Final Report Section 1

INTRODUCTION AND ASSUMPTIONS

Last year our committee was formed at the request of the Board of Directors to review and make recommendations for WMOTA regarding our current status as a 501 (C)(7) and the Benefits/Pitfalls for changing to a 501(C)(3).

The Committee is comprised of

Jerry Smith, Chair
Kristi Bruner, member
Ken Drozdowicz, member
Jim McKnight, member

The Assumptions the Committee made were as follows:

1. Determine if WMOTA is currently in compliance with all the provisions of a 501 (C)(7).

2. Examine the following WMOTA specifics for compliance with a 501 (C)(7).
    a. 35% rule for outside income.
    b. 15% rule inside the 35% rule.
    c. The Map project Grant using OHV money.
    d. Income earned by volunteering at Chamber of Commerce functions.
    e. Income earned from 50/50 Raffles
    f. Income earned from Poker Runs
    g. Membership limitations

3. Determine what the Benefits and Pitfalls are for WMOTA to be restructured as a 501 (C)(3).

4. Determine the requirements for a 501 (C)(3) Organization
    a. Completion of the 1023 application for tax exempt status.
    b. Selection of Exempt Purpose.
    c. Nonexempt purposes prohibited.
    d. Organizing Documents.
    e. Membership open to the public

5. Basis for review of any determinations criteria for either the 501(C)(3) or 501 (C)(7) would be whether or not the entity would be in compliance if examined by the IRS.

6. Prepare an IRS publications notebook with all relevant IRS publications for use by the Committee.

7. Prepare a Final Report for the WMOTA Board of Directors to be presented at the August 2, 2016 Board of Directors Meeting.

Final Report Section 2

EXECUTIVE SUMMARY

1. The Committee found that WMOTA is in full Compliance as a 501 (C)(7).

2. The Committee found that WMOTA should not try to convert the existing WMOTA organization to a tax exempt 501(C)(3).

3. A newly organized 501(c)(3) entity but separate from WMOTA could easily be formed if enough interest is found to warrant it.

Final Report Section 3

501 (C)(7) REQUIREMENTS

Ref: IRS notebook section 5B

1. IRC 501 (c) (7) exempts from federal income tax, clubs "organized for pleasure, recreation, and other nonprofit purposes, substantially all of the activities of which are for such purposes and no part of the net earnings of which goes to the benefit of any private shareholder"

2. Social clubs are membership organizations. The exemption of social clubs is based on the logic of allowing members to pool their funds for recreational purposes, rather than for a compelling public benefit and provided the club does not have a written policy which discriminates against individuals seeking membership on the basis of race, color, or creed.

3. Clubs may have more than one class of membership, such as regular, associate, corporation-sponsored, and corporate with each class having eligibility requirements and a formal admittance procedure. Commingling of members is a material part of the life of an organization. Face to face interaction is important for members of a social club.

4. Social clubs are permitted to receive a certain amount of income from the general public and from investments. It can receive up to 35% of its gross receipts from outside its membership and if no more than15% of its gross receipts are derived from nonmember use of club assets. A social club can exceed the 35%/15% limitations if it can show through facts and circumstances that "substantially all" of its activities are for "pleasure, recreation, and other nonprofit purposes." The receipt of unusual amounts of income by a club, such as from the sale of an asset, are not to be included in either the numerator or denominator for purposes of computing the 35% or 15% allowances.

5. Distributions to club members in the form of prizes for winning club recreational events are consistent with the exemption under IRC 501 (c) (7). A club is not exempt under IRC 501 (c) (7) if the money for the prizes is raised from the public. (This would fall into the 35% income rule)

Final Report Section 4:

