have any records to show a system for allowing only members access to the organization's facility and to exclude nonmembers. There are no sign-in sheets, cards/keys for members or other measures used by 501(c)(7) organizations to exclude nonmembers from coming into the organization's facility. The organization also does not have a system to have members bring in guests on to the premises.
- 3) The organization did not have records showing what events took place and who was in attendance. There was no calendar of events or any documentation of the activities that they provided.

All of the transactions are said to have been made in cash.

The organization filed a \_\_\_\_\_ for the year ended on \_\_\_\_\_ and did not file a \_\_\_\_\_

The organization was honest about saying that the people it served did not pay membership dues or assessments. There is no information on the number of people using the facilities. During the interview, the main income was stated to be coming in from games, but details on the amount of people or how much they typically spent were not documented. They said they had coffee and donuts sometimes, but it was part of what people brought in. Also, among the written answers it says, "people cannot afford [membership fees]" because "these are seniors receiving their social security checks from retirement and could not afford membership fees.

The organization just did not document the information necessary to fulfill the documentation requirements of a 501(c)(7) organization.

## LAW

### Membership

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

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club that has non-member income and/or investments has to meet the nonmember gross receipts or income limitations set by Congress which is a maximum of 35% of gross receipts.

Prior to its amendment in 1976, IRC § 501(c)(7) required that social clubs be operated exclusively for pleasure, recreation and other nonprofitable 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:

(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.

(c) In addition, the Committee Reports state that where a club receives unusual amounts of income, such as from the sale of its clubhouse or similar facilities, that income is not to be included in the 35 percent formula.

(d) The Senate report also indicates that even though gross receipts from the general public exceed this standard, it does not necessarily establish that there is a nonexempt purpose. A conclusion that there is a nonexempt purpose will be based on all the facts and circumstances including, but not limited to, the gross receipts factor.

Revenue Ruling 58-589 sets forth the criteria for exemption under section 501 (c)(7) of the Code and provides that a club must have an established membership of individuals, personal contacts, and fellowship. It also provides that, while the regulations indicate that a club may lose its exemption if it makes its facilities available to the general public, this does not mean that any dealings with nonmembers will automatically cause a club to lose its exemption. A club may receive some income from the general public, that is persons other than members and their bona fide guests or permit the general public to participate in its affairs, provided that such participation is incidental to and in furtherance of the club's exempt purposes, such dealings with the general public and the receipt of income therefrom does not indicate the existence of a club purpose to make a profit, and the income does not inure to club members.

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. The statute contemplates that clubs falling within the scope of section 501(c)(7) of the Code are designed primarily to provide for the pleasure and recreation of members. These activities may be



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supported by funds obtained from members, such as dues, assessments, and payment for the use of club facilities. However, to the extent that income is derived from nonmember sources, it inures to the benefit of the members. If such activities are other than incidental, trivial, or nonrecurrent, it is considered that they are intended to produce income and are reflective of a purpose inconsistent with exemption under section 501(c)(7) of the Code.

Revenue Ruling 68-119 provides that a club will not necessarily lose its exemption if it derives income from transactions with other than bona fide members and their guests, or if the general public on occasion is permitted to participate in its affairs, provided such participation is incidental to and in furtherance of its general club purposes and the income therefrom does not inure to members.

Revenue Ruling 60-324 provides that a social club that made its social facilities available to the general public through its member-sponsorship arrangement cannot be treated as being operated exclusively for pleasure, recreation, or other nonprofitable purposes and the club no longer qualified for exemption under 501 (c)(7) of the Code.

Revenue Procedure 71-17 sets forth guidelines for determining the effect of gross receipts derived from nonmember use of a social club's facilities on exemption under Internal Revenue Code Section 501 (c)(7) and recordkeeping requirements. Revenue Procedure 71-17 requires section 501 (c)(7) organizations to substantiate the status of individuals that use the organization's facility as either member or non-member. For groups of eight (8) people or less, the presumption is that the non-members in that party are guests of the member provided the member or the member's employer pays for such use of the facility. For groups larger than eight (8) persons, the organization can substantiate the status of the non-members as guests if records are kept that show that seventy-five percent (75%) or more of the persons in such a group are members and that a member or the member's employer pays for such use of the facility. In either of these circumstances described above, the activities involving the individuals is considered to be an exempt social function carried on by the club, and the income derived by the club for the entertainment of non-members as bona fide guests of members is not unrelated business income. However, if the club fails to maintain these records and cannot show that the conditions set forth above have been met, all such income derived by the club is assumed to be non-member income; this income is subject to taxation as unrelated business income and is not considered exempt function income.

