

1984 WL 249710 (S.C.A.G.)

Office of the Attorney General

State of South Carolina

March 28, 1984

***1** Revenue and Taxation—Income Tax—Taxability of Dividends Paid On Federal Home Loan Bank Stock.

Dividends received by a member bank on stock it holds in a Federal Home Loan Bank are subject to state income tax.

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QUESTION:

Are dividends received from stock ownership in a Federal Home Loan Bank taxable income?

APPLICABLE LAW:

[12 United States Code](#), §§ [1421](#), [1423](#), [1424\(a\)](#), [1426\(a\)](#), [1426\(c\)](#), [1426\(k\)](#), [1436](#), [1447](#) and [1464\(h\)](#); §§ [12-1-60\(2\)](#), [12-7-560\(4\)](#), [12-13-30](#), [34-25-210](#) and [35-1-20\(12\)](#), [South Carolina Code of Laws](#), 1976, as amended.

DISCUSSION:

[Title 12, U.S.C. § 1421](#), et seq., sets forth the Federal Home Loan Bank Act. Such Act establishes several Federal Home Loan Banks by districts ([12 U.S.C. § 1423](#)) and authorizes such banks to issue capital stock ([12 U.S.C. § 1426\(a\)](#)). Savings and loan associations, building and loan associations and other savings banks are eligible to become members of a Federal Home Loan Bank ([12 U.S.C. § 1424\(a\)](#)) and subscribe to the capital stock ([12 U.S.C. § 1426\(c\)](#) and [12 U.S.C. § 1447](#)).

The members receive dividends on their stock ([12 U.S.C. § 1426\(k\)](#)) with such dividends being paid by the Federal Home Loan Bank from net earnings after reserves ([12 U.S.C. § 1426](#)).

[Section 12-13-30](#) imposes an income tax upon an association's net income from all sources “ * * * except for income from municipal, state or federal bonds or securities exempted by law from such tax”. Thus in order for the dividend income to be exempt, the stock, since it is not a bond, must be a security with the income from such security exempted by law from income tax.

In determining the meaning of words in a statute, such words should be given their ordinary and popular significance. [Beach v. Livingston](#), 248 S.C. 135, 149 S.E.2d 328. “Security” in its ordinary meaning is “written evidence of ownership or creditorship; especially, a stock certificate”. American Heritage Dictionary. Further, security is defined at [§ 35-1-20\(12\)](#) as including stock. Thus, the stock owned by the association in the Federal Home Loan Bank is a security.

The requirement that income from such security be exempt by law from income tax, however, is not satisfied. Such dividend income from the stock is not exempt under federal or state law.

In determining what income from securities is exempt by state law, [§ 12-1-60](#) is instructive. This section “exempt[s] by law” certain notes, bonds and certificates of indebtedness. These instruments are within the ordinary meaning of securities as evidences of creditorship. Such a listing indicates the General Assembly intended certain debt instruments to be exempt, but did

not intend to exempt stock. Had the General Assembly intended to exempt dividend income from specified stocks as a security, it could have so identified such in § 12-1-60 along with other listed securities. Since § 12-1-60 does not exempt dividend income from stock, no exemption is available under such section for dividend income from stock in a Federal Home Loan Bank.

*2 Section 12-7-560(4) provides no exemption for the dividend income in question. This section exempts only interest income on specified obligations and is not appropriate to exempt dividends.

No exemption is available under federal law. Under the United States Constitution, a state may not tax an instrumentality of the federal government without the consent of Congress. *McCulloch v. Maryland*, 17 U.S. 316 (1819); *Federal Land Bank v. Board of County Commissioners*, 368 U.S. 146 (1961). Although the courts have disagreed as to whether federally chartered savings and loans are federal instrumentalities (are instrumentalities—*Kaski v. First Federal Savings & Loan Assoc. of Madison*, 240 N.W.2d 367 (1976), *Waterbury Savings Bank v. Danaher*, 20 A.2d 455 (1940); are not instrumentalities—*Midwest Federal Savings and Loan Association v. Commissioner of Revenue*, 259 N.W.2d 596 (1977); *Sooner Federal Savings and Loan Association v. Oklahoma Tax Commission*, 662 P.2d 1366 (1982)), the question becomes moot where Congress has authorized the states to tax such organizations. Title 12 U.S.C. § 1464(h) states the following in reference to federally chartered savings and loan associations:

“No state, county, municipal, or local taxing authority shall impose any tax on such associations or their franchise, capital, reserves, loans, or income greater than that imposed by such authority on other similar local mutual or cooperative thrift and home financing institutions.”

In *First Federal Savings and Loan Association of Boston v. State Tax Commission*, 437 U.S. 225, 98 S.Ct. 2333, 57 L.Ed.2d 187 (1978), the Court found a Massachusetts excise tax on federal savings and loan associations measured by net income to be a valid tax.

“Whether or not this tax may be characterized as a ‘franchise’ or an ‘income’ tax, it is certainly a tax ‘on’ federal associations and therefore within the ambit of § 5(h) [12 U.S.C. § 1464(h)].” 98 S.Ct. at 2338, footnote 9.

Further, the Oklahoma Supreme Court in *Sooner Federal Savings and Loan Association*, supra, held 12 U.S.C. § 1464(h) allows the nondiscriminatory state taxation of all the income of federal savings and loan associations including dividends paid by a Federal Home Loan Bank. The United States Supreme Court dismissed the appeal for want of a substantial federal question. 103 S.Ct. 1760 (1983).

South Carolina's taxation is nondiscriminatory since § 12-13-30 imposes an income tax on both federal and state associations and § 34-25-210 requires similar treatment of local and federally chartered savings and loan associations.

This opinion is in conflict with an earlier opinion, OAG # 4184, dated November 18, 1975, holding dividends paid on stock in a Federal Home Loan Bank to be nontaxable. Such earlier opinion was issued prior to *Sooner Federal Savings and Loan Association*, supra, and *First Federal Savings and Loan Association of Boston v. State Tax Commission*, supra. In light of such decisions, OAG # 4184 is revoked.

CONCLUSION:

*3 Dividends received by a member bank on stock it holds in a Federal Home Loan Bank are subject to state income tax.

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