



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

501.19-00

Date: March 14, 2011

Release Number: **201123040**

Release Date: 6/10/2011

LEGEND

ORG - Organization name

XX = Date Address = address

ORG

ADDRESS

Date:

Employer Identification Number:

Person to Contact/ID Number:

Contact Numbers:

Voice:

Fax:

CERTIFIED MAIL – RETURN RECEIPT REQUESTED

Dear

In a determination letter dated November 16, 19XX you were held to be exempt from Federal income tax under section 501(c)(19) of the Internal Revenue Code (the "Code") as a subordinate organization to the ORG pursuant to a group ruling, Group Exemption Number 9509.

Based on recent information received, we have determined you have not operated in accordance with the provisions of section 501(c)(19) of the Code. Accordingly, your exemption from Federal income tax is revoked effective January 1, 20XX. This is a final adverse determination letter with regard to your status under section 501(c)(19) of the Code.

We previously provided you a report of examination explaining why we believe revocation of your exempt status is necessary. At that time, we informed you of your right to contact the Taxpayer Advocate, as well as your appeal rights. On March 1, 20XX, you signed Form 6018-A, *Consent to Proposed Action*, agreeing to the revocation of your exempt status under section 501(c)(19) of the Code.

As a taxable entity, you are required to file Form[s] 1120, *U.S. Corporate Income Tax Return*, with the appropriate service center indicated in the instructions for the return.

You have the right to contact the Office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal Appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or

extend the time fixed by law that you have to file a petition in a United States 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 may call toll-free, 1-877-777-4778, and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

If you have any questions, please contact the person whose name and telephone number are shown at the beginning of this letter.

Sincerely,

Nanette M. Downing
Director, EO Examinations



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY

Internal Revenue Service
1122 Town & Country Commons Drive
Attention:TE:GE:EO:7956AS
Chesterfield, MO 63017

January 29, 2010

ORG
ADDRESS

Taxpayer Identification Number:

Form:

Tax Year(s) Ended:

Person to Contact/ID Number:

Contact Numbers:

Telephone:

Fax:

CERTIFIED MAIL – RETURN RECEIPT REQUESTED

Dear

We have enclosed a copy of our report of examination explaining why we believe an adjustment of your organization's exempt status is necessary.

If you do not agree with our position you may appeal your case. The enclosed Publication 3498, *The Examination Process*, explains how to appeal an Internal Revenue Service (IRS) decision. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process.

If you request a conference, we will forward your written statement of protest to the Appeals Office and they will contact you. For your convenience, an envelope is enclosed.

If you and Appeals do not agree on some or all of the issues after your Appeals conference, or if you do not request an Appeals conference, you may file suit in United States Tax Court, the United States Court of Federal Claims, or United States District Court, after satisfying procedural and jurisdictional requirements as described in Publication 3498.

You may also request that we refer this matter for technical advice as explained in Publication 892, *Exempt Organization Appeal Procedures for Unagreed Issues*. If a determination letter is issued to you based on technical advice, no further administrative appeal is available to you within the IRS on the issue that was the subject of the technical advice.

If you accept our findings, please sign and return the enclosed Form 6018, *Consent to Proposed Adverse Action*. We will then send you a final letter modifying or revoking exempt status. If we do not hear from you within 30 days from the date of this letter, we will process your case on the basis of the recommendations shown in the report of examination and this letter will become final. In that event, you will be required to file Federal income tax returns for the tax period(s) shown above. File these returns with the Ogden Service Center within 60 days from the date of this letter, unless a request for an extension of time is granted. File returns for later tax years with the appropriate service center indicated in the instructions for those returns.

You have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States 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 may call toll-free 1-877-777-4778 and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

If you have any questions, please call the contact person at the telephone number shown in the heading of this letter. If you write, please provide a telephone number and the most convenient time to call if we need to contact you.

Thank you for your cooperation.

Sincerely,

Nanette M. Downing
Acting Director, EO Examinations

Enclosures:
Publication 892
Publication 3498
Form 6018
Report of Examination
Envelope

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit: Form 6018-A
Name of Taxpayer ORG		Year/Period Ended 12/31/20XX 12/31/20XX

LEGEND

ORG = Organization name XX = Date Address = address City - city
State = state CPA = CPA Agent = agent RA-1, RA-2 & RA-3 = 1ST, 2ND
& 3RD RA CO-1 THROUGH CO-8 = 1ST THROUGH 8TH COMPANIES BM-1 THROUGH BM-9
= 1ST THROUGH 8TH BM

ISSUES

Issue 1

Whether ORG ("ORG"), doing business as "CO-1", meets the requirements for exemption under section 501(c)(19) of the Internal Revenue Code ("IRC")

Issue 2

Whether ORG operated exclusively for purposes listed in Treas. Reg. § 1.501(c)(19)-1(c).

FACTS

Background Information

ORG is a veterans organization that holds a group exemption for veterans organizations described in I.R.C. § 501(c)(19). Hereinafter, ORG will be referred to as "CO-2". CO-2 web page states that its mission is to "

."

CO-2 website lists several advantages to be included in its group exemption as a subordinate organization. These advantages include selling liquor, operating on Sundays, holding bingo games, and obtaining liquor licenses in dry counties. CO-2 website markets the ORG Organization and its group exemption to existing bars and restaurants located in State as a way to avoid restrictive local liquor laws and as a way to operate on a tax-exempt basis. CO-2 website states that it will assist in a club's formation and application for a liquor license. CO-2 refers to its subordinate organizations as "clubs."

CO-2 website requires that its clubs have at least 10 veteran members. It also requires its subordinate organizations to send it proof of all veteran affiliation. One question that appears on CO-2 web page is "do I have to be a member's only club?" The response is "[a]lthough the tax advantages of being a members only club are greater, we do not require you to limit your bar to members.....Your doors may be kept open. By incorporating separately, you keep control of your own club. It is your choice if you wish to keep your doors open or closed. We only ask that you honor members of other chapters."

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ORG's Formation and Purpose

ORG, doing business as "CO-1", was incorporated by BM-1 and BM-2. According to ORG's Articles of Incorporation, dated April 23 20XX, the corporation was formed to unite veterans and their families with other veteran families. The Articles further provide ORG is a membership organization. In the event of dissolution, the assets of the corporation will be distributed to other war veteran organizations covered under Section 501(c)(19) of the Internal Revenue Code.

