

Country Clubs and Taxation: A Cost – Benefit Analysis of the Non-Profit Status of  
Country Clubs

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## **Introduction**

Many country clubs operate under the status of 501 (c) (7), which denotes them as non-profit organizations and grants them exemption from federal income taxes. The classification of 501 (c) (7) is for all social clubs: golf clubs, swimming clubs, tennis clubs, and, of course, country clubs. The purpose of these clubs is to provide members with “pleasure, recreation, and other non profitable purposes” (Langley and Rosenberg 1). While not all country clubs are non-profit organizations, most hold this status.

Why does it matter that country clubs receive these tax breaks? Taxes affect everyone, whether you are paying them or reaping the benefits of them. They help provide us with many services such as roads and healthcare. The taxes that would be generated from these clubs could reach far more people than the benefits that the members of country clubs receive. Additionally, through social capital and discrimination they contribute to the widening income gap that exists in the United States. While they host a variety of charity golf tournaments, tennis tournaments, and other events, their construction and operation can have effects that are very detrimental to the environment around them.

This paper will present information regarding country clubs and their tax exempt status. It will provide you with economic theory and literature that help explain their history and operation. It examines both the costs and benefits, both to society and to country club members, while using economic theory. From there an analysis will be presented of what these costs and benefits mean when we consider the bigger picture, developing an idea and vision for the future taxation of country clubs. Hopefully, it will present a new way of looking at country clubs and their non-profit status.

### **Non-profit status: Cost or benefit to society?**

There are both many costs and benefits of country clubs. They provide benefits and social capital for their members, produce charitable actions as well as community outreach, supply a substantial number of jobs, and benefit the communities surrounding them. Their exclusive structure is the reason that they are able to provide such benefits to their members, but this means that costs are incurred. The non-profit status of country clubs provides them with federal income tax exemptions as well as other tax exemptions. While these exemptions immediately benefit the organizations, they also lead to taxes lost for the greater society. In addition, country clubs produce negative environmental impacts and discriminate based on income, race, religion, and gender. Consequently, the ways in which they function have larger implications for society.

This paper will present past scholarship, research, and studies in order to demonstrate the need for a different system of taxation. It will then give some background information on the various costs and benefits presented, and provide theoretical reasoning as to why they are costs and benefits. From there it will analyze these factors to try and supply solutions for how to adjust the tax exemptions that country clubs receive. I argue that these adjustments can offer us a way in which country clubs can afford more benefits for all members of society, not just the members of the clubs.

### **Review of Literature**

Langley and Rosenberg outline the purpose of social clubs and the tax benefits. Country clubs are under the classification of 501(c)(7) when they are “organized for pleasure, recreation, and other non profitable purposes” (1). As such, they are exempt from federal income taxes. Langley and Rosenberg provide us with the purpose of social

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clubs as “to provide benefits to members” (1) with those benefits being many amenities such as golf courses, dining facilities, tennis courts, and swimming pools. In my examination of the costs and benefits of country clubs, their outline of social clubs provides some basic framework for the purpose and justification of the current status of country clubs, noting that the mission of social organizations is to provide the exact benefits that will be discussed later in the economic theory section of this paper. Their thesis presents the idea that Congress grants tax exemptions to country clubs because “when...benefits are funded by members.... members will be in the same position as if they had paid for the benefits directly” (1). Therefore, clubs’ income must come solely from the members for this to be true.

The concept of social capital will be key in developing the argument for social clubs and the benefits that they generate for society. Putnam (1993) provides a concept of social capital. Social capital is the idea that society gains benefits from the connections that are created between people by networking and through client involvement with society and their communities. People develop trust by making these social connections and this “trust lubricates social life” (3). Country clubs are one of the ways that communities help develop social capital. Putnam goes on to address the fact that many of America’s ghettos do not have organizations that are recognized as developing social capital; people aren’t making connections and building trust in these communities. The author suggests that this could be one of the causes of the ill conditions in these areas. Putnam refers to social capital as a prescription for many of these environments. Throughout the paper, he frequently offers social capital as the secret to developing our economy and improving our governmental system. The connections that are created and

the social capital aid in lubricating our economy as well as feeding political activism and other types of activism to assist in pushing policy and our government forward. The evidence from Putnam's article on social capital will be fundamental in developing the argument as to why country clubs provide social benefits.

Glaeser, Laibson, and Sacerdote provide the specific economic theory of social capital. They examine and develop a model that displays social capital consistent with the economic model of investment. This model helps show us how social capital can be a benefit to society. They note that "network membership often has strong positive externalities. The entire network benefits from each new membership, so the aggregate social capital will exceed the naive sum of individual investments" (443). In their study of social capital, however, they also give us a small examination of the cost of social capital for organizations like social clubs in comparison to those who are not in the organizations. When examining certain costs of country clubs, it must be noted that "if the network itself is undertaking activities which hurt other people, there may be positive externalities within the network but negative externalities toward society as a whole" (443).

