1983 WL 182007 (S.C.A.G.)

Office of the Attorney General

State of South Carolina
September 26, 1983

***1** Mr. John T. Weeks
Chairman
South Carolina Tax Commission
P. O. Box 125
Columbia, South Carolina 29214

Dear Mr. Weeks:
In February, 1983, various publishers, editors and retailers throughout South Carolina requested that we review an opinion issued by this office on May 19, 1982 concerning whether advertising supplements to newspapers (‘preprints') qualify as ‘newspapers' within the meaning of § 12-35-550(7) [Code of Laws of South Carolina (1976 as amended)] so that they are exempt from the sales tax.’ In that earlier opinion, it was determined that preprints are not ‘newspapers' and therefore are subject to the retail sales tax.

Since the initial request for our review was made, consistent with our policy, we have met with and contracted a number of editors, publishers and representatives of merchants' associations. We have discussed the matter in considerable detail with many of these people and with persons at the South Carolina Tax Commission. A number of editors, printers and publishers have provided this office with considerable additional factual information regarding preprints and their use in South Carolina.

Moreover, it is significant to note that several recent court decisions in other jurisdictions have dealt with the preprint issue since our opinion was issued. One or two of these decisions suggest that the taxability of preprints when inserted in newspapers raises constitutional questions. In view then, of the public importance of the question, we have concluded that it is appropriate to now reexamine it in light of the additional facts presented and the developing case law in the area. This letter represents the product of that intensive reexamination, made over the course of the past several months.

The following is a good general synopsis of the function and distribution of preprints:
A business which chooses to advertise by means of a newspaper advertising supplement may have such a supplement printed by the newspaper, or by a commercial printer. The advantage to an advertiser of a commercial printer is its ability to print a high quality, attractive product in great quantity. If the advertiser has the supplement printed by a commercial printer, the supplement is printed to the advertiser's specifications and then shipped by the printer directly to the newspapers which incorporate and distribute the supplement.

Daily Record v. James, (Mo.), 629 S.E.2d 348 (1982). As noted in our earlier opinion, § 12-35-550(7) provides that [t]he gross proceeds of . . . newspapers . . .' are exempted from the sales tax. The question for consideration then is whether preprints qualify as ‘newspapers' or parts thereof, thereby exempting from the tax their sales by the commercial printer to the retailer.

Tax Commission Regulation 117-174.166 provides:
In order to qualify as a newspaper the publication must meet at least the following requirements.
1. It must be commonly and ordinarily considered and accepted as a newspaper by the public it is intended to serve.

***2** 2. It must be published at stated short intervals—daily or weekly.

3. It must contain news of general interest and intelligence of current events.

4. It must be sold and not given to the reader free of charge. . . .

5. It must be printed on newsprint paper.

6. It must not, when its successive issues are put together, constitute a book. . . .

7. Newspapers do not include magazines, periodicals, bulletins, and other publications.

Applying the well recognized principle of construction that tax exemptions are to be construed strictly against the taxpayer, M.B. Kahn Const. Co. v. Crain, 222 S.C. 17, 71 S.E.2d 507 (1952), we concluded in the earlier opinion that preprints fail to satisfy at least requirements (2) and (3) of the Regulation. We stated:
The preprints are not prepared at stated short intervals and since they consist entirely of one retailer's advertising, their appeal goes no further than a select group of consumers interested in purchasing the merchandise of a particular retailer.

Op., supra at 3.

We have since been provided additional information which indicates the preprint question is considerably more complex than first thought. For example, it is apparent that many advertisers contract to have preprints regularly published and included in certain newspapers in South Carolina; some of the larger advertisers do this on a weekly basis or even more often. Indeed, it appears that preprints are now distributed with many newspapers on a regular basis.

Neither can it now be confidently stated that the preprint's 'appeal goes no further' than a small group of consumers who wish to purchase from the particular retailer who advertises. The preprint supplement is but one form of commercial advertising. The United States Supreme Court stated in Virginia State Board of Pharmacy v. Virginia Citizen's Consumer Counsel, 425 U.S. 748, 48 L.Ed.2d 346, 359-60 (1976):
. . . As to the particular consumer's interest in the free flow of commercial information, that interest may be as keen, if not keener by far, than his interest in the day's most urgent political debate. . . .

