



STATE OF CALIFORNIA

STATE BOARD OF EQUALIZATION

LEGAL DIVISION (MIC: 82)

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June 15, 1994

This is in response to your December 9, 1993, letter to Mr. James Barga pertaining to the matter of whether The Crystal Cathedral Ministries' productions and recordings of its "Glory of Christmas" and "Glory of Easter" performances and licensing of same to an outside company for use in pay-per-view television broadcasts would impact upon the availability of the welfare exemption for the Ministries' property upon which the productions and recordings took place.

Per your letter, in part:

"... we have enclosed a copy of the Agreement between the Ministries and an outside firm that lead to the television broadcasts. The Agreement is in the form of a licensing agreement, as the Cathedral produced the actual video tapes, and then licensed them to the outside company for use in the broadcasts. This would be similar to recording a church choir, and then licensing the tape of the choir to a record company for the production of beautiful Christmas albums and tapes.

"As was discussed by telephone, the Ministries embarked upon the project as a ministry to its many television viewers of the 'Hour of Power' weekly televised church service. Although the Ministries has offered live performances of the 'Glories', which depict the birth of Jesus Christ and His crucifixion and resurrection, for many years at the crystal Cathedral, many of the viewers outside of California could not afford to travel to the Cathedral for the performances. Many of its viewers had written asking if the Ministries would broadcast the Glories over television. In order to cover its expenses of creating television programs of the two Glories, the Ministries decided to broadcast the shows on pay per view television, which shows were the first two Christian shows ever broadcast over pay per view."

As you know, Revenue and Taxation Code Section 214 and following, which provide for the welfare exemption, permit property used exclusively for religious or charitable purposes owned

and operated by a qualifying organization organized and operated for religious or charitable purposes to be exempt from property taxation if certain requirements are met. Thus, Ministries has to be organized and operated for religious and/or charitable purposes, and it can not be organized or operated for profit (Section 214, subdivision (a) (1)). Also, no part of its net earnings can inure to the benefit. of any private shareholder or individual (Section 214, 'subdivision (a) (2)).

When these and other organizational. requirements are met, Ministries must then establish that its property is actually used for an exempt activity or activities. Thus, its property must be used for the actual operation of religious and/or charitable activities, and must not exceed an amount of property reasonably necessary to the accomplishment of religious and/or charitable purposes (Section 214, subdivision (a) (3)). Also, its property must not be used, among other things, so as to benefit anyone through the distribution of. profits, payment of excessive charges or compensations, or the more advantageous pursuit of their business or profession (Section 214, subdivision (a) (4)).

Ministries has met the requirements for exemption in the past. As to the "Glory of Christmas" and "Glory of Easter" performances, they are presented as part of the ministry. As to the productions and recordings of the performances, your letter indicates that Ministries itself did so, as part of its ministry also. Thus, we are of the opinion that Ministries' performances and productions and recordings thereof for the reasons and in the manner set forth above are religious activities of the kind contemplated by Section 214, and do not impact upon the availability of the exemption for Ministries' property.

As to the licensing of the recordings to an outside company for use in pay-per-view television broadcasts, the December 1, 1992, Agreement between Ministries and the licensee, apparently a for-profit corporation, provides in part:

"1. The Cathedral will. produce a master video tape of the 'Glory of Christmas' and of the 'Glory of Easter ', which tapes shall. be of television broadcast quality

"2. The Cathedral shall be responsible for all expenses associated with the production of the video tapes, . . .

"3. The Cathedral hereby grants to Licensee an exclusive license for the worldwide exploitation of the video tapes in the television broadcast medium, including but not limited to pay per view television, for a term not to exceed seven years, unless extended by the written agreement of the parties. The Cathedral expressly reserves the right to exploit the video tapes in the video cassette medium.

"4. Licensee hereby agrees to pay to the cathedral a royalty of sixty percent (60%) of the gross proceeds received by Licensee in the exploitation of the video tapes in the broadcast television medium. The parties acknowledge that the pay per view broadcast of the video tapes will generally require that at least fifty percent (50%) of the actual sales proceeds of the broadcast will be retained by the individual cable

companies, and an additional ten percent (10%) will be retained by the network providing the satellite transmission of the video tape. Therefore, the gross proceeds received by Licensee will generally be forty percent (40%) of the actual sales proceeds received by the cable companies, and the Cathedral's royalty shall be based upon these proceeds

“5. Notwithstanding the foregoing provision, it is understood and agreed between the parties that one hundred percent (100%) of all proceeds received by Licensee from the exploitation of the video tapes shall be paid to the cathedral until such time as the Cathedral has recovered its entire costs of production of the video tapes. . . .

“6. Licensee agrees to negotiate and enter into the necessary agreements with the networks, cable companies or any other entity that may be required for the exploitation of the video tapes in the broadcast television medium. Licensee shall be responsible for all Costs. . . .

Again, the purpose of the licensing of the recordings was to make the performances available to Ministries' viewers outside of California who were unable to attend the performances in person. Under the Agreement, the licensee undertook to negotiate with networks and cable companies to arrange for the showing of the recordings and to make the financial arrangements. After payment of network and cable companies' charges, and after payments to Ministries to reimburse it for its costs of production, Ministries and licensee were to divide the remaining gross proceeds as provided in Paragraph 4. Per your December 9 letter in this regard:

"Unfortunately, the Ministries has not been able to cover its costs of the production, and for that reason is seeking to continue the pay per view broadcasts in an effort to 'break-even' in this ministerial project. For this reason, the outside company has not received any monies from the broadcasts, as the Ministries is to recover its expenses before the outside company is entitled to any funds. An accounting on the losses of the programs is also enclosed for your review."

