



STATE OF CALIFORNIA

STATE BOARD OF EQUALIZATION

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Executive Secretary

February 29, 1988

Dear

This is in response to your February 15, 1988, letter wherein you enclosed a copy of a 1968 Statement from the Board concerning hospital gift shops and circumstances under which hospital properties used for hospital gift shops would be eligible for the welfare exemption from property taxation (Revenue and Taxation Code section 214, et seq.), and you requested a copy of the latest statement in these regards.

In instances in which a gift shop is owned and operated by a hospital meeting all of the requirements for exemption, the current statement set forth in Assessors' Handbook AH 267, Welfare Exemption, at pages 20 and 21 is the same as that in the 1968 Statement:

“(2) Hospital Gift Shops

“Under certain conditions, hospital gift shops operated in nonprofit hospitals will be regarded as within the coverage of the welfare exemption because such a shop is incidental to and reasonably necessary to a modern and complete facility. The exemption will apply if:

“(a) The gift shop is operated by the hospital or a hospital auxiliary on a nonprofit basis with net revenue, if any, being expended for the direct benefit of the hospital.

“(b) The shop will in no way seek to make sales to other than hospital patients and their visitors or to members of the medical staff or other hospital employees. Compliance with this proscription is best demonstrated by a total lack of advertising, the placement of the shop in the interior of the hospital, and the maintenance of an inventory particularly suited to the needs of the patients and hospital personnel.

In instances in which a gift shop is owned by a hospital meeting all of the requirements exemption but is operated by an auxiliary that is a separate organization, such as a corporation or noncorporate fund or foundation, each must file a claim for exemption, and that portion of the hospital's property used for the gift shop will be eligible for the exemption only if the operator as well as the hospital is an exempt organization which meets such requirements. As explained in Assessor's Handbook AH 267, Welfare Exemption, at page 8:

“A qualifying organization, ‘A’, is the owner of 10 acres of land and a building used for qualifying religious purposes A nonqualifying organization, ‘B’, operates a preschool in a portion of the building in a private nonqualifying manner. Since ‘B’ (the operator) is not qualified, ‘A’ (the owner) does not receive an exemption on the portion

of the property, building and land, used by 'B'. However, the remaining property, building and land, is exempt as it is used exclusively by a qualifying organization, 'A', for qualifying religious purposes."

As to the requirements for the exemption, section 214 provides, in part, that property used exclusively for religious, hospital, scientific, or charitable purposes owned and operated by community chests, funds, foundations, or corporations organized and operated for religious, hospital, scientific, or charitable purposes can be exempt. Thus, the auxiliary organization would have to be organized and operated for charitable or other exempt purposes, and it could not be organized or operated for profit (section 214 (a) (1)); no part of its net earnings could inure to the benefit of any private shareholder or individual (section 214 (a) (2)); and its property would have to be irrevocably dedicated to charitable or other exempt purposes, and upon the organization's liquidation, dissolution or abandonment, its property would have to inure to the benefit of a fund, foundation, or corporation organized and operated for an exempt purpose or purposes (214 (a) (6)). Property is deemed irrevocably dedicated to religious, charitable, scientific, or hospital purposes only if a statement of irrevocable dedication to only those purposes is found in an organization's originating document, such as in the articles of incorporation of a corporation (section 214.01).

Section 214.8 provides that with certain exceptions, the exemption shall not be granted to any Organization which is not qualified as an exempt organization under section 23701d or section 501 (c) (3) of the Internal Revenue Code. An organization shall not be deemed to be qualified as an exempt organization unless the organization files with the assessor duplicate copies of valid, unrevoked letter or ruling from either the Franchise Tax Board or the Internal Revenue Service, which states that the organization qualifies as an exempt organization under the appropriate provisions of the Bank and Corporation Tax Law or the Internal Revenue Service Code. Thus, a Franchise Tax Board letter to the effect that the auxiliary organization is exempt from state income tax under section 23701d or an Internal Revenue Service letter to the effect that the organization is exempt from federal income tax under section 501 (c) (3) would meet the requirement of the section.

If and when organizational requirements are met, it is then necessary for the auxiliary organization to establish that the property is actually used for an exempt activity or activities in order for it to receive the exemption. Thus, the property must be used for the actual operation of an exempt activity, and must not exceed an amount of property reasonably necessary to the accomplishment of the exempt purposes (section 214 (a) (3)), the property must not be used so as to benefit anyone through the distribution of profits, payment of excessive changes or compensations, or the more advantageous pursuit of her or his business or profession (section 214 (a) (4)), and the property must not be used for fraternal, lodge, or social club purposes (section 214 (a) (5)) .

In conclusion, Revenue and Taxation Code sections relating to the procedure for claiming the exemption include 254 (return of the property to the assessor and affidavit required), 254.5 (time for filing claim and financial statement required), and 270 (late filing).

Very truly yours,

James K. McManigal, Jr.
Tax Counsel

JKM/rz