### Inadequate Records

IRC § 6001 provides that every person liable for any tax imposed by the IRC, or for the collection thereof, shall keep adequate records as the Secretary of the Treasury or his delegate may from time to time prescribe.

IRC § 6033(a)(1) provides, except as provided in IRC § 6033(a)(2), every organization exempt from tax under section 501(a) shall file an annual return, stating specifically the items of gross

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income, receipts and disbursements, and such other information for the purposes of carrying out the internal revenue laws as the Secretary may by forms or regulations prescribe, and keep such records, render under oath such statements, make such other returns, and comply with such rules and regulations as the Secretary may from time to time prescribe.

Treas. Reg. § 1.6001-1(a) in conjunction with Treas. Reg. § 1.6001-1(c) provides that every organization exempt from tax under IRC § 501(a) and subject to the tax imposed by IRC § 511 on its unrelated business income must keep such permanent books or accounts or records, including inventories, as are sufficient to establish the amount of gross income, deduction, credits, or other matters required to be shown by such person in any return of such tax. Such organization shall also keep such books and records as are required to substantiate the information required by IRC § 6033.

Treas. Reg. § 1.6001-1(e) states that the books or records required by this section shall be kept at all times available for inspection by authorized internal revenue officers or employees; and shall be retained as long as the contents thereof may be material in the administration of any internal revenue law.

Treas. Reg § 1.6033-1(h)(2) provides that every organization which has established its right to exemption from tax, whether or not it is required to file an annual return of information, shall submit such additional information as may be required by the district director for the purpose of enabling him to inquire further into its exempt status and to administer the provisions of subchapter F (section 501 and the following), chapter 1 of the Code and IRC § 6033.

*Rev. Rul. 59-95, 1959-1 C.B. 627*, concerns an exempt organization that was requested to produce a financial statement and statement of its operations for a certain year. However, its records were so incomplete that the organization was unable to furnish such statements. The Service held that the failure or inability to file the required information return or otherwise to comply with the provisions of IRC § 6033 and the regulations which implement it, may result in the termination of the exempt status of an organization previously held exempt, on the grounds that the organization has not established that it is observing the conditions required for the continuation of exempt status.

## **TAXPAYER'S POSITION**

Taxpayer's position has not been provided from this report. However, a partial statement from the organization during the examination is that they did not want to charge membership fees, would close down the 501(c)(7) and

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## GOVERNMENT'S POSITION

Based on the examination, the organization does not qualify for exemption as a social club described in IRC §501(c)(7) and Treas. Reg. §1.501(c)(7), which provide that in general, this exemption extends to social and recreation clubs which are supported solely by membership fees, dues, and assessments.

Since the organization does not charge any membership dues or assessments, it does not fulfill the requirements and the limitation on non-member income for 501(c)(7) organizations. The Organization exceeded the 35% non-member gross receipts limitation as outlined in Public Law 94-568, on a recurring basis during the tax year under examination ending . The Organization has a small . facility with a commercial lease, so only 15% of gross receipts could come from non-member use of this space. However, there are no records and they stated during the interview that there are about people that typically gathered on a consistent regular basis. This number of people would have to donate, contribute or buy enough merchandise from the club of to generate about \$ per member per month. Although they stated they were all retired receiving social security checks and could not afford a membership. The president of the club stated that they wouldn't pay for a membership, because they could not afford it on their limited budgets. The organization did not provide a membership roster to date or distinguish between member and non-member incomes. There were no records or a statement that said how they prevented non-members from coming into their club facilities. The Organization also did not file a for the year ended .

If there are no records to keep track of member vs. non-member income. This organization is like the one referenced in Rev. Rul. 59-95, in that the social club did not keep detailed enough records to show that only members (or mostly members) contributed to the pooling of resources such as a 501(c)(7) social club is supposed to maintain.

There are also requirements when there is use of facilities by members when there is a party that at least 75% of attendees would have to be members. But there are no records on that instances when the facilities were used in such a manner.

Accordingly, it is proposed that the tax- exempt status be revoked effective

## CONCLUSION

The reason why the no longer qualifies for exemption under § 501(c)(7) of the Code is that the organization has not kept appropriate records and since there are no distinctions on nonmember income and member income, all income has to be classified as the nonmember income and has exceeded the 35% nonmember limits on a continuing basis. Therefore, it is proposed that its exempt status under § 501(c)(7) of the Code be revoked effective

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Should this revocation be upheld, must be filed starting with tax periods ending