As indicated above, Section 214, subdivision (a) (3) requires that property be used for the actual operation of an exempt activity. Thus, to be eligible for exemption, property must be so used, not used for fundraising, the proceeds of which are then used for the accomplishment of an exempt purpose or purposes. Property used for fundraising purposes is not used for exempt purposes.

In *Cedars of Lebanon Hospital v. Los Angeles County*, 35 Cal.2d 729, wherein the hospital sought the welfare exemption for that portion of its premises upon which a thrift shop was being operated for sales of donated clothing, the proceeds from which were devoted to the upkeep of a free children's clinic, the California Supreme court held that the exemption was not available therefor. Although the proceeds were used for the accomplishment of exempt purposes, the property for which the exemption was claimed was not being used for the actual operation of the exempt activity.

More recently, in *Honeywell Information Systems, Ina. v. Sonoma County*, 44 Cal.App.3d 23, wherein Honeywell sought to avail itself of the public schools exemption for a computer system leased to Sonoma County Schools and used by Schools (96.44% of total time), by parochial schools (3% of total time), and by private business (.56% of total time), the proceeds from the latter's use of which were used by the County for its general purposes, the District Court of Appeal held that the exemption was not available therefor. In that instance, the property for which the exemption was claimed was not being used exclusively for the actual operation of an exempt activity but rather, it was being used partly therefor and partly for fundraising.

In this instance, Ministries presented the performances, etc., on its property itself and then engaged licensee to perform a service for it, that of making arrangements for pay-per-view showings of the recordings, in return for a fee. The fee was 60 percent of 40 percent of the gross receipts, or, 24 percent of gross receipts (Paragraph 4 of the Agreement).

Organizations qualifying for the exemption can and do, of course, contract for the performance of services by others. Generally, such contracts are not considerations for welfare exemption purposes. Where the services involve the use of an organization's property in some aspect, however, the nature and extent of that use must be considered. Thus, examination of the licensee's use of Ministries' recordings under the Agreement is necessary.

As to the making of arrangements for the pay-per-view showings of the recordings, under the Agreement, licensee was responsible for doing so. There is nothing then which would indicate that Ministries was involved in licensee's negotiations with networks and cable companies, in the resultant agreements pertaining to gross receipts and divisions thereof between them, or in any other aspects of the relationships. And there is, apparently, nothing which would indicate that licensee's agreements with networks and cable companies were distinguishable from networks' and cable companies' agreements with others such that it could be concluded that those agreements could be considered to be fundraising agreements. Based on the available information, we would not view licensee's agreements with networks and cable companies as fundraising agreements.

As to the fee arrangements, we are not aware of any authority that would make an agreed-upon 24 percent (Ministries) - 16 percent (licensee) division of gross receipts from such efforts fundraising per se for purposes of the welfare exemption. The Agreement suggests that 60 percent of gross receipts is typically taken by networks and cable companies, and the remaining 40 percent would have been the subject of negotiation between Ministries and licensee, as would have been the matter of payment of Ministries' costs of production. Nor does the agreed-upon division of gross receipts appear to have risen to a level of fundraising by Ministries in this instance. In addition to a relatively equal division of the remaining gross receipts, the history under the Agreement, which is available by virtue of the fact that Ministries' inquiry occurred subsequent to the Agreement's execution and implementation, is that Ministries' costs of production have yet to be satisfied and that Ministries has received no funds under the Agreement other than amounts for reimbursement of some of its costs.

Accordingly, in our view, the licensing of the recordings under the above-mentioned circumstances and under the Agreement does not run afoul of the use for the actual operation of an exempt activity requirement of Section 214, subdivision (a) (3).

Neither do we believe that the Agreement runs afoul of the requirements of Section 214, subdivision (a) (4). As indicated, the 40 percent would have been the, subject of negotiation between Ministries and licensee, and there is nothing to indicate that licensee's compensation under the Agreement was excessive, or that Ministries' property was used to benefit licensee through the more advantageous pursuit. of its business. Rather, the history of the Agreement indicates that the opposite has occurred.

As you know, the welfare exemption requires an annual filing by the claimant with annual review by this Board and the County Assessor. Since the Assessor may deny the claim of an applicant the Board finds eligible for the exemption (Revenue and Taxation Code Section 254.5), you may wish to obtain the opinion of the orange county Assessor also in this regard.

A final consideration is Ministries' possible sales or other exploitation of the video tapes in the video cassette medium (Paragraph 3 of. the Agreement).

Where church presentations have been recorded. and made available to those in attendance or to others who might be interested, the sales prices have been established to recover costs, and no substantial net income is realized from such sales, we have been of the opinion that the selling of such recordings would not run afoul of the use for the actual operation of an exempt activity requirement of section 214, subdivision (a) (3) and would not be considered fundraising under the section and applicable cases. In this instance, apparently, Ministries has not proceeded to sell or otherwise exploit the tapes in the video cassette medium, for there is no mention of it in your letter.

Were Ministries to so proceed, however, because costs or most costs for production would have been reimbursed under Paragraph 5 of. the Agreement, the basis for sales or other prices and costs to be recovered, as applicable, would have to be considered vis-a-vis the Section 214, subdivision (a) (3) and no fundraising requirements. Also, in our view, no substantial net income could be realized from such sales.

Very truly yours.

James K. McManigal, Jr.
Staff Counsel III

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CC: Honorable Bradley L. Jacobs
Orange County Assessor
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Mr. Jim Barga, MIC: 64
Ms. Jennifer Willis, MIC:70