Even an individual advertisement, though entirely commercial may be of general public interest.

Thus, in view of the Supreme Court's consistent holding in recent cases that 'speech proposing no more than a commercial transaction enjoys a substantial degree of First Amendment protection . . .,' Metromedia, Inc. v. San Diego, 453 U.S. 490, 505, 69 L.Ed.2d 800, 813 (1981), it cannot be accurately said that preprints do not contain 'news of general interest and intelligence of current events.'

Still, the Tax Commission Regulation requires that, to constitute a newspaper, a publication must meet at least all the enumerated criteria. For instance, the publication 'must be printed on newspaper paper.' Subsection (5). Our information indicates that a large portion of preprints do not meet this requirement. Moreover, the Tax Commission Regulation requires that the publication 'must be commonly and ordinarily considered and accepted as a newspaper by the public it is intended to serve.' (emphasis added). Subsection (1). No information or data has been provided us suggesting that preprints themselves are considered by the public to be newspapers.

***3** In short, it is difficult to conclude that a preprint itself meets each of the criteria set forth in the Tax Commission Regulation to constitute a 'newspaper.' Indeed, we doubt that any page of traditional newspaper advertising or other component part of the

paper (e.g. the want-ads) could, standing alone, meet all criteria contained in the Regulation. We thus believe it inappropriate to focus upon particular parts of the paper, separated from the remainder, to determine whether the part is itself a 'newspaper.' Instead, as concluded by many of the courts examining the question, it is more proper to analyze the question in terms of whether the preprint is an integral part of the newspaper. See e.g., Wisconsin Dept. of Revenue v. J. C. Penney, (Wis.) 32 N.W.2d 168 (1982). We will now examine the various cases concerning preprints in light of the facts presented.

The first case considered is Sears, Roebuck and Co. v. State Tax Comm., (Mass.), 345 N.E.2d 893 (1976). There, Sears arranged for the printing of supplements and for their shipment to the newspapers, who inserted the preprints into the paper. A use tax was assessed on the price paid by Sears to its commercial printers. The preprints carried the paper's logo and the date of the particular edition in which the preprint was inserted.

The tax board conceded that had the advertising supplement been printed directly by the paper and inserted therein, no tax would have been assessed. Citing Friedman's Express, Inc. v. Mirror Transp. Co., 71 F.Supp. 991 (D.N.J. 1947), affd., 169 F.2d 504 (3rd Cir. 1948), the Court stated:
The Friedman's Express case involved an exemption from the Interstate Commerce Act for motor vehicles used exclusively 'in the distribution of newspapers'. Vehicles carrying comic sections of newspapers were held to be within the exception, even though the comic sections were printed in a separate plant and transported from the printer to the newspaper and its wholesale outlets in delivering them to retailers who assembled the comic sections with other portions of the newspapers. . . . The appellate court said, 'We think that Congress did not intend to make a fine-spun distinction between the distribution of newspapers and parts or sections of newspapers.' . . .

345 N.E.2d, supra at 895-896. Thus, 'the fact that the advertising supplements were not printed directly by the newspapers does not change the result.' Supra at 895. Like the comic section in Friedman's Express, Sears held that preprints constituted an integral part of newspapers. Supportive of that conclusion was the fact that
A tax on the advertising revenue or newspapers could have a devastating effect on First Amendment freedom. See Grosjean v. American Press Co., 297 U.S. 233, 251, 56 S.Ct. 444, 80 L.Ed. 660 (1936) . . . In the present case the taxpayers are retailers, but no showing is made that the economic impact differs from that of a tax directly on the newspapers.

***4** 345 N.E.2d, supra at 896.

Caldor v. Heffernan, (Conn.), 440 A.2d 767 (1981) was the next preprint case. Caldor, a retailer, contracted with a printer to print preprints, and separately contracted with the newspaper 'for the sole purpose of' inserting the preprints in the paper. 440 A.2d, supra at 769.

