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Executive Director

October 18, 2001

VIA Facsimile and U.S. Mail

**Re: *Qualification for the Welfare Exemption of the
County***

Foundation, Los Angeles

Dear Mr. _____ :

This is in reply to your inquiry of May 30, 2001, in which you request our opinion concerning the property tax status of the _____ Foundation. Specifically, you would like to know whether the _____ Foundation is a qualified organization for purposes of section 214 of the Revenue and Taxation Code,¹ and whether its property would qualify for exemption from property taxes. As discussed below, the _____ Foundation can qualify under section 214, subd. (a) as a charitable organization, and its property can satisfy the requirements for the welfare exemption as property used exclusively for charitable purposes. However, the Foundation must amend its Articles of Incorporation to comply with the requirements in sections 214, subd. (a) (6) and 214.01 in order for its property to be granted the exemption. At your request, we have reviewed proposed amendments to the Articles, and we have determined that the proposed statement of irrevocable dedication complies with statutory requirements; however, the proposed dissolution clause requires revision, as specified in our facsimile of September 26, 2001 to Foundation staff.

Relevant Facts

The _____ Foundation (hereinafter Foundation) was incorporated as a California nonprofit corporation in 1952. _____ family members established the Foundation, provided funding, and also serve as Trustees. The purposes of the Foundation, as set forth in its Articles of Incorporation, are as follows:

To receive and administer all funds and property contributed by the founders or others for religious, charitable, scientific, literary or educational purposes, all for the public welfare and for no other purposes, all to that end to:

- (a) Receive property by gift, devise or bequest, subject to the laws regulating the transfer of property by will, and otherwise acquire and hold all property, real or personal, including shares of stock, bonds, and securities of other corporations.

¹ All section references are to the Revenue and Taxation Code unless otherwise indicated.

(b) Act as Trustee under any trust incidental to the principal objects of the corporation, and to receive, hold, administer and expend funds and property subject to such trust.

The Foundation makes grants to qualified nonprofit organizations exempt from federal income tax under section 501(c)(3) of the Internal Revenue Code. About ninety percent of its grants are made to such organizations in the Los Angeles area. According to the Foundation's 1999 Annual Report, nearly 50 million dollars in grants were distributed to nonprofit organizations to be used for charitable purposes, within the categories of culture, education, health and human services. The funds for such grants are from investment income derived from assets contributed by Family members.

The Foundation is classified as a private foundation for federal income tax purposes that is exempt from federal income tax under section 501(c)(3) of the Internal Revenue Code and exempt from state franchise tax under section 23701d of the Revenue and Taxation Code. The Foundation, however, is subject to an annual federal excise tax of 2 percent imposed on its net investment income. [IRC § 4940(a).] In 1999, the Foundation paid an annual excise tax of 1% on its net investment income because of the level of its qualifying distributions. [IRC § 4940(e)(1).]

The Foundation's real property is a three-story office building located at Boulevard in the City of (APN#). Personal property owned by the Foundation includes office furniture, equipment and paintings. The Foundation's real property was recorded in the name of the Foundation in a Corporation Grant Deed on in the Los Angeles County Recorder's office.

LAW AND ANALYSIS

I. Whether the Foundation's purpose of receiving, holding, administering and distributing funds to qualified nonprofit organizations comes within the charitable purposes aspect of section 214, subd. (a)?

A basic requirement for the exemption from property taxes provided in section 214 is that the organization which owns the property for which exemption is claimed, must be organized and operated for an exempt purpose, as specified. (§ 214, subd. (a).) Under subdivision (a) of section 214, the exemption is available for property used exclusively for charitable purposes, owned and operated by foundations organized and operated for such purposes if all the requirements for exemption are satisfied. (§ 214, subd. (a).) The charitable purpose aspect of the welfare exemption has been broadly construed by the California Supreme Court to include a wide range of activities that benefit the general public. (*Stockton Civic Theatre v. Board of Supervisors* (1967) 66 Cal.2d 13.) The primary test is whether the activity provides a general community benefit whose "ultimate recipients are either the community as a whole or an unascertainable and indefinite portion thereof." (*Stockton Civic Theatre, supra* at page 20.). This means that the class benefited must be sufficiently large that a gift to it may be considered to benefit an indefinite portion of the community.