Dietlind Stolle (1992) inspects whether or not social capital can be attributed to the group experience of joining an organization His work studies whether or not these associations within a club or congregation actually benefit those outside of the group. Stolle conducted studies of organizations in three countries: Sweden, Germany, and the United States. The author utilizes regression analysis to examine the various effects of group membership. Stolle found empirical evidence to support the hypothesis that being involved in more groups for longer amounts of time increases people's likelihood of

voting in elections. Much of Stolle's chapter is empirical evidence that supports Putnam's arguments for social capital, and therefore supports the argument for the societal benefits of country clubs. Although the article does find evidence for higher civic engagement with higher membership in organizations, it didn't find significant proof that this was very beneficial to wider society. In addition, Stolle also found that this trust that is created within associations is largely predetermined by those who self-select to join such organizations.

Scott R. Rosner examines why country clubs and social clubs similar to Augusta National in Georgia develop policies that promote exclusion. This article investigates the unique juxtaposition that arises from the economic importance of these clubs to our society but at the same time the judicial question of whether or not this exclusion is valid. Rosner reviews many precedent cases related to this issue where individuals have been discriminated upon the basis of race or gender or both. He also looks at legislation both on the state level and federal level as well as displays what has been done legally in the past. Rosner offers alternatives to what has been done in current legislation and proposes ideas such as the removal of liquor licenses or the repeal of income tax exemptions as well as property tax exemptions to the country club. Rosner claims that legal action needs to be taken with country clubs in order to bring about change and make them less exclusive. His argument questions the ethics and practice of member exclusivity.

## **Theory**

### *Benefits of Country Clubs*

Country clubs provide services to members. This is why they were developed and still exist today. When examining the Economic Theory of Clubs by James Buchanan, we are shown how they function through their structure and exclusivity. Country clubs are neither private nor purely public goods, and as such they must be examined under a different lens than either of these perspectives offer. If a good is public, it means that an individual's consumption is equal to the consumption of this good by all others. If a good is private, the good that is consumed by one individual reduces the potential consumption of others by the amount that they have consumed.

In order to provide benefits in an efficient manner, country clubs must operate as co-operative organizations: “if the single person is required to meet the full cost, he will not be able to enjoy the benefits of the good. Any enjoyment of the facility requires the organization of some co-operative collective sharing agreement” (Buchanan 7). This is a delicate balance because for every country club there exists an optimal size. No club can be too large or too small in order to provide the proper amount of benefits demanded by the club members. The “utility that an individual receives from its consumption depends upon the number of other persons with whom he must share its benefits” (Buchanan 3). As such, membership increases to reach an optimal point, due to the decreasing costs. This relationship provides more benefits to the members. As membership surpasses this optimal point though, we see a decline in benefits as congestion costs rise. This is the reason that country clubs demand exclusivity, because utility to individuals decreases as club membership increases.

This framework provides evidence as to why different country clubs have varying initiation fees as well as annual dues. Country clubs that offer amenities that are more

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extensive, elaborate, and extravagant must charge higher prices, as demand for these facilities is higher than the country clubs offering basic facilities. Not only do their services cost more, but more people want to be members at these country clubs. This necessitates the stratified pricing that we see among country clubs, those with big names and fancy facilities must demand higher prices in order to offer the exclusivity that their members require.

The social aspect of a country club is one of the main reasons that members join. If this factor was of little importance to members, they would go play golf at a public course or play tennis at a gym. This social aspect of country clubs generates social capital. Social Capital, defined as a person's "social skills, charisma, and the size of his Rolodex - which enables [them] to reap market and non-market returns from interactions with others" (Glaeser et. al. 438) is the economic way of measuring the social benefit. The joining of a country club produces network connections for members, in turn aiding in raising their status - an important aspect of social capital. The effects of this increasing social capital can be great for those who benefit: "market returns may include higher wages or better employment prospects for a socially skilled person. Non-market returns may include improvements in the quality of the individual's relationships, improvements in his health, or even direct happiness" (Glaeser et. al. 440) Social capital has been shown to provide utility and benefits not only to those who are participating in organizations such as country clubs, but also to society as a whole. Communities that have a large stock of social capital tend to operate more cooperatively and efficiently than those communities that are lacking it (Putnam 2).



The charitable actions and community involvement that many country clubs partake in are benefits that extend beyond these exclusive organizations. Members of country clubs often arrange charity golf tournaments, tennis tournaments, and other functions that can generate thousands of dollars for charities of their choice. Many of them, such as Greenbrook Country Club in New Jersey, have organized community involvement initiatives that are designed to reach outside of the country club, in order to help and offer benefits to others. These actions may include opening their doors to those who are less privileged and giving them an opportunity to learn how to play golf or tennis; fundraising and collecting and donating supplies for various non-profit organizations and charities; donating time to various charities; among many other various activities designed to benefit the wider community. These actions offer positive externalities for those effected, increasing social benefit for everyone, not just the members of the country club.