The Court considered whether preprints were 'newspapers' within the meaning of the tax exemption. Any exemption had to be construed strictly against the taxpayer. Moreover, the Court observed, the preprint must have been a 'newspaper' at the time the sale to the retailer was made. The Court noted that there was no evidence that preprints were prepared at short, regular intervals. And preprints were intended to reach only a narrow audience, not the general public. As stated earlier, based upon the factual information recently submitted to this office, and the Supreme Court cases concerning commercial speech, the holding of Caldor on this issue is of questionable applicability. See above.

The Caldor Court also sought to determine whether preprints were an integral part of the newspaper. Caldor disagreed with the Sears and Friedman's Express cases on two grounds. First, when 'the ownership of the preprints passes from the printer to the retailer',
[t]he only parties in privity to the contract providing for the printing and delivery of the preprints are the retailer and the printer.

440 A.2d, supra at 771. Secondly, the preprint

. . . is inserted into the newspaper, not as an integral part designed to capture a regular audience, but rather to make use of the newspaper's extensive distribution system. . . . An advertising supplement, inserted into the the newspaper at irregular intervals, is not like a member of the family of sections making up the newspaper, but is more similar to the occasional house guest. There was no factual showing that any substantial number of readers ordinarily purchase a newspaper because it may contain an advertising supplement. It is inserted to gain access to large numbers of homes otherwise inaccessible to it.

440 A.2d, supra at 772. Thus, the Court concluded that the preprint was not a component part of a newspaper.

Immediately following Caldor, Ragland v. K-Mart Corp., (Ark), 624 S.W.2d 430 (1981) was decided. Ragland, while recognizing Sears and Friedman's Express, found Caldor more persuasive. Based upon many of the factors outlined in Caldor and the fact that K-Mart had not met its burden of showing entitlement to the exemption beyond a reasonable doubt, the Court concluded that preprints were not an integral part of the newspaper.

Next, Daily Record Co. v. James, (Mo.), 629 S.W.2d 348 (1982) addressed the preprint issue. In this case, no sales tax was imposed by Missouri if the preprint supplement was printed by the newspaper; however, a sales tax was assessed against the commercial printer on the purchase price of the supplements printed for various stores in the area.

***5** Daily Record acknowledged and analyzed the Sears and Friedman's Express cases. The Court noted that the comic section possessed no character of its own and generally was not intended for sale separate and apart from the rest of the paper.
The same can be said of the newspaper advertising supplement. The advertiser orders the supplement solely to be incorporated into a newspaper. That supplement has no character of its own. The newspaper advertising supplement is part of a newspaper when printed. In actuality, there is but one continuous transaction.

629 S.W.2d, supra at 351. Continuing, the Court stated:
The conclusion . . . in Sears Roebuck and Co. v. State Tax Commission, supra . . . is equally sound in this case. Missouri's sales tax statute . . . has long been interpreted not to apply to newspapers which disseminate news, a nontaxable service. An advertising supplement, which is printed solely to be inserted into a newspaper and, in fact, is distributed in the newspaper is an integral part of that newspaper from the time it is printed and is entitled to the same exemption from the sales tax as is the remainder of a newspaper.

629 S.W.2d, supra at 351-352.

Wisconsin Dept. of Revenue v. J. C. Penney, 323 N.W.2d 168 (1982) also recently addressed the preprint issue. There, the Court immediately concluded that preprints ‘standing alone, do not fit the definition of ‘newspaper”, as the term is commonly used. 323 N.W.2d, supra at 171. The real issue was whether preprints are component parts of newspapers.

Relying principally upon Caldor supra, the Court concluded they were not. Friedman's Express was distinguished, in part, by the regularity of the appearance of the comics as compared to preprints. Also, like Caldor, the J.C. Penney case emphasized the retention of ownership of the preprints by the retailer. Secondly, the Court noted that while other features such as the television guide appear at short regular intervals and ‘contribute to the character of the paper, preprints do not.’ 323 N.W.2d, supra.

Next, is the Alabama case, Eagerton v. Dixie Color Printing Corp., (Ala.), 421 So.2d 1251 (1982). There, Dixie Color, an independent commercial printer possessed an agreement with a retailer, Moore-Hadley, Inc. in which Dixie Color printed preprints for Moore-Hadley for insertion into various newspapers. The supplements generally carried the masthead of the particular newspaper into which they were inserted and the newspapers required that certain specifications concerning the preprints be met. Pursuant to an Alabama regulation, if the newspaper printed the preprint or it contracted with a commercial printer, no tax was levied; however, if the retailer himself contracted with a commercial printer, a tax was levied on the sale.

