

# MOVES TO LIGHTEN TAX ON CLUB DUES

BY

WM. WARD FOSHAY  
*General Counsel*

**D**URING the past year there were a number of developments relating to the Federal club dues tax which are of interest to the member clubs of the United States Golf Association.

## LEGISLATION

### EXCISE TAX TECHNICAL CHANGES ACT OF 1957

This Bill (H.R. 7125) was passed by the House of Representatives on June 20, 1957, and is now before the Senate Committee on Finance for consideration at this session of Congress. The Bill includes a number of technical changes which would be desirable from the point of view of the member clubs.

#### **Assessments for Capital Construction—**

One of the changes would exempt from the club dues tax all assessments for the construction or reconstruction of any social, athletic or sporting facility (or for the construction or reconstruction of any capital addition to or capital improvement of any such facility). It should be noted, however, that only assessments paid after the effective date of the law for construction or reconstruction begun after that date would be exempt. This might be taken into consideration by those having in mind the possibility of adding to or improving their club facilities.

The House report on the Bill also contained the following:

"Since the exemption is applicable only to assessments for construction, or reconstruction, of a facility, amounts used for the purchase of land will not be exempt from tax. Similarly, the use of funds for the purchase of existing facilities will not be tax exempt. Exemption will be

available for the construction or reconstruction of buildings as well as various outdoor facilities, such as tennis courts, swimming pools, and golf courses. Mere upkeep and repairs do not constitute construction or reconstruction."

These further limitations should also be borne in mind.

**Life Memberships—**Under the present law, life members are required to pay annually a tax equal to the tax on the amounts paid by active resident annual members for dues or membership fees, but no tax is due on the amount paid for the life membership as such. If the Bill is enacted, the life members would have the alternative of paying a tax based on the tax paid by members having privileges most nearly comparable to those held by the particular life member or paying a one-time tax based upon the amount actually paid for the life membership. The election would have to be made at such time not later than the first payment for the life membership as would be prescribed by regulation.

**Honorary Memberships—**Under a 1955 ruling (Rev. Rul. 55-198), an honorary member of a club who is entitled to the use of the facilities of the club for a period of indefinite duration is considered to be a life member for the purposes of the tax. On the other hand, honorary memberships which are granted for a definite period of time and are in fact terminated at the expiration of that period, and not renewed, are not considered life memberships and are not subject to tax provided no dues or membership fees are paid. This will be changed if the Bill is enacted, as is made clear in the House report where

it is said: "If no payment is made for the life membership, as in the case of an honorary membership, no tax will be due."

**Admissions**—*In Exmoor Country Club v. U. S.*, 119 F. 2d 961 (7th Cir. 1941), it was held that a private country club which charged members and their guests for the use of the club's swimming pool and skating rink, and for the privilege of dining and dancing, was liable for the admissions tax on such charges, even though the club's premises and activities were not open to the public or operated for profit. The Bill would repeal the admissions tax on privately operated swimming pools, skating rinks, and other places providing participations in sports, except dancing.

#### OTHER LEGISLATIVE DEVELOPMENTS

**Optional Facilities and Services**—It will be recalled that in another 1955 ruling (Rev. Rul. 55-318), charges for the use of lockers and bathhouses for a period of more than six days were held to be subject to the tax on dues. It was later made clear in another ruling (Rev. Rul. 56-620) that payments for the service of cleaning and storage of golf clubs are not subject to the tax when made by the members to the golf professional as an independent contractor or concessionaire, even though collected for him by the club as a matter of convenience. It is understood that the earlier ruling has now been extended by some agents to apply to the rental or storage of golf carts, berthing or wharf areas for private boats and other facilities and services.

In his letter to the House Committee endorsing the Excise Tax Technical Changes Act of 1957, the President of the USGA registered strong objection to the application of the club dues tax to charges for golf lockers and other club facilities and services, the use of which is entirely within the discretion of the members. He characterized the tax as being in this respect more a nuisance than a revenue measure and suggested that the additional taxes collected could not be sufficient to justify the additional accounting burden to the

clubs, annoyance to members and work for the auditing staff of the Internal Revenue Service. He submitted that this application of the tax should be either eliminated or limited so that the tax would be applied to these charges only to the extent they exceed some percentage, such as 25%, of the dues.

In the current session of the Congress, two Bills (H.R. 9876 and H.R. 9877) have been introduced which, if enacted, would have the effect of eliminating the tax in this area. They would provide that the term "dues" does not include charges for privileges or facilities if the members have the option to decide whether they will avail themselves of such privileges or facilities.

**Tax Rate**—The President of the USGA has also recommended the reduction in the 20% tax rate. Under present circumstances, action in this regard appears unlikely.