ORG is a subordinate organization of CO-2 effective October 20XX.

ORG's governing documents include the "ORG Constitution and By Laws" a governing instrument provided to it by CO-2.

According to Section III of the "Bylaws for ORG Corporations", ORG's stated purpose is: "

. " These purposes include, but are not limited, to the following:

- A. Helping fellow veterans and their families receive the benefits for which they are entitled;
- B. Finding employment for veterans and their families;
- C. Helping the homeless veterans find housing and re-adjust to civilian life;
- D. Carrying on programs to perpetuate the memory of deceased veterans and members of the armed forces, and to comfort their survivors;
- E. Sponsoring or participating in activities of a patriotic nature;
- F. Providing social and recreational activities for its members;
- G. Assisting the disabled and needy war veterans and their dependents;
- H. Promoting awareness of the prisoners of war and the missing in action issues;
- I. Promoting the general welfare and prosperity of all ORG corporations; and
- J. Presenting and supporting the purposes of ORG before the public and the government.

According to Corporate Annual Registration Reports filed by ORG between June 27, 20XX and July 21, 20XX with the State Secretary of State, Officers and Board Members of the corporation are as follows:

	20XX	20XX	20XX	20XX
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President	BM-1	BM-1	BM-1	BM-1
Vice-President	BM-3	None Named	None Named	BM-4
Secretary	BM-5 ¹	None Named	None Named	BM-3
Treasurer	BM-5	None Named	None Named	None Named
Board Member	BM-1	BM-1	BM-1	BM-1
Board Member	BM-3	BM-3	BM-3	BM-3
Board Member	BM-5	BM-5	BM-5	BM-5

The corporation's current registered agent is BM-1, Address, City, State.

ORG's Business Operations, Business Activities, and Members

History and Background

An operational interview was conducted with BM-1, BM-3, and CPA on October 21, 20XX. CPA has been designated by the corporation as its authorized representative for the purpose of the examination by execution of Form 2848 "Power of Attorney and Declaration of Representative" signed by BM-1 on October 20, 20XX. Form 8821 "Tax Information Authorization" was also signed by BM-1 on October 17, 20XX authorizing BM-3 to inspect and receive confidential tax information for tax matters related to this examination.

The operational interview revealed that CO-1 is the first bar owned by BM-1. BM-1 purchased the bar as a means to supplement his retirement income. When he purchased the bar, it was a "CO-3" organization (an organization exempt under Section 501(c)(10) of the Internal Revenue Code). The previous owner of the bar, BM-6, and BM-1 met and the topic of purchasing the bar came up in conversation. There is no mortgage on the property. BM-1 made the purchase by making monthly payments to the previous owner. BM-1 does not have the purchase agreement related to the sale/purchase, however he did provide the Deed of Release (Full) showing the release

* * * *

¹ The Annual Registration Report dated July 24, 20XX "Statement of Correction", provides that the authorized officer for signatory purposes is BM-7, Title of Secretary.

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of the property effective October 8, 20XX pursuant to Deed of Trust entered into by the parties (BM-6 and BM-1). The Deed of Trust is dated April 19, 20XX.

BM-1 provided that while CO-1 was operating as a CO-3 organization when he purchased it, the previous owner owed such a substantial debt to the CO-3 Parent organization, that BM-1 said he had to convert to ORG. All of the paperwork associated with converting the bar to a ORG as a subordinate organization, e.g. the application for membership to ORG, the Articles of Incorporation, and the application for the liquor license, was completed by BM-1's then girlfriend. BM-1 is unaware of the former girlfriend's current whereabouts. He did not maintain copies of any of the paperwork related to applying for membership in the ORG.

The former girlfriend obtained the original liquor license. It was later transferred to BM-1's name. CPA responding to questions regarding encumbrances on liquor licenses, such as licenses being only offered to charities, and/or have limitations with regard to package liquor sales, offered that distributors sell to bars at higher prices than they do convenience stores. The bar may sell "liquor to go"; however they do not do so very often. When they do it is usually after "last call". They do not do so often, as it encourages drinking and driving. Liquor licenses are not available to "for-profit" establishments without the sale of food. The establishment, to qualify, must have a full kitchen and a full menu. BM-8 advised that the rule is relaxed for exempt organizations, as for example, ORG CO-1 does not have a full kitchen or menu.

BM-1 provided that his understanding of the requirements for operating as an organization exempt under IRC § 501(c)(19) means he has to operate the corporation as a membership organization, similar to the CO-4. His understanding of the benefits of being affiliated with the ORG Organization is:

- Socialization
- Conventions
- Networking
- Meet Other Veterans
- Newsletter Subscription

CO-2 advised about the Form 990 filing requirement. In fact, they "filled out" the first few Form 990s for the corporation the first few years. BM-1 does not believe there was a charge for the service. In 20XX or 20XX, the corporation hired an accounting service to prepare its Form 990s. It continues to use an independent accounting service to prepare the information returns.

BM-1 has not been involved with any Exempt Organizations previously as a volunteer, employee, owner, or administrator. He does however have experience as a commercial

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business owner. He owns CO-5. BM-1 is a High School graduate. He also completed a 5 year apprenticeship with the plumber's local.

Facility

ORG's primary activity is running a bar. ORG operates its business, on a cash basis (i.e., it only took cash and no credit card payments). CO-1 d/b/a "CO-1" is located at Address, City, State. The building's facade exhibits signs reflecting the names "ORG" and "CO-1". Nothing on the building's façade provides for it being a "members only" or even a "member" facility. The facility consists of approximately 800 - 1,000 sq. ft. of space, which includes a full service bar.

Assets identified within the facility are a newer flat screen 19" color television, another standard television about 19", two commercial hotplates or portable stoves; one small microwave; a bar; 15 bar stools; 4 tables with about three chairs each; two coin operated pool tables, a beer cooler, refrigerator, electronic dart machine, pinball type gaming machine; juke box; 2 dorm size refrigerators; another commercial cooler; a chest freezer, cash register, a multiple video gaming unit, miscellaneous neon liquor signs, and a coffee pot. All of the assets are located in the bar area. There is a store room for inventory, and two restrooms. There are chips hanging behind the bar. Miscellaneous photographs of bar patrons, and sport team schedule, e.g. KC Chiefs football team.

