



STATE BOARD OF EQUALIZATION

450 N STREET, SACRAMENTO, CALIFORNIA
PO BOX 942879, SACRAMENTO, CALIFORNIA 94279-0082
TELEPHONE (916) 322-3829
FAX (916) 323-3387
www.boe.ca.gov

BETTY T. YEE
Acting Member
First District, San Francisco

BILL LEONARD
Second District, Sacramento/Ontario

CLAUDE PARRISH
Third District, Long Beach

JOHN CHIANG
Fourth District, Los Angeles

STEVE WESTLY
State Controller, Sacramento

December 1, 2006

RAMON J. HIRSIG
Executive Director

Mr.
Chief Assessor Records and Exemptions
1600 Pacific Highway, Room 103
San Diego, CA 92101-2480

Re: San Diego Aircraft Carrier Museum – USS Midway

Dear Mr. :

This letter is in response to your correspondence of March 8, 2006, addressed to Mr. Dean Kinnee in the Property and Special Taxes Department regarding the application of the welfare exemption, as set forth in Revenue and Taxation Code section 214,¹ to an aircraft carrier museum which is also rented to private parties for social events. We conclude that the exemption applies to the portion of the property used exclusively for qualifying purposes.

Background and Facts

The museum consists of an aircraft carrier, the former *USS Midway* (“*Midway*”), as well as a possessory interest for the adjacent pier and a portion of the bay the vessel rests in. *Midway* served with valor in the United States Navy from 1945 to 1992.

After her final decommissioning, *Midway* was acquired via a contract with the United States Navy that placed her in stewardship of the San Diego Aircraft Carrier Museum. She was removed from long-term storage in Bremerton, Washington and towed to San Diego, arriving on January 5, 2004. The San Diego Aircraft Carrier Museum immediately began renovation of the *Midway* and the nearby pier to which she is anchored.

Since its opening, the museum has welcomed over a million visitors. The museum provides an educational experience for civilians, as well as active and retired military. Guests of the museum tour the ship with docents, some of whom served aboard the ship when she was active. Visitors may also choose self-guided tours, assisted by audio guides that explain the

¹ Unless otherwise stated, all section references are to the Revenue and Taxation Code.

workings of the ship and recount her history. Visitors also learn of the role aircraft carriers have played in this nation's history and receive an insight to US naval aviation.

The ship has an engine room, lower deck, hangar decks 1 and 2, flight deck and "island" (the superstructure containing the bridge and Captain's quarters). The pier accommodates the museum entrance, parking, supply elevator, as well as electrical, water and sewer connections for the ship.

To raise funds to support the mission of the museum, *Midway* is regularly rented for special events to individuals and for-profit organizations. Large areas on the flight deck and hangar decks are used for these events, as well as peripheral areas such as elevators, entrances and restrooms. The museum's Web site states that *Midway* can host up to 2,500 people for special events. As part of the package, tours of the ship are also made available. *Midway* hosted 135 special events during calendar 2005, with a total attendance at the events of 66,087. The attached schedule of events reveals that, of the average 336 hours of operation per month, 36 hours were devoted to special events.

The museum actively promotes the *Midway* as a place to hold these private functions. The *Midway* Web site includes a 30-page marketing brochure. The museum employs a marketing staff for private functions. (Brochure at p. 11.) The *Midway* has been named event site of the year in a national poll of meeting planners conducted by *Event Solutions* magazine. (Brochure at p. 3.)

The San Diego County Assessor's Office has valued *Midway* at \$4,000,000 and the possessory interest at \$2,275,750. The museum has applied for and been issued an Organizational Clearance Certificate ("OCC"). It has filed a claim for the welfare exemption from property taxation for fiscal year 2004-05. Our guidance on the following questions has been requested:

Question 1

Does the use of the museum for special events invalidate the exemption for the entire property?

Answer

No, claimant is entitled to a partial exemption.

