

4971 Lubin

THE STATE OF SOUTH CAROLINA
OFFICE OF THE ATTORNEY GENERAL
COLUMBIA

OPINION NO.

September 29, 1992

SUBJECT: Water District Dissolution - Requirements
under S.C. Code Ann. § 33-35-20 (1990) and
Internal Revenue Code § 501(c)(12).

SYLLABUS: The General Assembly intended to ensure
that dissolutions and final liquidations of
corporations subject to § 33-35-10 et seq.
are conducted in such a fashion as to
obtain the exempt status afforded by
Internal Revenue Code § 501(c)(12). A
corporation's bylaw, such as that of a
Water District, is consistent with §
33-35-20 when, upon dissolution or final
liquidation of the corporation, the bylaw
states that residual assets are deemed
distributed to the members and former
members based on their patronage of the
company, and further states that such
distribution is then deemed donated to an
organization described in § 501(c)(12) of
the Internal Revenue Code.

TO: Honorable Thomas L. Moore
Senator, Aiken and Edgefield Counties

FROM: Sarah G. Major *SGM*
Assistant Attorney General

APPLICABLE LAW: S.C. Code Ann. § 33-35-20 (1990).

QUESTION: Is a corporation's bylaw consistent with §
33-35-20, S. C. Code of Laws (1990) when, upon dissolution or
final liquidation of the corporation, the bylaw states that
residual assets are deemed distributed to the members and
former members based on their patronage of the company and
further states that such distribution is then deemed donated
to an organization described in § 501(c)(12) of the Internal
Revenue Code?

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DISCUSSION:

The Montmorenci-Coughton Water and Sewer District (Water District) is a "Federally-Financed Nonprofit Corporation" under S.C. Code Ann. Chapter 35, Title 33. The Water District has applied for tax exempt status under Internal Revenue Code (IRC) § 501(c)(12).

In order to qualify as an exempt organization under IRC § 501(c)(12), organizations must be operated on a true mutual or cooperative basis. Accordingly, the individual member's rights to any excess or residual assets generated by the company may not be terminated by the withdrawal of the member or upon dissolution. See Revenue Ruling 72-36, 1972-1 C.B. 151. Thus, upon dissolution the residual assets must be distributed to the corporation's members or former members in accordance with the members' patronage of the Water District.

Section 33-35-20 addresses the distribution of residual assets when a corporation like the Water District dissolves or has its final liquidation.

... upon dissolution or final liquidation, the residual assets will be turned over to one or more organizations which are organized and operate for similar purposes which themselves are exempt as organizations described in section 501(c)(12) of the Internal Revenue Code of 1954, or the corresponding provisions of any prior or future Internal Revenue Code, or the Federal, State or local government for exclusively public purposes.

Read literally, § 33-35-20 appears to require a direct transfer of residual assets from one IRC § 501(c)(12) organization to a similar IRC § 501(c)(12) organization after a dissolution. As previously discussed, the Internal Revenue Code does not allow a direct transfer of this type. It is, therefore, necessary to determine the intent of the Legislature in enacting § 33-35-20.

In Browning v. Hartvigsen, ____ S.C. ___, 414 S.E.2d 115 (1992), the South Carolina Supreme Court recognized the need to look at the intent of the Legislature in interpreting statutes.

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We are mindful that our primary function in interpreting a statute is to ascertain the intent of the legislature. *Multi-Cinema, Ltd. v. South Carolina Tax Commission*, 292 S.C. 411, 357 S.E.2d 6 (1987). A statute as a whole must receive a practical, reasonable, and fair interpretation consonant with the purpose, design, and policy of the lawmakers. *Caughman v. Columbia Y.M.C.A.*, 212 S.C. 337, 47 S.E.2d 788 (1948). The real purpose and intent of the lawmakers will prevail over the literal import of the words. *S.C. Department of Social Service v. Forrester*, 282 S.C. 512, 320 S.E.2d 39 (Ct. App. 1984).

Here, the intent of § 3-35-20 is to assure that upon dissolution the assets are treated in a fashion that will result in exempt status under IRC § 501(c)(12). The exempt status of an IRC § 501(c)(12) corporation can be achieved only where dissolution assets are distributed in accordance with the Internal Revenue Code. To interpret the statute in a manner that defeats tax exempt status leads to an absurd result. "However clear the language of a statute may be, the court will reject that meaning when it leads to an absurd result not possibly intended by the legislature." *Hamm v. South Carolina Public Service Commission*, 287 S.C. 180, 336 S.E.2d 470 (1985).

Based on the intent of the General Assembly to require § 33-35-20 to achieve exempt status for a corporation as an IRC § 501(c)(12) organization, the statute must be construed to effectuate that purpose. Such a construction is reached by concluding the General Assembly intended the assets be distributed to the members and former members (i.e. satisfying IRC § 501(c)(12)) who then contribute those assets to an IRC § 501(c)(12) entity. Such a construction accomplishes the intention of the General Assembly.

The bylaws of the Water District are consistent with the statute. The bylaws of the Water District provide, in part:

In the event the Corporation should dissolve in accordance with the Statutory Laws of the State of South Carolina,

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then, ...

(6) In the event of residual assets, the said residual assets will be deemed to be made to members or former members on the basis of their business with the Corporation and then such Members or former Members will be deemed to distribute or donate their assets to one or more organizations which are organized and operate for similar purposes which themselves are exempt as organizations described as § 501(c)(12) of the Internal Revenue Code as now enacted or as may be hereafter enacted or amended from time to time.

This bylaw passes the assets to the members in the true mutual fashion as required by IRC § 501(c)(12). Further, the bylaw results in contributing the assets to another entity bound by the same mutual and cooperative basis. Accordingly, the Water District's bylaw is consistent with the requirements of § 33-35-20.

CONCLUSION:

The General Assembly intended to ensure that dissolutions and final liquidations of corporations subject to § 33-35-10 et seq. are conducted in such a fashion as to obtain the exempt status afforded by Internal Revenue Code § 501(c)(12). A corporation's bylaw, such as that of a Water District, is consistent with § 33-35-20, S.C. Code of Laws (1990) when, upon dissolution or final liquidation of the corporation, the bylaw states that residual assets are deemed distributed to the members and former members based on their patronage of the company and further states that such distribution is then deemed donated to an organization described in § 501(c)(12) of the Internal Revenue Code.

SGM:rra