ORG's hours of operation are 9 a.m. to 1 a.m. Monday through Saturday. Sunday bar hours are 11 a.m. to 12 p.m. ORG is open to members and nonmembers (i.e., the general public). Patronage of the facility varies by day of week, time of year, and weather. Since the variables are so great the corporation is not able to provide an estimate of the number of customers it serves daily. It does not maintain a log or "sign in" sheet to gauge its patronage by the general public.

Membership

The organization considers a veteran, his/her spouse, and their children over 21 to be eligible members. Other relatives, such as grand children, parents, cousins, aunts, and uncles are not eligible. The corporation, to confirm its membership, provided a member roster containing ten (10) names, Exhibit A. The member roster was faxed over from CO-2 on October 17, 20XX according to the facsimile stamp. None of the corporation's officers are included in the member roster including BM-8 and BM-1, who both claim to be members. BM-8 advised that it is probably because the list has not been updated. Noting the member list only has ten names on it, BM-8 advised that her recent check

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(October 17, 20XX) with CO-2 provided ORG actually has 19 members despite there only being ten names on the list.

The corporation provided membership cards for the ten people on the member list, Exhibit B. The cards were sent pursuant to the request for a member roster, and were forwarded to ORG by postal mail subsequent to that request according to BM-8. Noting the corporation and not the *member* is in possession of the membership card, BM-8 advised ORG's recordkeeping requires it to keep a duplicate of the membership cards, and since the cards presented were the only ones the ORG Parent sent, the corporation kept them. The cards correspond to the names on the member roster. BM-8's attempts to contact the organization to secure an updated member roster from CO-2 during the field visit were unsuccessful. However, in response to an Information Document Request (IDR) dated October 27, 20XX, Exhibit C, BM-8 provided a written statement "BM-3 called _____ – They did not respond. On November 6, 20XX, she called ORG again; they told her that they did not fax 20XX & 20XX rosters because they are the same as the 20XX roster".

The corporation provided that other applications for becoming members of ORG are pending submission to CO-2. Noting that BM-8's is one of the pending applications, she was asked if she had only just become a member. BM-8 responded that she and her husband became members of ORG when the organization converted from a CO-3 to ORG. She could not explain why she and her husband's names are not on the member roster, but since they aren't they just re-applied. BM-8-9 membership applications are dated August 25, 20XX, Exhibit D. Noting all of the applications are dated beginning the end of August through the beginning of September 20XX, BM-8 advised that she just started signing people up because of a letter from CO-2 to start signing more people up. The corporation was unable to produce such a letter. Additionally, neither BM-8 nor BM-1 are veterans, however BM-8 pointed out that her husband is a veteran. There is no application for membership pending for BM-1.

There are no separate levels of membership. New applications and a membership "joining fee" of \$ are forwarded to CO-2. Members are required to pay their own joining fee. The corporation provided there is no annual membership fee or dues. Recruitment for new members is accomplished by signs in the bar "Open Enrollment for ORG." Permanent membership cards are issued by CO-2. Until the permanent membership card is issued, a part of the application for membership form serves as a temporary membership form. All of the "pending" applications are in tact, i.e. the portion to serve as a temporary membership card is still attached.

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The corporation assumes that Veteran status and period of active duty service is confirmed by CO-2 based on the DD 214 information provided in the application. ORG does not confirm such status and length of service.

ORG does not have a sign-in book for members or nonmembers to sign when they use the organization's facilities; however, the corporation maintains one of the advantages of being a member of ORG is the discounted liquor prices, although members and nonmembers pay the same price for food. Members of other ORG Chapters are afforded the same benefits as ORG's members. The corporation maintains the revenue from such sales is as well considered in member receipts.

The corporation provided its current pricing list, Exhibit E and the pricing list in effect during 20XX and 20XX, Exhibit F. No separate liquor prices are noted for members.

Operations and Activities

The bar is operated by volunteers. Volunteers are BM-5, RA-1, and RA-2 occasionally. All tend bar. They receive tips only, no wages according to persons interviewed. The corporation does not track the tips. BM-9 is at the bar on Saturdays and every other Sunday and Thursday. RA-3 is the only employee currently. He formerly worked for the organization as a volunteer. The week of October 13, 20XX was his second week on payroll. RA-3 was put on the corporation's payroll to provide record of earned income in order for RA-3 to claim dependent exemptions for his children. He works on Monday, Wednesday, Friday, Saturday, and Sunday nights from 5:30 pm until close. All other times either BM-4 or BM-3 is there.

BM-8 is also at the bar in the mornings from 7:30 until about 9:30 to set things up for the day. She remains at the bar until Wendy or whoever is working that day comes in to work. Tables are waited and food is prepared by the Bartender on duty. This person is also responsible for clean up.

BM-1 stated he receives little to no compensation. Rather, receipts are put back into the building and operations. He no longer considers the corporation a retirement investment as "it is more trouble than anything".

During the operational interview, the corporation, when describing member benefits, provided its activities consist of fundraiser events, sending care packages to soldiers overseas, and social activities such as the annual fish fry when dinner is prepared for ORG's members and their families. Flags are placed on the graves of local veterans on Veteran's Day. The corporation maintains it has an ongoing outreach to active duty soldiers, sending them care packages 3 – 4 times per year, providing as evidence a flag

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and plaque signed by the soldiers of a troop currently serving in Iraq as their thanks for its support. Upon further inquiries and observations, the corporation provided one of the troop's members is a relative of BM-3.

ORG holds its Board of Directors' meetings every three months. The corporation provided during the operational interview that attendees used to be BM-5, BM-3, and BM-1, however currently meetings are attended by only BM-8 and BM-1.