The Court addressed the question whether the preprint was a 'component part of tangible personal property or products manufactured or compounded for sale . . .', thereby exempting it from the sales tax. Responding to the argument that Moore-Hadley did not manufacture any product in which it included the supplements, and instead itself consumed them, the Court said: ***6** We agree that Moore-Hadley did not manufacture the supplements, but we do not agree that it consumed them. The supplements were printed with the intended purpose of being inserted and resold as part and parcel of the newspaper . . .. The commissioner acknowledges that had the newspapers purchased the supplements from the same printer for insertion in the newspaper, the 'component part' exemption would apply and no tax would be due. The supplements are just as much a part of the newspaper when ordered by Moore-Hadley as they are when ordered by the newspaper. We see no reason why the tax consequences of identical transactions should differ, based entirely and solely on who makes the purchase.

421 So. 2d, supra at 1253. Such a distinction, said the Court, 'is both unfair and constitutionally unacceptable.' Supra. Emphasizing the lack of any real distinction between preprint advertising and other newspaper advertising, the Court concluded: . . . Under the facts in this case, an advertising supplement, which is printed solely for the purpose of being inserted into a newspaper and distributed in the newspaper is an integral part of the newspaper. Daily Record Co. v. James, 629 S.W.2d 348 (Mo. 1982). Moore-Hadley pays the newspaper by linear inch as it does for any other advertisement carried in the paper. The fact that the supplements are not printed directly by the newspaper does not change the result. Sears, Roebuck and Co. v. State Tax Comm., 370 Mass. 127 345 N.E.2d 893 (1976).

421 So.2d, supra.

Two recent unpublished decisions have also addressed the question of the taxability of preprints. Both, relying upon many of the reasons expressed in the Eagerton and Sears cases concluded that preprints were an integral part of the newspaper and were thus not subject to the sales tax. See, Homecrafters, Inc. v. State of Alabama, Civ. Act. No. CV-81-1399-14 (Circuit Court of Montgomery County Alabama); Sears Roebuck and Co. v. D. of Cola., (D.C. Superior Court, filed March 26, 1982).

Upon examination of these decisions discussed above, it is clear that the courts are divided over the question of whether preprint supplements are an integral part of the newspaper. Those courts which hold that the preprint is not part of the newspaper, analyze the issue in technical terms; these courts consider ownership and privity of contract to be controlling. These cases also assume that, unlike other portions of the newspaper, preprints do not appear in the paper on a regular basis.

By contrast, the other line of cases views the issue as one of intent and result. These cases note that preprints exist almost solely to be included in the newspaper; they lack independent identity. In those decisions, the function of the preprint is compared to other forms of advertising in the newspaper and little, if any, distinction is found; the fact that the preprint is printed independently is of no significance. Where the supplement is printed solely for insertion in the newspaper, these cases hold it is an integral part of the paper.

***7** The problem is now to apply these conflicting authorities to the additional facts presented to this office. Those facts are as follows. It has been documented that many major retailers contract with various newspapers to have preprint supplements inserted into the newspaper on at least a weekly basis, and many times twice or three times a week. Further, it has been represented that preprint supplements now comprise a substantial portion of South Carolina's newspaper's advertising revenues. Estimates are that the revenue from preprints account for as much as twenty percent of the newspaper's revenue from advertising, perhaps more. Moreover, certain data has been submitted to us indicating that many newspaper purchasers consider preprints to be a part of the newspaper, and it is documented that these purchasers even call to often complain when the supplement is not included in the particular paper which they buy. [1]

Also, we have been presented with sample preprint contracts between the retailer and various South Carolina newspapers. Often, the name of the particular newspaper must appear on the preprint. Also required in some contracts are the words 'advertising

supplement' to the particular newspaper. Usually preprints must, as part of the contract, be received by the newspaper well in advance (10 days) of insertion in the paper. The newspaper often determines the size of the preprints and reserves the right to reject preprints not acceptable to it. In some cases preprint advertising rates are determined in the same way as other newspaper advertising, by the linear inch. For the purpose of advertising rates charges, we understand preprint advertising is usually considered in the same manner as run of press advertising.