Section 214, subdivision (a), requires that property for which the welfare exemption is claimed is used exclusively for religious, hospital, scientific or charitable purposes. The information you provided to us indicates that in addition to being a museum, the *Midway* is made available for a fee to for-profit-corporations, other non-exempt organizations, and individuals for business social functions, receptions and private parties. These activities are not qualifying activities, and are grounds for finding those portions of the property so used ineligible for the welfare exemption under section 214, subdivision (a).

The Revenue and Taxation Code does not specifically define the term *used exclusively*; however, the courts have done so in a series of decisions. The State Supreme Court, following a

rule of strict, but reasonable construction, has construed “exclusively used” in section 214, subdivision (a), to include any use of the property which is “incidental to and reasonably necessary for the accomplishment of the [exempt] purpose.”²

Thus, if the property is used primarily for exempt purposes, the term “exclusively” does not preclude activity, “which while not charitable in the traditional sense, is merely incidental to the charitable purpose and not in competition with commercial enterprise.” (See *Greek Theatre Assn. v. County of Los Angeles* (1978) 76 Cal.App.3d 768, 776, holding that a bar within a theater for the convenience of theatergoers “is used exclusively for a purpose incidental to the charitable function.”) In contrast, incidental uses, found to be “largely commercial in character” are viewed as disqualifying uses. (See *YMCA v. County of Los Angeles* (1950) 35 Cal.2d 760, 775, finding the YMCA’s restaurant, tailor and barber shop to be “largely commercial in character properly classifiable as business ventures.”) In *YMCA*, money derived from nonqualifying use which was used exclusively for the organization’s operations upkeep as a charitable organization did not alter the court’s conclusion that such uses were not merely incidental to and reasonably necessary for the accomplishment of exempt purposes. Thus, in qualifying for the welfare exemption, case law tells us that an organization’s use of its property for profit-making activities is to be scrutinized to determine if the activities are incidental to its exempt purpose, or whether the organization has engaged in an unrelated business activity that is conducted in a manner similar to a commercial enterprise.

Turning to the facts at hand, the use of the *Midway* as a place for businesses and private parties to hold their special events is similar to banquet facilities offered by hotels and restaurants, as well as other tourist venues in the San Diego area. In fact, the museum special events brochure even states, “[y]our event could be held in a ballroom or it could be held in the middle of a historic aircraft carrier . . .” (Brochure at p. 11.) Thus, the special events brochure indicates that the museum is marketing and using the *Midway* in a manner similar to commercial enterprises.

Accordingly, it is our opinion that the special events use is commercial in character, and not incidental to and reasonably necessary for the accomplishment of the *Midway*’s exempt purpose. Such planned systematic commercial use of the property is grounds for denial of the welfare exemption for the portions of the property so used. A qualifying organization’s property may be exempted fully or partially from property taxes, depending on how much of the property is used for qualifying purposes and activities. The welfare exemption may be claimed for the portion of the *Midway* used exclusively for exempt purposes; i.e., those portions of the *Midway* that are not used by private party special events.

Question 2

Can the special events use be considered non-disqualifying occasional fundraising?

² *Cedars of Lebanon v. County of Los Angeles* (1950) 35 Cal.2d 729, 736.

Answer

No. With respect to fundraising, subdivision (a)(3)(A) of section 214 provides that use of the property for fundraising will not disqualify the property if it is “occasional.” The specific language of subdivision (a)(3)(A)(i) of section 214 indicates this provision was added to allow qualifying organizations to conduct occasional fundraising on their properties to further their exempt activities without jeopardizing the exemption for their properties. “Occasional use” is defined by subdivision (a)(3)(B)(i) of section 214 as “irregular or intermittent” use that is “incidental to the primary activities of the owner. . . .”

As explained above, the provisions of section 214 expressly prohibit the continuous use of property for fundraising (section 214, subdivision (a)(3)(A)), and judicial precedent makes it clear that property used more than occasionally for fundraising purposes is not exempt, even if the proceeds are used for an exempt purpose (see *Cedars of Lebanon Hospital v. Los Angeles County, supra*; *Honeywell Info. Sys. Inc. v. Sonoma County* (1974) 44 Cal.App.3d 23). Thus, a nonprofit organization’s use of its property to generate income in an activity unrelated to its exempt purpose may disqualify the property if the use is more than occasional.