Meeting minutes for Board meetings held from January 20XX through July 20XX were provided for review. The minutes of the 20XX, 20XX, and 20XX meetings are Exhibit G. The minutes provide no specific dates, and do not provide any detail with regard to attendees. As well they are not signed by any Officer or member of the Board. They provide the corporation's activities were as follows:

Date of Minutes	Activity	Date of Activity
January 20XX	Chili Cook Off (Proceeds to "Meals on Wheels")	January 13, 20XX
April 20XX	9 Ball Tournament (Proceeds to "CO-6")	May 12, 20XX
July 20XX	CO-7 (Proceeds to "CO-8")	July 14, 20XX
October 20XX	Annual Fish Fry	November 12, 20XX
October 20XX	Annual Fish Fry	None provided. ²
January 20XX	Annual Chili Cook Off (Proceeds to "Meals on Wheels")	January 20, 20XX
April 20XX	9 Ball Tournament (Proceeds to "CO-8")	April 14, 20XX
July 20XX	Pitch Tournament (Proceeds to be spent on Flags to be placed on graves in 20XX)	July 14, 20XX
October 20XX	Annual Fish Fry and Adopting 3 Veterans for Christmas	October 13, 20XX
January 20XX	Annual Chili Cook Off (Proceeds to "Meals on Wheels")	January 12, 20XX
April 20XX	Planning and organization of disbursing flags at local cemeteries in honor of Veterans.	None provided.
July 20XX	Pitch Tournament (Proceeds split between flags and Adopt a Veteran at Christmas)	July 19, 20XX

ORG's Financial Information

* * * *

² The organization presented two Meeting Minutes dated October 20XX. There is no indication as to whether one is a continuation, correction, etc. of the other.

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Information obtained from BM-1 and BM-3 during the initial telephone contact with the corporation on October 1, 20XX includes the following:

- BM-3 is the bar manager. She prepares a spreadsheet monthly detailing the revenue and expenses of the organization using an Excel program set up by her daughter. The detail is prepared on her home computer and the spreadsheets, along with bank statements, which are reconciled monthly, are maintained in her home. It is the documentation that is provided to the return preparer for preparation of the Form 990 and the employment tax returns. The organization does not receive cancelled checks, however there are copies provided with the bank statements.
- BM-8's spreadsheet identifies receipts that are from members. Member receipts are identified by using a special key on the cash register. The member identifies him or herself by their identification card, or face recognition because of their frequent visits to the establishment. BM-8's spreadsheet further breaks the receipts down by source, for example: cigarettes, beer, food and liquor; and payment type, cash or checks.
- Supporting documentation, e.g. receipts, invoices, cash register receipts, etc. that support the spreadsheet are given to BM-1.
- The corporation is also required to file sales tax returns with the state. The returns are also in the possession of BM-1.

With regard to the sales tax returns, the corporation provided during the operational interview that sales tax is paid on all receipts including member receipts. The corporation was advised by CO-2 of a requirement to keep a separate accounting of member and non-member receipts; however neither BM-1 nor BM-8 understand the purpose of such accounting. Additionally, neither BM-1 or BM-8 knows whether or not the receipts reported on Form 990 include revenue from both member and non-member sources. Neither is aware of a requirement to file Form 990-T to accommodate tax liabilities associated with non-member receipts.

Additional information provided includes the following:

- Fundraisers are used to buy items for care packages sent to active duty military troops, and to accommodate related mailing costs.
- Some of the corporation's revenues are donated to charitable organizations such as the Cancer Foundation (in the name of veterans affected by cancer), and Meals on Wheels, as some veterans in town use the service.
- Fundraiser and special event revenue is deposited with general receipts.
- Cash receipts are deposited into the organization's bank account every week (Monday). Until they are deposited, they are locked in a cabinet in BM-8's

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house. The corporation has no procedure to cross check the weekly receipts tally with receipts deposited.

- BM-1 has check writing authority. BM-8 has a signature stamp to use in lieu of BM-1's actual signature.
- BM-1 is not required to review checks, invoices, or other billings against payment made.
- Cash expenditures are recorded in BM-8's spreadsheet and receipts for such are maintained by the corporation.
- There is no formal or official petty cash fund. Cash purchases are taken from the cash register.
- To account for inventory on hand, BM-8 said she keeps a clipboard in the store room where anyone taking anything out is required to log it off the clipboard, so she knows at all times exactly what is in the store room. She does not know whether the beginning or ending inventory is included in the preparer's Cost of Goods Sold computation. The preparer never asked her for beginning and ending inventory amounts.
- The corporation has a Sam's Warehouse Club membership in the name of CO-1. Receipts for such purchases are maintained with the cash receipts.

Per the 20XX and 20XX Form 990 of ORG, the corporation's only revenue source in 20XX was from "gross sales of inventory". In 20XX there was also a small amount of interest revenue.

The corporation's 20XX Sales Tax Returns provide its 20XX gross receipts were \$. The spreadsheet, prepared by BM-8, detailing the source of the receipts provides only liquor and food sales were allocated between member and non-members, cigarettes were not. According to the spreadsheets, members consumed % of liquor and % of the food sold in the bar. Total member liquor receipts in 20XX were \$ and food, \$.

Gross receipts per the corporation's 20XX Sales Tax Returns total \$. According to the spreadsheets attached to the returns, members consumed % of liquor and % of the food sold in the bar. Total member liquor receipts in 20XX were \$ and food, \$.

In item #11 of the 10/27/20XX IDR, the corporation was asked to provide cash register tapes to support the allocations on the spreadsheets accompanying the sales tax returns. The corporation provided a written response to the request. "Cash register tapes were not kept. Information from them is entered into the spreadsheet and then the tapes are thrown away. The organization was not aware that they should be kept. They will be from now on."

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Item #5 of the 10/27/20XX IDR asked the organization to provide the two week sign in roster that was started on October 22, 20XX, plus cash register receipts for the corresponding period in order to gauge the corporation's volume of patronage. The corporation returned Exhibit H. The date range of the entries on the form is October 25, 20XX through November 6, 20XX. The instructions given the corporation were to have every person entering the bar sign in and indicate their status, (e.g. member, non-member or guest of member). Bar receipts which the corporation claims it now maintains were not provided as requested. The corporation's written response is Exhibit I.

The corporation's gross profit from the sales of inventory is as shown per Form 990:

	20XX	20XX
Gross sales of inventory, less returns and allowances		
Less: Cost of goods sold		
Gross profit from sales of inventory		

Cost of goods sold, reported in Part I, line 10b of the respective years' Form 990, per the instructions should include items usually included in a cost of goods sold computation such as direct and indirect labor, materials and supplies consumed, freight-in, and a proportion of overhead expenses where applicable. The return provided no insight into items included in the cost of goods sold computation as it is reflected on the returns, including information with regard to beginning and ending inventories or returns and allowances.

