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Taxation

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TAXATION

I. Income Tax — Nonprofit Organization Exemption

In *Elmwood Cemetery Association v. South Carolina Tax Commission*,[1] Elmwood Cemetery, which was chartered as an eleemosynary corporation, brought an action against the South Carolina Tax Commission for a judgment declaring that the Association was exempt from the payment of income taxes by statute[2] and restraining the Commission from assessing or attempting to collect any tax from it. The Tax Commission contended that the action could not be maintained because of the rule of sovereign immunity and, furthermore, because the action was not authorized by the provisions of the taxing statutes.[3] The court accepted the Tax Commission's contention and held that the only remedy provided by statute[4] is the payment of the tax under protest, whether such tax is legally due or not, followed by a suit at law for recovery of this amount. The court said that the exclusiveness of this statutory remedy is provided by law[5] and its adequacy has been frequently decided.[6]

II. Income Tax — When Income Is Taxable

In *Woodward v. South Carolina Tax Commission*[7] the court decided that the gain from the sale of land is taxable in the year in which the deed and mortgage are delivered into escrow.[8]

Elizabeth Woodward[9] entered into an agreement for the sale of land wherein she agreed to execute a deed and take a mortgage as security for the purchase price. The consideration was agreed upon as $1000 per acre with an estimated 500 acres in the tract.

1. 253 S.C. 76, 169 S.E.2d 148 (1969).
2. S.C. Code Ann. § 65-226(3) (1962) provides in part that cemetery corporations and corporations organized for religious, charitable, or educational purposes shall be exempt from taxes under this chapter.
3. S.C. Code Ann. § 65-2655 (1962).
4. S.C. Code Ann. §§ 65-2661, -2662 (1962).
5. S.C. Code Ann. § 65-2655 (1962) provides: "There shall be no other remedy than those provided in this chapter in any case of the illegal or wrongful (a) collection of taxes, (b) attempt to collect taxes . . . ."
6. Chesterfield County v. State Highway Dep't, 191 S.C. 19, 3 S.E.2d 686 (1939); Textile Hall Corp. v. Riddle, 207 S.C. 291, 35 S.E.2d 701 (1945).
7. 174 S.E.2d 344 (S.C. 1970).
8. The year in which the gain was received becomes material because of the statutory changes made after 1959 affecting capital gains and reporting of income on the installment method. See S.C. Code Ann. §§ 65-258(6), -286 (1962).
9. Hereinafter referred to as Mrs. Woodward.

The deed and mortgage were delivered into escrow so that the parties could later adjust the consideration to conform with the acreage shown by an "accurate survey."[10] The agreement further stated that "the deed and mortgage may be held in escrow and not recorded until necessary."[11] The survey, showing the tract to contain 414 acres, was completed in 1959. The results of this survey were not accepted by Mrs. Woodward until 1960. Partly because of the prolonged discussions relative to the shortage in the acreage in the tract, the deed and mortgage were held in escrow and were not recorded until 1961.

The Tax Commission made a deficiency assessment for income taxes based upon the sale of the land and receipt of the gain in the year 1959. The taxpayer, contending that the sale was not completed and the gain not received until 1961, paid the taxes under protest and brought suit to recover the amount paid.[12]

The court held that the execution of the deed and mortgage and their delivery into escrow clearly vested title to the land in the grantee and that the sale was complete for income tax purposes at that time. The only condition of the escrow was the making of an accurate survey, and this was for the sole purpose of fixing the amount of consideration, since the exact acreage in the tract was unknown.[13] The fact that the parties did not finally recognize the accuracy of the survey until after 1959 did not alter its binding effect.

The court also had to decide when the gain from the sale should be recognized if the sale were complete in 1959. The taxpayer contended that she received nothing of value in connection with the transaction until 1961 and therefore received no taxable income until that time. The court said that taxable income is earned and received "[w]hen all events have occurred which fix its amount and determine the liability of the party from whom it is forthcoming to pay."[14] Although the deed and mortgage were not recorded until 1961 and the purchase price of the property was to be paid in installments in the future, the liability of the parties became fixed in 1959, and the sale was taxable in that year.

10. 174 S.E.2d at 345.
11. *Id.*
12. As provided in S.C. CODE ANN. §§ 65-2661, -2662 (1962).
13. 174 S.E.2d at 346.
14. Adams v. Burts, 245 S.C. 339, 346, 140 S.E.2d 586, 590 (1965).

III. LICENSE TAXES — REINSURANCE PREMIUMS

In *Southeastern Fire Insurance Co. v. South Carolina Tax Commission*,[15] Southeastern, a South Carolina corporation, reinsured contracts of insurance issued by Emerald Fire and Casualty Insurance Co. The Tax Commission levied a two percent tax on the reinsurance premiums collected by Southeastern on the ground that they constituted a part of Southeastern's total premium income as contemplated by the statute[16] and therefore were taxable. Southeastern paid the tax under protest and sued to recover the amount so paid; Southeastern contended that the premiums paid Southeastern by Emerald were not within the scope of the statute[17] because the contract was one of indemnity and not one of insurance.