Applying these principles to the facts presented, we conclude that the *Midway* is being rented for special events by for-profit organizations and private parties more than occasionally. Your letter indicates that in its first year of operation the *Midway* was rented for use by private parties at least six times per month:

January :	10	July:	9
February:	8	August:	15
March:	7	September:	18
April:	14	October:	12
May:	12	November:	6
June:	15	December:	9

Use of the *Midway* for private party special events is not use of the property for exempt fundraising activity, but is a nonqualifying commercial activity which disqualifies from exemption those portions of the *Midway* used by private parties for special events.

Question 3

If a partial exemption is appropriate, how should it be calculated? Are the areas of the museum used for special events, including parking and elevators, entirely ineligible for exemption? If that is the case, should a pro-ration based on square footage be calculated for areas used for special events vs. areas not used for special events?

Answer

Areas of the museum which are not used exclusively for the exempt purpose do not qualify for the welfare exemption. Accordingly, those areas of the museum used by persons attending the private parties do not qualify for the welfare exemption. Thus, if the rental for special events includes the use of parking areas and elevators, those parking areas and elevators must be excluded from the portion the property for which the welfare exemption is allowed.

Question 4

Can a partial exemption be calculated based on a pro-ration of the time used for non-exempt activity? For example, if the museum were open 336 hours per month and 33 hours were used for special events, would it be appropriate for the museum to receive a 90% exemption?

Answer

No. The exemption is based on exclusive use of the property for exempt purposes. Only that portion of the property used exclusively for an exempt purpose can qualify for exemption.

Question 5

Does Revenue and Taxation 214.05 apply in this case? Should the exemption be calculated based on the amount of unrelated business taxable income (UBTI) reported to the Internal Revenue Service, even though the admission revenue portion from the special events is not included in the figure that the museum reports as UBTI to that agency?

Answer

Section 214.05 only applies to those properties where the property qualifies for the welfare exemption, but a portion of the exempt property is being used to generate income in a way which is related to the charitable purpose. An example is a museum gift shop. If the museum is exempt under the charitable purpose aspect of section 214, and the museum gift shop is exempt as a facility related to the primary charitable purpose of the museum and reasonably necessary and incidental to that purpose, but the gift shop generates unrelated business taxable income, the provisions of section 214.05 apply to determine the amount of the partial exemption for the gift shop. Thus, the provisions of section 214.05 do not apply to the facts here since the use of the property for special events is a nonqualifying purpose.

Question 6

How does section 214.14 (for property used exclusively for charitable purposes by museums) apply to the museum?

Answer

Section 214.14 reiterates the “used exclusively for charitable purposes” and “reasonably necessary and incidental” to those purposes requirements of the welfare exemption, for museums claiming the welfare exemption. Uncodified legislative intent states that the addition of section 214.14, made at the 1989-90 Regular Session of the Legislature, does not constitute a change in,

but is declaratory of, existing law. (Section 3 of Stats. 1989, Ch. 912.) The uncodified legislative intent further states:

It has never been the intent of the Legislature to disqualify from the welfare exemption those properties used for activities or facilities reasonably necessary and incidental to the charitable purposes of museums, including restaurants, cafes, bars, or other food service facilities, and bookstore/giftshops selling primarily educational materials, for the convenience of museum visitors and staff. (Section 1, subdivision (c), Stats. 1989, Ch. 912.)

In our opinion, neither the language of section 214.14 nor the uncodified legislative intent provide authority to extend the welfare exemption to museum property rented out to private parties as a place to hold special events as a commercial enterprise.

The views expressed in this letter are only advisory in nature. They represent the analysis of the legal staff of the Board based on present law and the facts set forth herein, and are not binding on any person or public entity.

Sincerely,

/s/ Nancy Vedera

Nancy Vedera
Senior Tax Counsel

NV:pb
Prec/Welexact/06/152.nv.doc

Attachments

cc: Mr. David Gau, MIC:63
Mr. Dean Kinnee, MIC:64
Ms. Mickie Stuckey, MIC:62
Mr. Todd Gilman, MIC:70