Profits from the corporation's sales are reported in Part I, line 10c of Form 990. A schedule is required which, according to Form 990 instructions, is to include a breakdown of the items sold; (for example, sales of food, souvenirs, electronic equipment, uniforms, or educational publications.) No such schedule is included with either return.

The corporation reported the following expenses in Part II of its 20XX and 20XX Form 990:

	20XX
Salaries and wages	\$\$
Legal fees	\$
Supplies	\$
Equipment rental and maintenance	\$
Taxes and licenses	\$
Office expense	\$

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Event expenses	\$
Pest control	\$
Utilities	\$
Miscellaneous expenses	\$
Total	\$

20XX

Salaries and wages	\$
Supplies	\$
Equipment rental and maintenance	\$
Depreciation, depletion, etc.	\$
Taxes and Licenses	\$
Office Expenses	\$
Event Expenses	\$
Pest Control	\$
Utilities	\$
Repairs & Maintenance	\$
Miscellaneous expenses	\$
Total	\$

The expenses tracked on the spreadsheets prepared by BM-8 have been analyzed. The analysis is found in Exhibit J for 20XX and Exhibit K for 20XX expenses.

A summary, dated October 24, 20XX which was signed by BM-3 and witnessed by CPA and Agent, Internal Revenue Agent for the IRS attesting to the facts taken from the statements offered during the operational interview on October 21, 20XX by BM-3 and BM-1 is included as Exhibit L.

A statement provided by BM-1 addressing the decision to join ORG and the requirement for the corporation to have 10 members is Exhibit M.

LAW AND ANALYSIS

Tax Exemption - Veterans Organizations

Prior to the enactment of I.R.C. § 501(c)(19) by Public Law 92-418, 1972-2 C.B. 675, many veterans organizations qualified for exemption from federal income tax under I.R.C. § 501(c)(4) because most of the traditional activities of these organizations were recognized by the IRS as primarily promoting social welfare. Staff of Joint Comm. on Taxation, 109th Cong., Historical Development and Present Law of the Federal Tax

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Exemption for Charities and Other Tax-Exempt Organizations, JCX-29-05 NO 8, (Comm. Print 20XX). The traditional activities of veterans organizations that were social welfare organizations included promoting patriotism, preserving the memory of those who died in war, and assisting veterans in need. Id. A veterans organization whose primary activity consisted of operating social facilities for its members was not able to qualify for exemption as a § 501(c)(4) social welfare organization, but it could qualify as a social club under § 501(c)(7). Rev. Rul. 66-150, 1966-1 C.B. 147; S. Rep. No. 1082, 92d Cong., 2d Sess. 2 (1972) reprinted in 1972-2 C.B. 713; H.R. Rep. No. 851, 92d Cong., 2d Sess. 1 (1972).

In 1972, Congress enacted I.R.C. § 501(c)(19) and I.R.C. § 512(a)(4) to address the concern that a veterans organization exempt under I.R.C. § 501(c)(4) or (7) may be subject to unrelated business income tax on the provision of insurance to its members. S. Rep. No. 1082, 92d Cong., 2d Sess. 2 (1972) reprinted in 1972-2 C.B. 713.³ Section 512(a)(4) excludes amounts attributable to, or set aside by a §501(c)(19) veterans organization for the payment of life, sick, accident, or health insurance benefits for their members and their members' dependents. Public Law 92-418, 1972-2 C.B. 675.

The Section 501(c)(19) Exemption Requirements

In General

Section 501(c)(19) of the Internal Revenue Code provides for the exemption from federal income tax of a post or organization of past or present members of the United States Armed Forces if it is:

- (a) organized in the United States or any of its possessions,
- (b) at least 75 percent of its members are past or present members of the Armed Forces of the United States,
- (c) substantially all of its other members are individuals who are cadets or are spouses, widows, widowers, ancestors or lineal descendants of past or present members of the Armed Forces of the United States or of cadets, and

* * * *

³ "Before the enactment of the Tax Reform Act of 1969, there was no tax on the insurance activities of the veterans' organizations since the unrelated business income did not apply to social welfare organizations and social clubs. However, the 1969 Act extended the application of the unrelated business income tax to virtually all exempt organizations including social welfare organizations and social clubs." S. Rep. No.1082, 92d Cong., 2d Sess. 2 (1972) reprinted in 1972-2 C.B. 713.

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(d) no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Membership Requirements

Under I.R.C. § 501(c)(19), at least 75 percent of an organization's members must be past or present members of the Armed Forces of the United States ("veterans"). Section 501(c)(19) does not define the term "Armed Forces of the United States." The regulations under I.R.C. § 501(c)(19), likewise, do not define the term. Section 7701(a)(15) of the Code, however, defines "Armed Forces" to include all regular and reserve components of the uniformed services which are subject to the jurisdiction of the Secretary of Defense, the Secretary of the Army, the Secretary of the Navy, or the Secretary of the Air Force, and the Coast Guard.

In addition, I.R.C. § 501(c)(19)(B) requires that substantially all other members of an organization be cadets or spouses, widows, widowers, ancestors, or lineal descendants of veterans or cadets. According to the Senate Report accompanying the legislation, "substantially all" means 90 percent. See S. Rep. No. 1082, 92nd Cong. 2d Sess. 5 (1972), reprinted in 1972-2 C.B. 713, 715. Therefore, of the 25 percent of the members that do not have to be veterans, 90 percent must be cadets, or spouses, etc. Consequently, no more than 2.5 percent (10% x 25%) of an I.R.C. § 501(c)(19) organization's total membership may consist of individuals not mentioned in the statute.⁴

Neither, I.R.C. § 501(c)(19), its legislative history, nor the regulations under I.R.C. § 501(c)(19) define what it means to be a member of a veterans organization. However, whatever the organization requires for one to become a member, the organization must maintain records tracking who its members are and the proportions in the various categories of membership permitted under I.R.C. § 501(c)(19)(B) (member of armed forces, cadet, relative, etc.) to substantiate that its members are veterans or other permitted members. See I.R.C. § 6001 and Treas. Reg. §1.6001-1(c).⁵

* * * *

⁴ Prior to 20XX, ancestors and lineal descendent were not included in the statutory list of persons permitted to be members. In 20XX, Congress amended I.R.C. § 501(c)(19) to include ancestors or lineal descendents of present or former members of the United States Armed Forces or cadets in the statutory list of individuals who may be members of an organization. The regulations have not been updated to reflect this change nor do they reflect the 1982 statutory change eliminating a requirement that veterans be veterans of war.