The taxing statute involved here taxes "total premiums . . . from insurance contracts . . ."[18]; therefore, the question before the court was whether this statute refers to insurance contracts only, or to both insurance and reinsurance contracts. The court said that, if the terms of the statute are susceptible of more than one interpretation, they must be construed to give effect to the intent of the legislature. "The legislature by failing to specify that the taxing statute applies to reinsurance as well as insurance may have been attempting to encourage reinsurance."[19] The court said that there is no question but that the state has received two percent of the premiums which were paid by insured persons to Emerald, and undoubtedly the legislature did not intend that these persons should bear the brunt of another two percent tax.[20]

The court also noted that premiums paid for reinsurance by a foreign corporation would not be subject to such tax and, therefore, to hold South Carolina corporations as taxable on

15. 253 S.C. 407, 171 S.E.2d 355 (1970).
16. S.C. CODE ANN. § 37-130.2 (1962) provides:
> [T]here is hereby levied upon each domestic fire insurance company, each domestic accident and health insurance company, each domestic casualty or surety company and all other domestic insurance companies of any class . . . an additional and graded license fee in an amount equal to two per cent of the total premiums, that is, total premium income or total premium receipts for insurance contracts . . . .

17. *Id.*
18. *Id.*
19. 253 S.C. at 411, 171 S.E.2d at 356.
20. Although the tax is not levied against the insured individuals, it is inescapable that the payment of taxes is a cost of doing business and must be passed on to the policyholders.

these premiums would indicate that the legislature intended to discriminate against its own domestic corporations.

IV. LICENSE TAXES — REASONABLENESS

The City of Newberry enacted an ordinance in 1966 known as the City of Newberry Business and Professional License Ordinance under which enterprises doing business in the city were required to obtain a license. The license was to be issued upon payment of a tax based on the gross receipts of the business in the previous year that were earned within the City of Newberry. In *United States Fidelity and Guaranty Co. v. City of Newberry*,[21] the plaintiff insurance company paid the required amount to obtain the business license and brought an action for its recovery on the theory that the tax imposed upon the company was "unjust, unreasonable, confiscatory, or excessive."[22]

The insurance company presented two arguments attacking the ordinance. First, it contended that license tax charges for other businesses, as compared to charges for fire and casualty insurance companies, showed that in and of itself the charges for the insurance companies were unreasonable. Rejecting this argument, the court stated, "The fact that one class may pay more proportionately than other classes does not, of itself, make the license fee unreasonable or arbitrary since this is largely within the discretion of city council."[23] The court said further, "In the absence of positive evidence to the contrary, acts or ordinances licensing or taxing an occupation or privilege are presumed to be reasonable, and the courts will not interfere unless their unreasonableness and oppressiveness is clearly apparent . . . ."[24]

Second, the insurance company argued that the license tax was unreasonable because the company was losing money as a property insurer. The court also rejected this argument and upheld the ordinance; in so doing, the court decided that profits and losses are not a proper consideration in determining reasonable amounts to be charged for licenses, especially when the taxpayer, as here, is regulated as to rates by a government agency and may obtain an increase in rates upon a proper showing.[25]

21. 253 S.C. 197, 169 S.E.2d 599 (1969).
22. *Id.* at 199, 169 S.E.2d at 600.
23. Great Atl. and Pac. Tea Co. v. City of Spartanburg, 170 S.C. 262, 170 S.E. 273 (1933); City of Columbia v. Putnam, 241 S.C. 195, 199, 127 S.E.2d 631, 633 (1962).
24. 53 C.J.S. *Licenses* § 16 (1948).
25. S.C. CODE ANN. § 37-673, -683 (1962).

V. ESTATE TAX — ALLOWABLE MARITAL DEDUCTION

In *White v. South Carolina Tax Commission*[26] the administrator of the estate of Benjamin F. Adams filed an estate tax return wherein he deducted one-third of the adjusted gross estate from the taxable estate as the marital deduction of the widow. The Tax Commission determined that the amount of the allowable marital deduction should be reduced to a value equal to that calculated after the allowance for state and federal estate taxes and imposed a deficiency assessment. The administrator paid this deficiency under protest and filed suit for recovery of the amount so paid.[27]

The court said that by the passage of the marital deduction provisions[28] Congress left the common law states where, if they so desired, they could allow their citizens the full benefit of the marital deduction provisions by casting, or not casting, the burden of the tax upon property that would otherwise pass free of tax to the surviving spouse. Therefore, the method used by the Tax Commission for determining the allowable marital deduction is correct only if the law of South Carolina imposes the tax upon the widow's distributive share. In holding that the law of this state does not impose such a tax on the share passing to the widow, the court cited the rationale of the Court of Appeals for the Fourth Circuit as expressed in *Pitts v. Hamrick*,[29] in which the Internal Revenue Service took the identical position of the Tax Commission here. The South Carolina Supreme Court said, "Where the estate is to receive the benefit of the deduction of the widow's share . . . it would be unfair and unjust to require her share to bear any portion of the tax . . . ."[30] Further, there is no provision in the law of South Carolina which requires such a result.

The court had previously held that assets not includible in the taxable estate and which generate no part of the estate tax should not be burdened with the payment of any portion of the tax[31]; this holding is strengthened by the result of the presently surveyed case.

26. 253 S.C. 79, 169 S.E.2d 143 (1969).
27. Pursuant to S.C. CODE ANN. §§ 65-2661, -2662 (1962).
28. 26 U.S.C. § 2056 (b)(4) (1952).
29. 228 F.2d 486 (4th Cir. 1955).
30. *Id.* at 490.
31. Myers v. Sinkler, 235 S.C. 162, 110 S.E.2d 241 (1959).

Another argument presented by the Commission was that, if the widow were allowed to receive her one-third share free from the estate tax, the children, after payment of the tax, would each receive less net proceeds than the widow, and this result would be in contravention of the Statute of Descent and Distribution.[32] The court, rejecting this argument, said that the legislature saw fit to impose the tax on the distributive shares passing to the children, but not to impose a tax upon the distributive share passing to the widow.

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32. S.C. CODE ANN. § 19-52 (1962).