In addition to aiding outside community members, members of the club, who partake in such charitable giving, receive utility from donating. Many justify the negative externalities that result from other actions by negating them with the positive externalities that occur from charitable actions. Donating also aids in improving their personal image, in turn providing them with additional social capital. Additionally, donating leads people to believe that they are doing good for others besides themselves, thus creating a “warm glow” effect; ergo increasing personal happiness and providing utility to the donator.

Those who live on the perimeter of country clubs or near country clubs with golf courses (and most clubs do have golf courses) receive added benefits. In a study by Paul Asabere and Forrest Huffman (1996) it was found that houses located on golf courses had

premiums that are 8% higher than houses not on golf courses, but of comparable size and in similar areas. People value the utility that they receive from living near areas that provides recreation, nature, and aesthetically pleasing views. Often, these golf courses offer space to walk or exercise for residents with access. The increase in property value that the golf courses provide benefits the homeowners as well as the housing market. Additionally, the higher property values aid in keeping a community in good condition with regard to crime, safety, and general well being.

The last benefit to be discussed in this paper is the employment provided by country clubs. In 2012, country clubs provided 334,661 jobs in the United States (Golf Courses and Country Clubs Industry 4). The economic benefit of these jobs is explicit - they provide income for individuals, and that income aids in stimulating the economy as a whole. If country clubs were to lose their tax-exempt status, there would be a decrease in membership across the board as the trust signal is lost for many, and these new taxes will mean higher dues for members. When there is a decrease in membership, employees are let go, for not as many workers are needed.

#### *Costs of Country Clubs*

In addition to the federal income tax granted to country clubs, many receive exemptions from other taxes at the state level. Additionally, many clubs receive property tax breaks on their large, valuable land tracts. These tax breaks are based upon the provision that the organizations keep their property as open spaces (Jolly-Ryan 1). Some clubs have initiation fees of almost \$300,000 with annual dues that can surpass \$30,000. The taxes that could be generated if these institutions were not labeled as 501(c)(7) could have a heavy impact. When looking at it from a macroeconomic perspective, these tax

dollars could be used for government spending elsewhere, hopefully being put to more necessary measures that benefit more of society. These taxes could potentially reach more people than just members of the club who currently benefit from the tax exemption.

Another cost of country clubs is the environmental externality that many of them generate. When a golf course is initially built, the land is cleared of much natural vegetation and is subject to erosion, which can hurt land other than the golf course. The course construction has been shown in many places such as Jackson Hole, Wyoming to deplete habitat for wildlife, driving animals away from their home, such as bald eagles (Nauright and Wheeler 432). Often times, construction of a country club, with the clubhouse and other amenities, leads to the building of more commercial developments near the course, such as restaurants, spas, and shops. Subsequent commercial growth has a large environmental impact due to the amounts of electricity needed.

There are also many environmental impacts in the upkeep and maintenance of golf courses. Golf courses often use chemicals such as fertilizer, insecticides, pesticides and fungicides to keep their courses as green and as desirable as possible. These chemicals contribute to air pollution, but also seep into streams and groundwater, polluting those as well. These chemicals can be harmful to the health of those who spend a considerable amount of time on the golf courses. It has been estimated that “an 18-hole course consumes 3,000-5,000 cubic meters of water per day; enough to meet the daily consumption needs for 2,000 families or 15,000 individual Americans.” (Wheeler and Nauright 433). In the southwest, it has been noted that regardless of a drought, high prices for water, and limited access, golf courses will still manage to remain lush and

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green, often monopolizing much of the water supply (Deford). This environmental impact is a large cost of country clubs.

In addition to exclusivity and environmental externalities, we must consider discrimination as another large cost of country clubs. Many country clubs still discriminate on the basis of race, religion, and gender. Although both the fifth and the fourteenth amendments to the constitution prohibit this type of discrimination, many of these private clubs are able to deny membership on the basis of exemption from civil rights laws. This can translate to us seeing that this prejudice and bias are legal and subsidized through tax exemptions. Country Clubs, as discussed earlier, discriminate on the basis of income, but upon examining theories of status organizations and of clubs, this discriminatory pricing is necessary to provide the proper benefits to members. However, that does not mean that subsidizing it does not have detrimental effects for society.