⁵ Section 6001 of the Code provides that every person liable for any tax imposed by the Code, or for the collection thereof, shall keep adequate records as the Secretary of the Treasury or his delegate may from time to time proscribe. Every organization exempt from tax under § 501(a) and subject to the unrelated footnote continues next page

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Operational Test

Section 1.501(c)(19)-1(c) of the regulations provides that an organization exempt under I.R.C. § 501(c)(19) must be operated exclusively for one or more of the following purposes:

- 1) To promote the social welfare of the community as defined in section 1.501(c)(4)-1(a)(2) of the regulations,
- 2) To assist disabled and needy war veterans and members of the United States Armed Forces and their dependents and widows and orphans of deceased veterans,
- 3) To provide entertainment, care, and assistance to hospitalized veterans or members of the Armed Forces of the United States,
- 4) To carry on programs to perpetuate the memory of deceased veterans and members of the Armed Forces and to comfort their survivors,
- 5) To conduct programs for religious, charitable, scientific, literary, or educational purposes,
- 6) To sponsor or participate in activities of a patriotic nature,
- 7) To provide insurance benefits for their members or the dependents of their members or both, or
- 8) To provide social and recreational activities for their members.

Treas. Reg. § 1.501(c)(19).

Social and Recreational Activities for Members

While Treas. Reg. §1.501(c)(19)-1(c)(8) does not address what it means to “exclusively” provide social and recreational activities for members it is similar to the exempt purpose contained in I.R.C. § 501(c)(7), as both provisions permit an exempt organization to operate social and recreational facilities for its members. In fact, prior to the enactment of I.R.C. § 501(c)(19), a veterans organization whose primary activity consisted of operating a bar or restaurant for the benefit of its members would have to qualify as

continued footnote

business income tax, including veterans organizations, must keep such records. Treas. Reg. § 1.6001-1(a). These books and records are required to be available for inspection by the Service. Treas. Reg. § 1.6001-1(a). In addition, veterans organizations are required to keep books and records to substantiate information reported on their information return. See I.R.C. § 6033 and Treas. Reg. § 1.6001-1(c). They are also required to submit additional information to the Service for the purpose of enabling the Service to inquire further into its exempt status.

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§501(c)(7) social club to be tax-exempt. See Rev. Rul. 60-324 and Rev. Rul. 69-219.⁶ These organizations, prior to 1976, were required to operate “exclusively” for the pleasure and recreation of its members. See I.R.C. § 501(c)(7) (1975). Thus, the rulings and case law under I.R.C. § 501(c)(7) are useful for purposes of determining whether an I.R.C. § 501(c)(19) veterans organization is providing social and recreational activities exclusively for its members.

Treas. Reg. § 1.501(c)(7)-1(b) provides that a club that engages in business, such as making its social and recreational facilities available to the general public is not organized and operated exclusively for pleasure, recreation, and other nonprofit purposes, and is not exempt under I.R.C. § 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.

In West Side Tennis Club v. Commissioner, 111 F.2d 6 (2nd Cir. 1940), cert. denied, 311 U.S. 674 (1940), the Second Circuit upheld the board of tax appeals determination that a social club was not exempt because a substantial amount of its income was received from the general public. West Side Tennis Club was organized to provide tennis facilities for the use and enjoyment of its members. The facilities were only available to members for most of the year; the club hosted annual national championship tennis matches, however, that were open to the general public. The club shared in the ticket proceeds from these matches. The Second Circuit upheld the board of tax appeals determination that the national championship matches were a substantial and profitable business which jeopardized the club’s exemption. West Side Tennis Club, 111 F.2d at p. 7.⁷

In Rev. Rul. 60-324, 1960-2 C.B. 173 and Rev. Rul. 69-219, 1969-1 C.B. 153, the Service held that a § 501(c)(7) social club is not operated exclusively for the pleasure or recreation of its members if it makes its facilities available to the general public to a

* * * *

⁶ In 1976, Congress amended § 501(c)(7) replacing “exclusively” with “substantially all.” This change was effected to establish that social clubs will not jeopardize their exempt status if they receive 35% of their gross receipts from non-membership sources. Only 15% of their gross receipts, however, may be derived from nonmembers’ use of club facilities or services. Pub. L. No. 92-568, S. Rep. 1318, 94 Cong., 2d Sess. (1976).

⁷ In 1976, Congress amended § 501(c)(7) replacing “exclusively” with “substantially all.” This change was effected to establish that social clubs will not jeopardize their exempt status if they receive 35% of their gross receipts from non-membership sources. Only 15% of their gross receipts, however, may be derived from nonmembers’ use of club facilities or services. Pub. L. No. 92-568, S. Rep. 1318, 94 Cong., 2d Sess. (1976).

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substantial degree. Id. However, this does not mean that all dealings with the general public are necessarily inconsistent with the club's exempt purposes. For instance, in Rev. Rul. 60-324, 1960-2 C.B. 173, the Service stated that:

[w]hile [the] regulations indicate that a club may lose its exempt status if it makes its facilities available to the general public, [it] does not mean that any dealings with outsiders will automatically cause a club to lose its exemption. A club will not lose its exemption merely because it receives some income from the general public, that is, persons other than members and their bona fide guests, or because the general public may occasionally be 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.

In 1971, the Service issued Revenue Procedure 71-17, 1971-1 C.B. 683, which contains guidelines for determining the impact of an organization's nonmember gross receipts on its exempt status under I.R.C. § 501(c)(7). The revenue procedure provides that "[a] significant factor reflecting the existence of a nonexempt purpose is the amount of gross receipts derived from use of a club's facilities by the general public." The revenue procedure went on to provide a safe harbor for organizations serving the general public:

As an audit standard, [the gross receipts derived from the general public] alone will not be relied upon by the Service if annual gross receipts from the general public for [use of the club's facility] is \$2,500 or less or, if more than \$2,500, where gross receipts from the general public for use is five percent or less of total gross receipts of the organization.

