



Tax Reduction Letter

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Treasury Decision 8601

Definition of Club

July 1995

SUBJECT MATTER: Section 274.-Disallowance of Certain Entertainment, etc., Expenses

APPLICABLE SECTIONS:

26 CFR 1.274-2: Disallowance of deductions for certain expenses for entertainment, amusement, or recreation. Internal Revenue Service 26 CFR Part 1

TEXT:

AGENCY:

Internal Revenue Service (IRS), Treasury.

ACTION:

Final and temporary regulations.

SUMMARY:

This document contains final and temporary regulations relating to the definition of a *club organized for business, pleasure, recreation, or other social purpose* for purposes of the disallowance of a deduction for club dues. The regulations reflect changes to the law made by the Omnibus Budget Reconciliation Act of 1993 and affect persons who pay or incur club dues.

DATES:

These regulations are effective July 19, 1995.

For dates of applicability, see 1.274-2 (a) and (e).

SUPPLEMENTARY INFORMATION:

Background

This document provides final and temporary Income Tax Regulations (26 CFR part 1) under section 274 (a) (3) of the Internal Revenue Code of 1986 (Code). This provision was added by section 13210 of the Omnibus Budget Reconciliation Act of 1993 (107 Stat. 469).

On August 12, 1994, the IRS published a notice of proposed rulemaking defining *club* in the Federal Register (59 FR 41414). No public hearing on the proposed regulations was requested or held, but written comments were received. After consideration of all the comments, the proposed regulations are adopted by this Treasury decision with one minor editorial change in 1.274-2 (a) (2) (iii) (b).

On December 16, 1994, the IRS published a notice of proposed rulemaking in the Federal Register (59 FR 64909) relating, in part, to the tax treatment of payment by an employer of an employee's club dues. This Treasury decision has no effect on the notice of proposed rulemaking published on December 16, 1994. Final regulations on this subject will be published at a later date.

Explanation of Provisions

Section 274 (a) (3) of the Code disallows a deduction for amounts paid or incurred for membership in any club organized for business, pleasure, recreation, or other social purpose.

Under the final regulations, the dues disallowance provisions of *section 274 (a) (3)* apply to any membership organization a principal purpose of which is to conduct entertainment activities for members or their guests or to provide members or their guests with access to entertainment facilities. The membership organizations subject to dues disallowance under the final regulations include, but are not limited to, country clubs, golf and athletic clubs, airline clubs, hotel clubs, and clubs operated to provide meals under circumstances generally considered to be conducive to business discussion. The dues disallowance provisions of *section 274 (a) (3)* do not, in general, apply to (1) civic or public service organizations such as Kiwanis, Lions, Rotary, Civitan, and similar organizations; (2) professional organizations such as bar associations and medical associations; and (3) certain organizations similar to professional organizations, specifically, business leagues, trade associations, chambers of commerce, boards of trade, and real estate boards.

Under the final regulations, the three exceptions from dues disallowance listed above do not apply if a principal purpose of the organization is to conduct entertainment activities for members or their guests or to provide members or their guests with access to entertainment facilities.

A commentator on the proposed regulations requested clarification of the terms *entertainment* and *a principal purpose*. The term *entertainment* is defined in existing *1.274-2 (b) (1)* and that definition applies for purposes of these final dues disallowance regulations. The final regulations do not provide any additional guidance with respect to determining whether a principal purpose of an organization is to conduct entertainment activities or provide access to entertainment facilities.

Two commentators objected to the proposed regulations' disallowance of all deductions for airline club dues. The commentators indicated that these clubs are used for business purposes, and little or no personal benefit is derived from airline club membership. However, the legislative history of *section 274 (a) (3)* specifically provides that deductions are not allowed for airline club dues. Therefore, the final regulations do not change the proposed rule concerning airline clubs.

One commentator stated that the proposed regulations would permit taxpayers to deduct, as a business expense, dues paid to certain organizations described in *section 501 (c) (8)* because the organizations are civic or public service organizations. The commentator requested that the regulations be amended to preclude a business expense deduction for these dues because the organizations are not formed for a business purpose but, rather, to promote charitable, philanthropic, patriotic, and educational activities.

The IRS and the Treasury believe that the regulations, as proposed, adequately address the commentator's concern. *Section 274* and these regulations do not expand the category of items that are deductible as business expenses. Rather, *section 274* disallows certain business expense

deductions that would otherwise be allowable under *section 162*. If dues paid to certain *section 501 (c) (8)* organizations are not deductible under *section 162* because they are not ordinary and necessary business expenses, *section 274* and these regulations do not make the dues deductible.

The final regulations are effective with respect to amounts paid or incurred after December 31, 1993.

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in EO 12866. Therefore, a regulatory assessment is not required. It has also been determined that *section 553 (b)* of the Administrative Procedure Act (5 U.S.C. chapter 5) and the Regulatory Flexibility Act (5 U.S.C. chapter 6) do not apply to these regulations, and, therefore, a Regulatory Flexibility Analysis is not required. Pursuant to *section 7805 (f) of the Internal Revenue Code*, the notice of proposed rulemaking preceding these regulations was submitted to the Small Business Administration for comment on its impact on small business.

