Tamarisk Country Club v. Commissioner, 84 T. C. 756 (1985)

Gain on the sale of property by a tax-exempt social club is recognized unless the full proceeds are reinvested in property used directly in the performance of the club's exempt function within a specified period.

Summary

Tamarisk Country Club, a tax-exempt social club, sold land it had purchased for expansion but later deemed unnecessary due to membership decline. The club argued for nonrecognition of the $148,640 gain under Section 512(a)(3)(D), claiming it had reinvested its equity in new property. The Tax Court, however, held that the full proceeds of the sale, not just the equity, must be reinvested to qualify for nonrecognition. The court's decision emphasized that the sale proceeds were used to reduce debt and refund assessments, not solely for exempt purposes, thus the gain was taxable.

Facts

Tamarisk Country Club, exempt under IRC Section 501(c)(7), purchased a 55-acre tract in 1972 for potential expansion of its golf course or recreational facilities. Due to declining membership, the club sold the land in 1974 for $850,000, realizing a gain of $148,640. The proceeds were used to refund membership assessments, pay off a loan, and cover selling expenses, with $260,959 retained. Within the required timeframe, the club spent $305,511 on new property for exempt functions.

Procedural History

The Commissioner determined a deficiency of $44,592 for the taxable year ending September 30, 1974, asserting the gain was unrelated business taxable income. Tamarisk filed a petition with the U. S. Tax Court, which heard the case and issued a decision on April 24, 1985, holding for the Commissioner.

Issue(s)

1. Whether, under IRC Section 512(a)(3)(D), gain realized by a tax-exempt social club on the sale of property used directly in the performance of its exempt function must be recognized to the extent that the sales proceeds exceed the cost of other property purchased and used directly in the performance of the exempt function?

Holding

1. Yes, because the full amount of the sales proceeds, less selling expenses, must be reinvested in property used directly in the performance of the exempt function to avoid recognition of the gain. Tamarisk's use of proceeds to reduce debt and refund assessments did not qualify for nonrecognition under the statute.

Court’s Reasoning

The court relied on the plain language of Section 512(a)(3)(D), which requires nonrecognition of gain only if the entire sales proceeds are reinvested in new property used for exempt purposes. The court rejected Tamarisk’s argument that only the reinvestment of its equity or profit was necessary, citing the Senate Finance Committee report indicating that the purpose was to allow nonrecognition when funds are reinvested, not when they are withdrawn for members’ benefit. The court also applied Section 1034, as referenced in Section 512(a)(3)(D), to interpret