Rev. Proc. 71-17, 1971-1 C.B. 683 at § 3.01.

The term "general public" is defined as persons other than members or their dependents or guests. Id. at § 2.01. Section 3.03 of Rev. Proc. 71-17 provides four instances in which nonmembers are assumed to be the guests of the members. The assumptions include:

Where a group of eight or fewer individuals, at least one of whom is a member, uses club facilities, it will be assumed for audit purposes that the nonmembers are the guests of the member, provided payment for such use is received by the club directly from the member or the member's employer.

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Where 75 percent or more of a group using club facilities are members, it will likewise be assumed for audit purposes that the nonmembers in the group are guests of members, provided payment for such use is received by the club directly from one or more of the members or the member's employer.

Rev. Proc. 71-17, Section 3.03.

In Pittsburgh Press Club v. United States, 615 F.2d 600 (3rd Cir. 1980), the Third Circuit upheld the Commissioner's determination that a social club failed to qualify for exemption from income tax as a §501(c)(7) organization because it was operated for business and not for the pleasure and recreation of its members. The Pittsburgh Press Club was organized for the purpose of providing a professional and social meeting place for its members. During the years under exam, however, the Pittsburgh Press Club hosted several functions for nonmember outside groups, although each such group had been member sponsored. Based on the amount of nonmember revenues (\$281,000 of nonmember receipts), as well as the percentage of those revenues (11 to 17 percent of gross receipts), the Third Circuit upheld the revocation stating that the exemption from Federal income tax for §501(c)(7) organizations "is to be strictly construed." Pittsburgh Press Club, 615 F.2d at 606. The Court stated that such strict construction cannot be reconciled with the fact that a substantial amount of the Club's activities and income consisted of nonmember functions and nonmember income. Therefore, the Court held "revocation of its exemption was proper." Id.

Recordkeeping and Reporting Requirements

Every person liable for any tax imposed by the Code, or for the collection thereof, shall keep adequate records as the Secretary of the Treasury or his delegate may from time to time prescribe. See I.R.C. § 6001. Every organization exempt from tax under I.R.C. § 501(a), and subject to the tax imposed by I.R.C. § 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 §6033. See Treas. Reg. §§ 1.6001-1(a) and 1.6001-1(c). The books or records required by section 1.6001-1 shall be kept at all times available for inspection by authorized internal revenue officers or employees, and shall be retained so long as the contents thereof may become material in the administration of any internal revenue law. See Treas. Reg. §1.6001-1(e).

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Except as provided, every organization exempt from tax under I.R.C. § 501(a) shall file an annual return, stating specifically the items of gross 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.

See I.R.C. § 6033(a)(1).

Every organization which is exempt from tax, whether or not it is required to file an annual information return, shall submit such additional information as may be required by the Service for the purpose of inquiring into its exempt status and administering the provisions of subchapter F (i.e., I.R.C. § 501 and following), chapter 1 of subtitle A of the Code, I.R.C. § 6033, and chapter 42 of subtitle D of the Code. See Treas. Reg. §1.6033-2(i)(2). See also, I.R.C. § 6001, Treas. Reg. §1.6001-1.

An organization's failure or inability to file required information returns or otherwise to comply with the provisions of I.R.C. § 6033 and the regulations which implement it, may result in the termination of the organization's exempt status based on the grounds that the organization has not established that it is observing the conditions that are required for the continuation of its exempt status. See Rev. Rul. 59-95. These conditions require the filing of a complete and accurate annual information return (and other required federal tax forms) and the retention of records sufficient to determine whether the organization is operated for the purposes for which it was granted tax-exempt status and to determine its liability for any unrelated business income tax. Id.

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. Its records were so incomplete, however, that the organization was unable to furnish such statements. The Internal Revenue Service held that the organization's failure or inability to file the required information return or otherwise to comply with the provision of section 6033 of the Code 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 its exempt status.

Government's Position and Conclusions

Issue 1. ORG has not established it meets the membership requirements of IRC 501(c)(19).

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The IRC provides that an exempt Veterans organization must meet certain membership requirements to maintain its exempt status. At least 75% of the members must be past or present members of the Armed Forces of the United States (veterans). Substantially all, which the IRC defines as 90%, of all other members must be cadets or spouses, widows, or widowers of veterans or cadets. Specifically, of the 25% of the organization's members that are not Veterans, 90% must be cadets, spouses, etc. Only 2.5% of the organizations total membership may consist of individuals who are not veterans, cadets or spouses, widows or widowers of these individuals.

An organization failing to meet the membership requirements will no longer qualify for exemption.

To illustrate, where a Veterans organization consists of 100 members, at least 75 must be Veterans. Of the 25 remaining members, 90% (23) must be cadets or spouses, widows, or widowers of veterans or cadets. The remaining 2 people may be members who are not veterans, cadets, spouses, etc. ($75 + 23 + 2 = 100$)

The instruction offered by CO-2 to its subordinates, ORG among them, is that it requires only ten members and the proof of the veteran status of such members; and "[a]lthough the tax advantages of being a members only club are greater, it does not require it subordinates to limit their bar to members.

The tax advantages of being a members only club *are* greater for an organization exempt under IRC § 501(c)(19) because as the statute clearly provides it is the organizational requirement for such exempt status. An organization that does not meet the membership requirements is not exempt.

The statutes as cited above, further provide that in order that it may be clear that such membership exists, the organization must maintain records tracking who its members are and the proportions in the various categories of membership permitted (members of the armed forces, cadets, spouses, etc.) to substantiate that its members are veterans or other permitted members.

The facts provide ORG does not maintain its own membership roster. When asked to present such, it called upon CO-2 to produce one which included the names of ten people. Further inquiries to CO-2 by ORG resulted in the fact that there has been no change in its membership through 20XX, 20XX and even up to November of 20XX. Since ORG does not verify the veteran status of its so-called members, it was unable to provide that these members meet the definition of Veteran, or other permissible member (e.g. cadet, spouse, etc.). Bringing further into question the validity of this

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membership is the fact that the so-called members do not carry their own membership cards. Rather, the cards are maintained at ORG now, as they were only obtained from CO-2 at the time it made inquiries with regard to its member list. Accordingly until it received the member cards and lists in October 20XX, ORG did not know who its members were. The facts provide that neither BM-1 nor BM-8 who both claimed to be non-veteran members themselves are not listed as existing members however BM-8 and her husband did complete membership applications in August 20XX, seven years after ORG became a subordinate of CO-2.