* * *

Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 1 is amended as follows:

PART 1-INCOME TAXES

Paragraph 1. The authority citation for part 1 continues to read in part as follows:

Authority: *26 U.S.C. 7805* * * *

Par. 2. *Section 1.274-2* is amended as follows:

1. Paragraph (a) (2) (ii) is revised.
2. Paragraph (a) (2) (iii) is added.
3. Paragraph (a) (3) (iii) is revised.
4. The heading of paragraph (e) and text for paragraph (e) (1) are revised.
5. Paragraph (e) (3) (ii) is revised.

The additions and revisions read as follows:

1.274-2 Disallowance of deductions for certain expenses for entertainment, amusement, or recreation.

(a) * * *

(2) * * *

(ii) *Expenditures paid or incurred before January 1, 1979, with respect to entertainment facilities, or paid or incurred before January 1, 1994, with respect to clubs-(a) Requirements for deduction.* Except as provided in this section, no deduction otherwise allowable under chapter 1 of the Internal Revenue Code shall be allowed for any expenditure paid or incurred before January 1, 1979, with respect to a facility used in connection with entertainment, or for any expenditure paid or incurred before January 1, 1994, with respect to a club used in connection with entertainment, unless the taxpayer establishes-

- (1) That the facility or club was used primarily for the furtherance of the taxpayer's trade or business; and
- (2) That the expenditure was directly related to the active conduct of that trade or business.

(b) *Amount of deduction.* The deduction allowable under paragraph (a) (2) (ii) (a) of this section shall not exceed the portion of the expenditure directly related to the active conduct of the taxpayer's trade or business.

(iii) *Expenditures paid or incurred after December 31, 1993, with respect to a club-(a) In general.* No deduction otherwise allowable under chapter 1 of the Internal Revenue Code shall be allowed for amounts paid or incurred after December 31, 1993, for membership in any club organized for business, pleasure, recreation, or other social purpose. The purposes and activities of a club, and not its name, determine whether it is organized for business, pleasure, recreation, or other social purpose. Clubs organized for business, pleasure, recreation, or other social purpose include any membership organization if a principal purpose of the organization is to conduct entertainment activities for members of the organization or their guests or to provide members or their guests with access to entertainment facilities within the meaning of paragraph (e) (2) of this section. Clubs organized for business, pleasure, recreation, or other social purpose include, but are not limited to, country clubs, golf and athletic clubs, airline clubs, hotel clubs, and clubs operated to provide meals under circumstances generally considered to be conducive to business discussion.

(b) *Exceptions.* Unless a principal purpose of the organization is to conduct entertainment activities for members or their guests or to provide members or their guests with access to entertainment facilities, business leagues, trade associations, chambers of commerce, boards of trade, real estate boards, professional organizations (such as bar associations and medical associations), and civic or public service organizations will not be treated as clubs organized for business, pleasure, recreation, or other social purpose.

(3) * * *

(iii) "Expenditures paid or incurred before January 1, 1979, with respect to entertainment facilities or before January 1, 1994, with respect to clubs", see paragraph (e) of this section, and

* * *

(e) *Expenditures paid or incurred before January 1, 1979, with respect to entertainment facilities or before January 1, 1994, with respect to clubs-*(1) *In general.* Any expenditure paid or incurred before January 1, 1979, with respect to a facility, or paid or incurred before January 1, 1994, with respect to a club, used in connection with entertainment shall not be allowed as a deduction except to the extent it meets the requirements of paragraph (a) (2) (ii) of this section.

* * *

(3) * * *

(ii) *Club dues-* (a) *Club dues paid or incurred before January 1, 1994.* Dues or fees paid before January 1, 1994, to any social, athletic, or sporting club or organization are considered expenditures with respect to a facility used in connection with entertainment. The purposes and activities of a club or organization, and not its name, determine its character. Generally, the phrase *social, athletic, or sporting club or organization* has the same meaning for purposes of this section as that phrase had in section 4241 and the regulations thereunder, relating to the excise tax on club dues, prior to the repeal of section 4241 by section 301 of Pub. L. 89-44. However, for purposes of this section only, clubs operated solely to provide lunches under circumstances of a type generally considered to be conducive to business discussion, within the meaning of paragraph (f) (2) (i) of this section, will not be considered social clubs.

(b) *Club dues paid or incurred after December 31, 1993.* See paragraph (a) (2) (iii) of this section with reference to the disallowance of deductions for club dues paid or incurred after December 31, 1993.

* * *

1.274-5T [Amended]

Par. 3. In 1.274-5T, the first two sentences of paragraph (c) (6) (iii) are amended by removing the language "at any time" in each sentence and adding the language "before January 1, 1994," in its place.

Margaret Milner Richardson,
Commissioner of Internal Revenue.

Approved June 21, 1995.

Leslie Samuels,
Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on July 18, 1995, 8:45 a.m., and published in the issue of the Federal Register for July 19, 1995, *60 F.R. 36993*)