#### OTHER DEVELOPMENTS

There have been several administrative rulings and court decisions which may also be of interest to member clubs.

**Minimum Charges**—In this era of rising costs, many clubs have been faced with the problem of maintaining their customary standards without failing to make ends meet. To meet the problem, the thinking is usually directed first toward an increase in dues, but there lies a further problem. Those in charge of the club's finances find that there is a certain level of the use of the club's facilities and services which has to be maintained if a deficit is to be avoided. At the same time they note substantial variations in the degree of use by the members. Some use the club regularly and contribute more than the average, while others use the club only occasionally or not at all. Therefore, an increase in dues has not appeared to provide a fair answer to the problem inasmuch as it would apply to all members equally and accordingly place additional burdens on the regular users in order to make up for the deficiencies of the occasional users.

Some clubs have sought a solution in the so-called minimum charge. Under this arrangement, there is imposed a specified charge against which members may eat or drink and to the extent they do not use up the charge be billed for the difference. The Internal Revenue Service has taken the position informally that the entire amount of the minimum charge is subject to the club dues tax even though the member more than uses up the charge. This has been objected to by a number of clubs, and some have requested rulings. At this writing, word has not been received of the issuance of a ruling in response to any of these requests.

One club has approached the problem in a somewhat different manner, and has received a favorable ruling of the Internal Revenue Service. This club's proposed arrangement and the views of the Internal Revenue Service itself with respect to it can best be described by quoting the ruling in full, as follows:

T:R:ExA  
SC

September 27, 1957

Gentlemen:

We are in receipt of a letter dated . . . , requesting a ruling relative to your liability for collection of the tax on dues imposed under the provisions of section 4241 of the Internal Revenue Code of 1954, in connection with certain payments made by members of your club.

The information submitted indicates that the (club) . . . is in the business of conducting and operating a club for the pleasure, recreation, and entertainment of its members. In addition to the principal membership category of resident member, the classes of memberships in the organization consist of resident inactive, social, non-resident, and junior members. A resident member has voting privileges in the organization, is entitled to use all of the club's facilities, and also has an ownership interest in the property of the club. The other classes of members are subject to special qualification provisions and certain restrictions in

voting and use of facilities. Under the present bylaws of the club, resident members pay annual dues of \$260.00, payable in monthly installments in advance. Members in other categories are subject to different dues requirements.

At a meeting to be held in November, the Board of Governors proposes to offer an amendment to the bylaws of your organization. Such amendment would authorize the Board of Governors at the beginning of each fiscal year, to divide the resident members into two classifications, namely, resident members and resident members-sustaining. The annual dues of resident members under the proposed amendment would continue to be \$260.00, payable in monthly installments in advance, and the dues of resident members-sustaining would be fixed by the Board of Governors at not less than \$300.00 nor more than \$420.00, to be paid in advance in monthly installments.

Under the proposed amendment to the bylaws the Board of Governors would determine the amount needed to make up the club's operating deficit for the preceding fiscal year, and would use such amount as the basis for determining the amount of dues to be paid by resident members-sustaining for the succeeding year. The proposed amendment would prohibit the classification of any resident member as a resident member-sustaining, who had been billed by the club for all purposes, except special assessments, in a total amount of \$800.00 or more, such amount to include membership dues, charges for the use of facilities, and charges made by the club for food, liquor and similar items. If the total expenditures of resident members for such items as above enumerated fall below \$800.00 for the preceding year, the Board of Governors would be authorized to classify such members as resident members-sustaining, and raise the annual dues on a graduated scale. No change would be made in the proposed amendment to the bylaws with respect to the dues of the other categories of membership.

The information also indicates that resident members and resident members-sustaining will have equal rights and privileges in regard to property ownership, voting privileges and use of facilities, the only difference being in the amount of yearly dues required to be paid. The information further discloses that while the payment for such items as food, liquor, etc., may reduce the membership dues of a particular member for the next succeeding year, such payments are not required as a condition to the continued enjoyment of the privileges and facilities of the club. The question presented is whether the dues tax would apply to such charges for food, liquor, and similar items, merely because they serve as a basis for determining the amount of dues to be paid by a member in the next succeeding year.

Section 4242(a) of the Code defines the term "dues", as used in section 4241 of the Code, to include any assessment, irrespective of the purpose for which made, and any charges for social privileges or facilities, or for golf, tennis, polo, swimming, or other athletic or sporting privileges or facilities, for any period of more than six days. It is our position that any amount required to be paid and/or spent by a member of a social, athletic, or sporting club or organization as a requisite to continued membership, or to continued membership in a particular membership class, constitutes a payment of dues within the meaning of section 4242(a) of the Code, and if the total dues paid by the active resident annual members are in excess of \$10.00 a year, the total dues paid by all classes of members are subject to the tax imposed by section 4241(a)-(1) of the Code. On the other hand, we have consistently held that amounts paid for food and drink in a social, athletic, or sporting club or organization are not subject to the dues tax unless a mandatory minimum expenditure for such items has been previously set by such club or organization.