ORG presented as evidence of its on-going efforts to attract new members denoted only by a sign inside of the facility with regard to "open enrollment", applications completed during August and September of 20XX. Mindful of the fact that the membership went unchanged in the two years prior, this appears to be a recent attempt at increasing membership, however not a legitimate one seemingly. The original applications were still at the ORG (a bar) in October 1998, having sat for one to two months, without having being submitted to CO-2 with the membership fee of \$ per member. ORG by its own admission does not verify veteran or other permissible status, a requirement for membership, and the gross receipts as presented by ORG's own records do not provide for a fee having been collected for any new members during the examination period.

Issue 2. ORG has not established that it operates exclusively for exempt purposes listed in Treas. Reg. § 1.501(c)(19)-1(c).

As is discussed more fully above, an organization described in I.R.C. § 501(c)(19) carries out activities in furtherance of its exempt purposes only when such activities are carried out exclusively in furtherance of the purposes listed in Treas. Reg. § 1.501(c)(19)-1(c). Among these purposes is the provision of social and recreational activities for its members. Accordingly, when a veterans organization described in I.R.C. § 501(c)(19) provides social and recreational activities for its members, or for guests whose expenses are paid by members, the organization is engaged in activities in furtherance of its exempt purposes. If such an organization makes its facilities available to the general public to a substantial degree, and/or a significant amount of the organization's income is received from the general public, the organization may lose its tax exemption.

The statute is clear that an organization recognized as exempt under IRC § 501(c)(19) is a *membership* organization. Patronage of the facility and the participation in the activities of an organization so exempt is limited to the exclusively to the organization's membership and guests.

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The statute provides that a club that engages in business, such as making its social and recreational facilities available to the general public is not organized and operated exclusively for pleasure, recreation, and other nonprofit purposes, and is not exempt under I.R.C. § 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. Evidence of such solicitation is further suggested by making the facility easily accessible to the general public, and by failing to denote that the facility is a members' only establishment.

Revenue Procedure 71-17 provides that a significant factor reflecting the existence of a nonexempt purpose is the amount of gross receipts derived from use of a club's facilities by the general public. However, gross receipts alone will not be relied upon by the Service where gross receipts from non-member use of the organization's facility is \$ or less or, if more than \$ where gross receipts from non-member use is 5% or less of the organization's total gross receipts.

The recordkeeping requirements under the Code, if followed, enable the Service to engage the audit standard afforded by the Revenue Procedure. That is, a member organization whose exempt status is predicated on its ability to establish that its facility meets the exclusive use test as defined by the statute is required to maintain books and records to account for patronage of its facility, and the relationship of its patrons to the exempt organization, (member, guest of member, spouse, etc.). Additionally, adequate books and records sufficient to establish how the amount of gross receipts and related expenses are allocated to each type of patronage are required. Where the organization has failed to maintain such a recordation, the audit standards require that all receipts and expenses of the organization are treated as if from non-member sources.

In the instant case, very few documents were produced during the examination that demonstrated ORG engaged in exempt activities during the years at issue. ORG did not maintain any records that distinguished the amount of income that its bar operations generated from ORG's members, their families, guests, auxiliary members, and nonveterans. Nor did it maintain any records that tracked who used the facilities (i.e., members, members' families, guests, non-veterans, etc.) on a daily basis. BM-8 provided in a written statement that the single record, the cash register receipts on which member and non-member revenues were tracked were discarded.

According to ORG's President, BM-1, who has had no prior experience with operating a veteran's or any other type of exempt organization, and who himself is not a veteran, said he purchased the "business" as a retirement investment. Since BM-1 has also stated that he does not receive a salary or rent from use of the facility, it is not clear

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how purchasing a bar and converting it to an exempt member organization will meet that financial goal except that he never intended that it be operated in accordance with such exempt purpose, but rather as a commercial facility.

Organizations exempt under section 501(c)(19) of the IRC have been permitted broad purposes by Congress. They promote Americanism, sponsor youth activities, provide color guards, conduct patriotic ceremonies and functions, and conduct community activities. In other words, they promote the social welfare of the community. Many also conduct social activities *among their members*. Some examples of promoting social welfare are:

- Sponsoring youth activities
- Sponsoring the Boy Scouts, Girl Scouts, or other youth units of the post, and providing scholarships for students
- Making donations to charities described in section 501(c)(3) of the IRC, such as hospitals, schools, the Red Cross, and the local Community Chest
- Visiting sick or hospitalized members, veterans and their families

The meeting minutes provide some insight into charitable and some civic activities. Information provided established ORG made some contributions to its local fire department, and national and local charities, and the purchase of flags to be placed at the graves of local veterans. Allotting a full day to plan and one to execute, the minutes provide that over a three year period, from January 20XX through July 20XX, twenty (20) days out of 1,095 days (365 days x 3) were devoted to such activities.

In accordance with the foregoing, the organization did not maintain records adequate to confirm the percentage of member receipts in the sales tax returns, and as such in accordance with the audit standards afforded by Revenue Procedure 71-17, all of the corporation's receipts are considered to be from non-member sources, or the general public.

While the records and information obtained provide the organization did engage in some exempt activities, the time devoted to such activities are insignificant in comparison to ORG's bar operations.

The facts support that ORG primary activity was operating a bar for use by the general public a non-exempt activity, and it has not established that it has met the membership requirements necessary to be recognized as exempt under section 501(c)(19) of the Internal Revenue Code, it is proposed that its exempt status be revoked effective January 1, 20XX.

An examination closing conference was offered, and held on January 27, 20XX with _____, Exempt Organizations Manager.

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If you accept our findings, please sign the enclosed Form 6018-A, Consent to Proposed Action-Non Declaratory Judgment. Please return it to the following address within 30 days of the date of this letter:

Internal Revenue Service

As a taxable entity you are required to file form 1120 "U.S. Corporation Income Tax Return". Please submit the completed returns for 20XX, 20XX, and 20XX to the address shown above within 30 days of this report. If you would like to schedule a conference to discuss this report, please call Agent at between 8:00 a.m. and 4:30 p.m. to schedule.