501 (C)(7) INVESTIGATION RESULTS { WMOTA}

1. Examine the following WMOTA specifics for compliance.
    a. 35% rule for unrelated or outside income. WMOTA's normal income from all sources is about $5,000. To approach the 35% limit, WMOTA's Gross income from all sources would have to be about $7,700. i.e $2,700 in outside income ($2,700/$7,700 = 35%)
        i. What constitutes "outside Income" for WMOTA?
        ii. Chamber work is not unrelated (outside) income because it is derived solely from volunteer work by non-compensated members . Ref Section 3 of the Publications Notebook page 9 "Volunteer Workforce:" Any trade or business in which substantially all of the work is performed for the organization without compensation is not an unrelated trade or business."
        iii. Poker Runs, Auctions and 50/50 raffles are income generated from members or our guests.
        iv. Conclusion : WMOTA is in compliance with the 35% Rule

    b. 15% rule inside the 35% rule. WMOTA's normal income from all sources is about $5,000. In the example above, to exceed the 35% rule, the gross receipts would have to be $7,700.00 The 15% limit states that no more than15% of its gross receipts are derived from nonmember use of club assets. In this example that amount would be $1,155.00.
        i. This rule is applied only if the 35% Rule is violated
        ii. We have only the club trailer as an asset, and we have never rented it out to a non-member.
        iii. Conclusion: WMOTA is in compliance with the 15% Rule inside the 35% Rule.

    c. Is the grant money considered unrelated or outside Income?
        i. The Map project Grant is funded thru State of AZ OHV money.
        ii. WMOTA does not have "Constructive Receipt" of this money. The money is and always has been dedicated to pay the cost of printing, none of the money is available for use by WMOTA.
        iii. Constructive Receipt is defined by the IRS in Ref: Section 8D, Publication 538 Page 9 " Income is constructively received when an amount is credited to your account or made available to you without restriction. You need not have possession of it. If you authorize someone to be your agent and receive income for you, you are considered to have received it when your agent receives it. Income is not constructively received if your control of its receipt is subject to substantial restrictions or limitations."
        iv. Given the nature of the grant, it is evident that it is not income to WMOTA as there is NO constructive receipt.
        v. Conclusion: The Map Grant is NOT unrelated or outside income, therefore WMOTA is in compliance with the Map Grant.

Final Report Section 4 – continued

d. Does WMOTA conduct its memberships as required by 501 (C)(7) rules.
   i. Social clubs are membership organizations. The exemption of social clubs is based on the logic of allowing members to pool their funds for recreational purposes, rather than for a compelling public benefit and provided the club does not have a written policy which discriminates against individuals seeking membership on the basis of race, color, or creed.
   ii. Clubs may have more than one class of membership, such as regular, associate, corporation-sponsored, and corporate with each class having eligibility requirements and a formal admittance procedure. Commingling of members is a material part of the life of an organization. Face to face interaction is important for members of a social club.
   iii. WMOTA expends its member derived income for recreational purposes and not for a compelling public interest.
   iv. WMOTA does not have a written policy that restrict its membership on the basis of race, color or creed.
   v. WMOTA has three classes of membership: Regular, Business, Comp & Lifetime, and each has its own rules for membership.
   vi. WMOTA members regularly comingle with face to face interaction at meetings, camping, trail work and rides to name a few.
   vii. Conclusion: WMOTA is in compliance with Membership requirements.

2. Conclusion: WMOTA is and has been fully in compliance with the requirements of 501 (C)(7).

Final Report Section 5

501 (C)(3) REQUIREMENTS

1. An organization may qualify for exemption from federal income tax if it is organized and operated exclusively for one or more of the following purposes. (Ref sec 1B page 21)
   A. Religious
   B. Charitable
   C. Scientific
   D. Testing for public safety
   E. Literary
   F. Educational
   G. Fostering national or international amateur sports competition
   H. Prevention of Cruelty to children or animals

2. Contributions to a 501 (c)(3) are generally tax deductible as charitable contributions to the donor . (Ref sec 1B page 22)

3. Nonexempt purposes (ref Sec 4B Line 6)
   If the organization is expressly empowered by its articles to carry on, other than as an insubstantial part of its activities, activities that are not in furtherance of its exempt purpose(s), it will not meet the organizational test even though its stated purposes are within the Code. For example, if the articles expressly reserve the power "to engage in a manufacturing business," or "to engage in the operation of a social club," the organizational test is not met.