This prejudice imposes a large cost to society and to those who are discriminated against, as they already are at a disadvantage. Women and people of color already have a harder time affording opportunities, and on average have a lower income than those who are white males. Those who are members of country clubs have higher incomes than most of society, residing in the upper class. The country clubs, through social capital accretion, aid them in gaining status and networking. The social capital for these individuals is not as necessary as the social capital needed for those outside of the country clubs. This gaining of status through these elite organizations can contribute to the widening income gap in the United States.

## Analysis

After outlining the costs and benefits of country clubs and explaining the theory behind them, the question begs: Would it be more beneficial to have country clubs classified as non-profit organizations or should we do away with their tax exempt status?

Without empirical information, it is hard to decide what the weight of each cost and benefit should be. I will theoretically analyze the costs and benefits to propose what should be done in the question of classification of country clubs. This is an economic paper, but it must be noted that ethics play a large role in this question.

Examination of costs and benefits clearly demonstrate that actions must be taken. The environmental impact that country clubs have is a huge negative externality. Something has to be done about this. I argue that there should be either a tax placed on clubs that do not try to mitigate their environmental impacts or a subsidy given to clubs that are not using pesticides, implementing methods of watering that help to lessen the amount of water needed, as well as employing other measures that negate their environmental impact. A tax would effectively bring in more revenue for the government and our economy, and in turn provide more incentive for clubs to not pollute than a subsidy would.

A large part of a country club's image lies in the charity golf and tennis tournaments that it provides. These are a huge benefit to society, but even country clubs that are not classified as non-profits, such as Vanderbilt Country Club, still have annual charity tournaments capable of generating hundreds of thousands of dollars. By examining these other clubs that are in the minority and not receiving tax exemption, we

can see that these very benefits will not be lost if country clubs lose their tax-exempt status.

If taxes are implemented upon these country clubs, membership will decrease. Clubs will have to meet their cost by either redistributing funds meant for other things within their club or raise dues for members. This will cause a decrease in amenities if funds are redistributed, an action which could cause members to leave. In the case of higher dues, there will also be exit by the members. This decrease in membership will in turn decrease the number of employees needed by the country club in question. Due to the recent recession, it is important to consider that country club memberships have been on the decline (Swartz). The addition of a tax on these clubs does not bode well for clubs or the people that they employ.

As for the discrimination aspect of country clubs, solutions are not as clear-cut. In order for the clubs to operate effectively and efficiently, they must use and practice price discrimination. This does not mean that price discrimination should be condoned through tax breaks. Country clubs can demand high prices in order to remain exclusive and only serve a certain sector of society, but tax exemption should not be an option for them.

In addition to price discrimination not warranting tax breaks, discrimination upon the basis of race, religion, or gender is morally and ethically wrong. Additionally, it provides negative externalities for the rest of society. The sector of society that would benefit the most from the social capital accrued are the very people excluded from these social clubs. If no action is taken, we support the widening income gap, a detrimental factor of society and give advantages to those who are already advantaged.

**What has to be done?**

What I am proposing is the implementation of a progressive-tax for country clubs, much like the progressive income tax utilized in the United States. Under a certain level of initiation fee and annual due requirement, non-profit status should be given and is deserved. Clubs are still offering services to members but in a way that is not extravagant or extremely advantaged. I know not what the benchmark should be, as further empirical research needs to be done to find what that optimal point. After a certain point, this progressive income tax would be implemented. This would hopefully mitigate the number of memberships lost, as those with higher incomes going to clubs with outrageous annual dues and initiation fees will likely have the disposable income to make up for this.

I also propose that an environmental tax be implemented on clubs. Based upon their environmental impact, a club will be taxed a certain amount. Clubs that mitigate their environmental impacts would then benefit from this. This will give clubs the incentive to reduce their impact and learn to operate in ways that are more environmentally efficient.

### **Conclusion**

Social clubs are created for “pleasure, recreation, and other non profitable purposes” (Langley and Rosenberg 1). While they do provide pleasure and recreation to their members, they do not always serve their non-profitable purpose. They use price discrimination as well as other forms of discrimination, and create tools that help further their members statuses and wealth through social capital. This is not a non-profitable purpose. Through outlining and examining the various costs and benefits that these tax exempt country clubs present, I move to say that we change the way that these country

clubs are classified and taxed. Using a progressive tax on country clubs based upon how much money they charge their members, we can provide greater benefits to society.

Taxing environmental impacts will also prove fruitful as well as aiding in the movement for country clubs to become more environmentally friendly.

Though many people in the United States are not members of country clubs, the tax status of these organizations affects all. The lack of taxation and the way that they contribute to the widening income gap is relevant to all society, and thus more Americans should become aware of it.

Moving forward, it would be helpful for more investigation to go into the empirical evidence needed to support this argument, as no empirical data was researched. Examining the exact environmental impacts, costs to the consumers, potential taxes generated, and quantifying the benefits that country clubs provide would be useful in finding out what would be the most beneficial plan of action to take.



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