It is the policy of this office not to review and overrule its previous opinions except in the rarest of circumstances, i.e., only when an opinion is determined to be 'clearly erroneous'. Once an opinion has been researched and issued, normally the matter is ended.

And this office can issue an opinion only on the basis of the facts submitted; since we cannot resolve factual disputes, we must assume those facts submitted and outlined above to be true and undisputed.

In view of the existing case law just discussed, our earlier opinion was not 'clearly erroneous'. As noted, several cases hold that preprints are not an integral part of a newspaper. And, like those cases, the earlier opinion was primarily based upon the assumption that preprints were not inserted into newspapers on a regular basis. No facts to the contrary were submitted to this office prior to issuance of our previous opinion. We also assumed earlier, as cases such as Caldor had indicated, that preprints had little if any, impact on newspaper sales. No information to the contrary had been presented. Based, upon these assumptions, therefore the earlier opinion was not 'clearly erroneous'.

However, the additional facts presented since the opinion was issued cannot be now ignored. We must now assume that, in a good many instances, preprints are inserted in South Carolina newspapers on a regular basis. We also now assume that preprints have considerable impact upon some readers' decision to purchase a newspaper. In light of the United States Supreme Court's consistent holding for First Amendment purposes that commercial advertising is news of general interest, and in view of these additional facts, the conclusions reached by the courts in the Caldor, Ragland and J.C. Penney cases, where no such facts were present, as to these points at least must be considered of questionable applicability.

***8** However, the questions of ownership of the preprints and of privity of contract raised in those cases remain. All of the decisions which have concluded that preprints are subject to taxation have placed considerable emphasis upon the fact that the preprint is owned by the retailer, not the newspaper, at the time of sale; and, these cases have emphasized that the newspaper publisher is not in privity with the agreement between retailer and commercial printer for the printing of the preprint.

Technically, as we understand it, the newspaper normally does not 'own' preprints until their physical delivery to the newspaper. This usually occurs well after sale by the printer to the retailer, pursuant to separate contract. On the other hand, we understand that the newspaper, by contract with the retailer, does control many aspects of the preprint supplement such as the right to reject the preprint, based upon content and form and the right to dictate the size of the preprint. Thus, while technically the newspaper does not own the preprint until physical delivery to the newspaper, contractual rights nevertheless give the newspaper publisher considerable control over the preprint from the outset.

Moreover as seen, several cases conclude that ownership and privity of contract are of little, if any, significance. For example, in Daily Record, supra, the Missouri Supreme Court stated that '[a]n advertising supplement which is to be inserted into a newspaper and, in fact, is distributed in the newspaper is an integral part of that newspaper from the time it is printed . . ..' 629 S.W.2d, supra at 351-352. The Alabama Supreme Court in Eagerton declared that '[t]he fact that the supplements are not printed directly by the newspaper does not change the result.' 421 So.2d, supra at 1253, citing Sears, Roebuck and Co. v. State Tax Comm., supra.

While not free from doubt, the Massachusetts, Missouri and Alabama cases discussed above appear to us on balance to be more persuasive in holding that preprints are not subject to the sales tax because they are an integral part of the newspaper. Like the comic section discussed in Friedman's Express, the preprint supplement is prepared almost solely for insertion in the newspaper; except for those relatively few preprints that are distributed elsewhere (about which, we understand, there is no

dispute), the preprint supplement possesses no independent identity. At the time the sale to the retailer occurs, the preprint will usually become part of the newspaper. And, based upon the information received by the office, it appears that the supplements have become accepted by the general public as constituting a part of the newspaper. Therefore, it would prefer form over substance to subject the preprint to the sales tax, while at the same time exempting therefrom the more traditional form of newspaper advertising.

The argument has been presented that often not every issue of the same paper contains a preprint supplement; many times a paper will distribute preprints only in certain zones. Therefore, it is argued, the preprint supplement is not an integral part of the newspaper. However, the same may certainly be said for other parts which are clearly integral to the paper, such as traditional newspaper feature segments containing news related only to a particular portion of a metropolitan area.[2] The mere fact that preprints are distributed only in certain geographical areas is not relevant to the question whether preprints are an integral part of a newspaper.