As noted above, the Foundation is incorporated as a nonprofit corporation in California and is exempt from income tax under federal and state law. The Foundation's purpose is to provide grants to nonprofit tax-exempt organizations located in the greater Los Angeles area, which provide a broad range of cultural, educational, health and human services. The grants fund community activities including, but not limited to homeless programs, scholarships for financially disadvantaged students, cultural activities, as well as the construction and/or renovation of community facilities such as hospitals, schools, day care centers, theatres, and art museums. Thus, the Foundation's purpose is philanthropy, which is a charitable purpose within the meaning of section 214, subd. (a) The board staff has previously determined that other such philanthropic foundations were qualified organizations under the charitable purposes aspect of section 214. Our position is consistent with well-settled judicial precedent that charitable purposes are to be construed broadly. Moreover, the Foundation's grants to numerous community organizations may be construed as benefiting an indefinite portion of the community, satisfying the "community benefit" test of Stockton Civic Theatre.

II. Whether the Foundation's property qualifies for exemption as property used exclusively for charitable purposes.

Another basic requirement for the exemption from property taxes under section 214 is that the property must be used exclusively for exempt purposes. (§ 214, subd.(a).) The Revenue and Taxation Code does not define the term, "used exclusively;" thus, by necessity, it has been construed by the courts. The California Supreme Court has held that used exclusively [for exempt purposes] includes any property that is used exclusively for any facility, which is "incidental to and reasonably necessary for the accomplishment of the exempt purpose." (*Cedars of Lebanon v. County of Los Angeles* (1950) 35 Cal.2d 729.) The *Cedars* case clarifies that the phrase, "incidental and reasonably necessary for" refers to property that is normally associated with or related to the accomplishment of an exempt purpose. (see also page 23, of Assessors' Handbook, section 267, Welfare, Church and Religious Exemptions.)

Your letter indicates that the Foundation uses the entire office building for its operations. The Foundation is also claiming exemption for personal property, which includes office furniture, equipment and paintings.² The building is occupied by Foundation staff who review and interview grant applicants, for purposes of evaluating the quality of their programs and determining whether the community organizations are "well managed, fiscally sound, and have a developed history and maintain a record of program integrity." (page 90, Annual Report, 1999.) In our view, the building, office furniture, and office equipment are "used exclusively" for charitable purposes since this property is used to accomplish Foundation's charitable purpose of providing grants to tax-exempt community organizations. In addition, there are 20 paintings by early 20th century California artists, which are displayed in a large open area so that nearly all can be viewed at the same time by visitors to the building. In our opinion, the paintings should be considered exempt as part of the décor of a building, which we have determined, is used exclusively for charitable purposes.

² Foundation lists the paintings with a value of \$268,303 on its financial statement, dated October 31, 2000; but were recently appraised at \$400, 000 according to Foundation staff; however, no supporting documentation has been provided regarding the value of the paintings.

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III. Whether the Articles of Incorporation Satisfy the Requirements in Sections 214, subd. (a)(6) and 214.01.

A nonprofit organization must irrevocably dedicate its property to religious, hospital, scientific or charitable purposes, and its formative documents must contain a statement to that effect. (§ 214, subd. (a)(6).) Moreover, section 214.1 requires an express statement of irrevocable dedication to only those purposes. Similarly, a dissolution clause is required in the formative documents stating that upon dissolution of the organization, its assets are to be distributed to a nonprofit entity organized and operated for religious, hospital, scientific or charitable purposes. As we have discussed, the dedication and dissolution clauses in the Foundation's Articles of Incorporation are not in compliance with these statutory requirements. You have submitted for our review, proposed amendments to the Foundation's Articles, which we addressed in our facsimile of September 26, 2001 to Ms. _____, Treasurer of the Foundation. As noted in that correspondence, the proposed statement of irrevocable dedication in the dedication clause complies with statutory requirements; however, the proposed dissolution clause requires revision, as specified, to comply with the statutory requirements. Since we have already provided specific guidance in this regard, we will not address the language requirements again here.

IV. Conclusion

The Foundation's philanthropic purpose of providing grants is charitable purpose with the meaning of section 214, subd.(a). The real and personal property of the Foundation can satisfy the requirement for the welfare exemption as property used exclusively for charitable purposes. Finally, the Foundation will be required to amend its Articles, consistent with the guidance provided in our facsimile of September 26, 2001.

Very truly yours,

/s/ Mary Ann Alonzo

Mary Ann Alonzo
Senior Tax Counsel

MAA:tr
prop/prec/welexqal/01/23maa

cc: The Honorable Richard Auerbach
Los Angeles County Assessor

Mr. Dick Johnson, MIC:63
Mr. David Gau, MIC:64
Mr. Dean Kinnee, MIC:64
Ms. Hadley Alger, MIC:64
Ms. Lois Adams, MIC:64
Ms. Colleen Dottarar, MIC:64