It appears from the information furnished that the total amount paid by members of the (club), for food and drink is not a required minimum expenditure for such items, nor is it required as a condition to the continued enjoyment of the privileges and facilities of the club. On the basis of such information, we have concluded that the dues tax imposed by section 4241(a)(1) of the Code will not apply to any charges for food, liquor and similar items made against the members of the club.

Very truly yours,  
(Signed) H. T. Swartz  
Director, Tax Rulings Division

Particular attention is called to the last sentence of the next to last paragraph of the ruling. The reference there to "a mandatory minimum expenditure \* \* \* \* previously set" would seem to indicate that the Internal Revenue Service's informal position with respect to minimum charges will be confirmed.

**Voluntary Contributions versus Assessments**—In years past, there was a good deal of controversy over the question whether voluntary contributions for a club's capital or operating purposes should be regarded as assessments subject to the club dues tax. As far as the Internal Revenue Service is concerned, most of the disputes were laid to rest by two other rulings issued in 1955. In one of these (Rev. Rul. 55-576) it was held that loans made by members voluntarily to finance a club's building program are not subject to the dues tax where the individual members' rights and privileges in the club do not depend on whether or not they make the loan and the club guarantees the repayment. The same ruling, however, added that where such loans are required of new members or of members electing to acquire a new or different membership, the amounts are taxable as initiation fees.

One of the arguments that was advanced in opposition to the treatment of voluntary contributions as assessments was that they could not be regarded as such where

the club was not lawfully authorized by its charter to make legally enforceable assessments. Following a court decision rejecting this argument, the Internal Revenue Service ruled (Rev. Rul. 55-533) that where a club's members are subjected to assessments or are requested to contribute amounts fixed in prorated or uniform allocations on the basis of membership privileges or the class of membership held, any amounts so paid are taxable as dues whether or not the club has authority to enforce collection.

This position was further confirmed in the recent case of *City Athletic Club v. U. S.*, 242 F. 2d 43 (2d Cir. 1957). In that case the court said that the question is entirely a matter of Federal law and that the deciding factor is not enforceable under State law. The Court added that it is the effective call for a definite contribution or payment from the members which should be held to characterize an assessment, as distinguished from a voluntary contribution or gift. The reasoning was that such a call always carries with it some degree of compulsion, even if it be social or moral rather than legal. Taxwise, said the court, no distinction need be made between payment under such sanctions and payment under legal sanctions.

**Life Memberships**—In 1957 there was an interesting ruling (Rev. Rul. 57-239) on a life membership question. A golf course had two classes of members, regular and senior, and each class had full club rights and privileges. A person was eligible for senior membership if he were more than 60 years of age and had been a regular member for more than 25 years. The annual dues for regular members was \$600, while for senior members it was \$300. The club also has life members, who were not required to pay annual dues, and some of them were more than 60 years of age and had been regular members for more than 25 years. As indicated above, the present law is that life members are required to pay annually a tax equivalent to the tax upon the amount paid by "active resident annual members" for dues or

membership fees. In this case both the resident and senior members were within this definition, and the question was whether the life members' tax was to be based on the regular or the senior members' dues. The ruling was to the effect that where there is more than one class of active resident members, the club dues tax of a life member is equivalent to the tax upon the amount paid as dues by an active resident annual member of the class in which the member qualifies. Thus, in this case, the life members who would qualify as senior members would pay taxes based on the \$300 rate and the others on the \$600 rate.

In *McIntyre v. U. S.*, 151 F. Supp. 388 (D. Md. 1957), the question presented was whether a particular initial fee of \$125 was a non-taxable payment for life membership or a taxable initiation fee. A group of civic leaders unable to persuade public authorities to construct a swimming pool at taxpayers' expense organized a club to erect and operate the pool. Membership was limited to 600 families owning residential property within a designated portion of the city. Each member paid the initial fee of \$125 and annual dues of \$10. The persons paying the fee were entitled to a life membership certificate but not to use the pool except on payment of the \$10 dues. The court held that the dues tax was not applicable to either amount, since the club was more a community enterprise than a civic or social club. The court went on to consider, however, what would have been the tax status had the decision been otherwise. It concluded that the \$125 payment would be taxable as an initiation fee.

## CONCLUSION

These developments serve to illustrate the numerous, varied and recurring complexities of the present Federal excise tax in this area. They emphasize strongly the need for technical changes in the law such as those which have been proposed or recommended.