4. Unrelated Business Income (Ref Sec 2 pg 7)
   a. Unrelated Business Income is any income that does not further the organizations exempt purpose.
   b. An exempt organization must file a form 990-T if it has $1,000.00 or more in unrelated business income and must make quarterly payments of estimated tax if more than $500.00 is owed.

5. Application for a 501 (C)(3) is Form 1023 (Ref Sec 3A) Key questions
   a. Part III Required Provisions in your Organizing Documents (Articles of Incorporation)
      i. Your organizing documents must state your exempt purpose(s) such as charitable, religious, educational and/or scientific purposes.
      ii. Describe specifically where your organizing documents meets this requirement by reference to a specific article or section

Final Report Section 5 continued

b. Part IV Successor Organization
    i. Are you a **successor** to another organization? Complete Schedule G to the application if you have taken over the activities of another organization or if you took more than 25 % of the net assets of anther organization. {see 4.c. below}
    ii. Do not file form 1023 Application until you have amended your organizing document. Submit both your original and amended organizing documents (showing state filing certification if you are a corporation)
c. Schedule G of IRS Form 1023 application. (abbreviated version)
    i. Question 2a. Are you a successor to an organization other than a for-profit organization? If so, provide the tax status and EIN of the predecessor organization and explain why you took over the activities or assets of the predecessor organization.
    ii. Questions 4 & 5. List the officers and governing board members of the Predecessor organization and describe in detail the relationship and activities of any of these members that will be maintaining a working relationship with you.

6. 501 (C)(3) Membership . Open to the public and is unrestricted.

Final Report Section 6

501 (C)(3) INVESTIGATION RESULTS { WMOTA}

Introduction: There are really two alternatives to creating a 501 (C)(3). These two alternatives are (1) a Successor Organization to WMOTA or(2) a new organization.

1. Successor Organization
a. In reviewing the Instructions for Application for Recognition for Exemption under Section 501 (C)(3) of the Internal Revenue Code {ref section 3A of the IRS Publications Notebook, one of the "RED FLAGS" is a "successor Organization". This is not specifically prohibited, but obviously the IRS is going to scrutinize an organization that is a "successor organization", because it requires a complete Schedule G on the application for "successor organizations".
b. Ref page 22: You should complete Schedule G of the application if you have taken or will take over the activities that were previously conducted by another. the" other" organization is the predecessor organization. You should complete this schedule G regardless of whether the predecessor was exempt or not exempt from federal income tax. In Schedule G, the IRS requires a narrative explanation of why you are taking over these activities.
c. The Articles of Incorporation would require amending to state that the purpose is one of the allowed exempt purposes.
d. Summary: The Successor Organization may be possible to create, but it raises many, many "red flags" to the IRS. It would require extensive amendments to our Articles of Incorporation and Bylaws.
e. Conclusion: WMOTA should <u>not</u> attempt to change from a 501(C)(7) to a 501(c)(3) Successor Organization.

2. Creation of a new 501(C)(3) Entity
    a. Select one of the 8 Exempt Purposes
    b. Create the Organizing Documents (Articles of Incorporation and Bylaws) specifically to support the Exempt Purpose.
    c. Make Application to the IRS using form 1023 or 1023EZ.
        i. As a new organization, the 1023 Application requires that a copy of the organizing documents (articles of Incorporation) certifying that the copy is a complete and accurate copy of the original and include evidence that the State has approved it.
        ii. In the application, describe specifically where your organizing documents meets this requirement by reference to a specific article or section
    d. Conclusion: A new entity could be created as a 501(C)(3), having an exempt purpose in accordance with the provisions of 501 (C)(3). This would be fairly easy to do and would not create the "Red Flags" that would be generated if WMOTA were to become a predecessor organization. If there is enough interest in forming such a new entity, the committee would recommend this avenue.

Final Report Section 7

COMMITTEE SSTATEMENT AND SIGNATURES

Committee members have unanimously agreed to the contents and conclusions of this Final Report:

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Jerry Smith, Chair

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Kristi Bruner, Member

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Ken Drozdowicz, Member

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Jim McKnight, Member