***9** It is also argued that the rule of statutory construction in this situation requires that any doubt, as to the interpretation of the newspaper's exemption, be decided against the exemption. It is, no doubt, correct as a general proposition that the exemption must be strictly construed. However, the Sears, Daily Record and Eagerton cases have ruled in favor of the tax exemption despite the fact that jurisdictions where those cases were decided clearly possessed the very same rule of construction.

Moreover, there also exists in South Carolina the principle of construction that every statute or its application must be construed in a constitutional manner. As the Supreme Court of South Carolina stated in Thomas v. Macklen, 186 S.C. 290, 195 S.E. 539 (1937),

all presumptions are in favor of the power of [the General Assembly] . . . to enact the law . . .. So long as doubt concerning this power remain, it is our plain duty to resolve them in favor of the validity of the Act.

186 S.C., supra at 305. At least one court, Massachusetts, in Sears v. State Tax Comm., supra, has concluded that the imposition of the sales tax on preprints raised serious questions regarding freedom of the press under the First Amendment in light of Grosjean v. American Press Co., 297 U.S. 233, 251, 56 S.Ct. 444, 80 L.Ed. 660 (1936).[3] This constitutional question, while not controlling, would militate in favor of a construction exempting the preprint from taxation where they are printed and sold solely for insertion in the newspaper. Sears, Roebuck and Co. v. State Tax Comm., supra.

Therefore, in view of the additional facts presented that many preprints appear in the newspaper on a weekly basis, if not more often, and that preprints apparently now have considerable impact upon newspaper circulation as well as public acceptance as part of the newspaper, it is the conclusion of this office that preprints are exempted from the sales tax because they are, under ordinary circumstances an integral part of the newspaper; in short, we find the Sears, Daily Record and Eagerton cases more persuasive in their reasoning and logic in light of the additional facts which have been submitted to us.

It should be recognized, however the limitations we place upon our opinion. Our conclusion is not directed to all preprints; those preprints not ultimately inserted into the newspaper would present a different question. In addition, this opinion does not address the issue of whether other types of supplements or publications physically inserted into the newspaper are integral parts of the newspaper. We have been presented with no information and do not consider these publications. We caution also that we have assumed all facts submitted to us to be true because this office has neither the resources nor authority to resolve issues of fact.

And, as noted, the question is not one free from doubt. As demonstrated, it must be acknowledged that there are several cases from other jurisdictions which reach a different conclusion; the question is a close one.

***10** While we have advised you as to our interpretation of § 12-35-550(7), we strongly suggest, because of the closeness of the question, that the ultimate solution to the issue rests either with the General Assembly or the courts. Or, a possible solution might be a comprehensive regulation covering the entire subject and promulgated by the Tax Commission, pursuant to § 1-23-10 et

seq wherein 'all interested persons' would have 'reasonable opportunity to submit data, views or arguments orally or in writing.' However, in the meantime we would advise that preprint advertising supplements which are on a regular basis, usually daily or weekly, 'printed solely to be inserted in a newspaper and, in fact [are] . . . distributed in the newspaper [are] . . . an integral part of that newspaper from the time it is printed and [are] . . . entitled to the same exemption from the sales tax as is the remainder of a newspaper.' Daily Record, supra.

With kindest regards, I remain
Very truly yours,

T. Travis Medlock
Attorney General

Footnotes

1 Other information has been submitted to us to the effect that customer complaints of persons not receiving their daily newspapers are demonstrably higher in number on those days when preprints are inserted in the newspaper than on those days when no preprint is inserted. This may be supportive of the fact that persons consider preprints to be an integral part of the newspaper.

2 We understand that many newspapers focus advertising toward particular audiences and to certain locales; this same method is utilized with respect to special features such as television guides or local news.

3 But see, Minneapolis Star and Tribune Co. v. Minnesota Comm. of Revenue, 51 U.S. L.W. 4315 (March 29, 1983). The Eagerton case also found that the taxation of preprints by commercial printers and sold to retailers where there was no tax imposed upon those preprints printed by or for the newspaper violated equal protection.

1983 WL 182007 (S.C.A.G.)

End of Document