April 3, 1987

Constitutionality of the Imposition of the Florida State Sales/Use Tax on Out-Of-State Advertising Revenues

Dear Sirs:

You have asked for our opinion as to the constitutionality of the proposed imposition of a 5% Florida State sales/use tax on revenue from advertising carried in Time Inc. publications. For the reasons set forth below, we believe the imposition of such a tax would be a violation of the Commerce and Due Process Clauses of the United States Constitution. As is also set forth below, we believe that the proposed relocation of the Time subscription fulfillment facility in Tampa, Florida, would pose a risk to the immunity of Time's advertising revenue from the proposed Florida service tax under the United States Constitution, would place Time at a disadvantage vis-a-vis its competitors who have such facilities outside the State of Florida and should be reconsidered.

Under legislation currently pending before the Florida legislature, the State would impose a 5% sales tax on the sale of services performed within Florida. That legislation also enacts a complementary 5% tax on the use of any service in Florida where the sale is not taxable in the State when the services are rendered, furnished or performed in the State or where the product or result of the service is used in Florida. The legislation also provides that the sales price of sales of interstate advertising services or the cost price of the use of interstate advertising services shall be apportioned between Florida and the United States in proportion to relative "market coverage", which in the case of print media is defined as relative average daily circulation.
The typical relevant advertising transaction on which Florida would impose its proposed service tax takes the following form. The advertising is solicited by representatives of Time or the advertiser outside Florida, most often in New York. The terms of the advertising, the space, the number of issues, the timing, the geographic and demographic groups to be reached, and price are negotiated by the parties' representatives outside the State of Florida. The advertising copy is generated by the advertiser or some third party and delivered to Time in New York where it is reviewed by Time for acceptability. Payment for the advertising services is made to Time in New York.

The advertising copy is incorporated by Time into the "masters" for each edition of Time's publications in New York. The magazines are then printed from these masters at various locations throughout the country, all outside the State of Florida. Copies of the magazines are then sold to distributors for resale or newsstand sales or delivered to subscribers throughout the United States through the United States mails.

Under these circumstances, the State of Florida cannot constitutionally impose its proposed service tax on Time advertising revenue. This conclusion follows from the decision of the Supreme Court of the United States in Western Live Stock v. Bureau of Revenue, 303 U.S. 250 (1938). Like all other States, the power of the State of Florida to impose a sales/use tax on services is territorially limited to services performed in the State of Florida. The advertising services performed by Time under the circumstances described are all performed outside the State of Florida, primarily in New York. Florida therefore lacks the constitutionally required territorial relationship with the performance of Time's advertising services to impose its proposed tax.

In the Western Live Stock case, the State of New Mexico imposed a 2½% tax on the revenue received from the sale of advertising space by a taxpayer engaged in the publication of a livestock trade journal. The taxpayer wholly prepared, edited and published the trade journal in the State of New Mexico where its only office was located. "All of the events upon which the tax is conditioned -- the preparation, printing and publication of the advertising matter and the receipt of the sums paid for it -- occur in New Mexico and not elsewhere". 303 U.S. at 260. The Supreme Court allowed the State of New Mexico to impose its gross receipts tax on the taxpayer's entire advertising gross revenue notwithstanding the fact that its publications and advertisements were solicited and distributed both within and without the State of New Mexico. The reason that it did so is that, in its view, no other state could impose a tax on the advertising activities of Western Live Stock. As the Court said:
"The tax is not one which in form or substance can be repeated by other states in such a manner as to lay an added burden on the interstate distribution of the magazine. . . . All the events on which the tax is conditioned -- the preparation, printing and publication of the advertising matter and the receipt of the sums paid for it -- occur in New Mexico and not elsewhere. All are beyond any control and taxing power which, without the commerce clause, these states could exert through its dominion over the distribution of the magazine or its subscribers". 303 U.S. at 260.

The Western Live Stock case clearly indicates that the State of Florida may not impose its proposed service tax on Time's advertising revenue. As in Western Live Stock, "the preparation, printing and publication of the advertising matter and the receipt of sums paid for it" (303 U.S. at 260) occur in another taxing jurisdiction outside of Florida. And Florida may not, "through its dominion over the distribution of the magazine or its subscribers" (303 U.S. at 260), impose a tax on Time's advertising revenues.

The Western Live Stock case has never been overruled and remains binding authority limiting the taxing powers of the State of Florida to this day. Some commentators have viewed a more recent case, Complete Auto Transit v. Brady, 430 U.S. 274 (1977) as restating and modifying the interstate commerce principles applicable to state and local taxation. In Complete Auto Transit, the Supreme Court upheld the imposition of a state tax of 5% of the gross sales derived from the transportation of motor vehicles between two points within the State. The Court held that the appropriate test to be applied to judge the validity of State sales taxes impinging on interstate commerce was the following four-factor test:

(1) Was there a constitutionally significant nexus between the taxing State and the activity taxed?

(2) Was the tax fairly related to the benefits provided by the taxing State to the taxpayer?

(3) Did the tax discriminate against interstate commerce?

(4) Was the tax fairly apportioned?

The Court held that the tax under consideration satisfied these four criteria.

There is no reason to believe that the Complete Auto Transit case would in any way affect the unconstitutionality of
the proposed Florida service tax as applied to Time advertising revenue. In that case, the Supreme Court did not overrule Western Live Stock. It relied on it and quoted it extensively. 430 U.S. at 288. The facts involved in Complete Auto Transit had nothing to do with advertising services. They had nothing to do with an attempt by a state to impose its sales taxes on revenues derived from services rendered outside the State. The tax involved was specifically limited to revenues from transportation services rendered between points within the taxing State.

Even if the four-factor test of Complete Auto Transit were itself applied to the question raised by Florida's attempt to impose its sales tax on out-of-state advertising services, it would be unconstitutional. Florida fails to meet the very first test of Complete Auto Transit. Because the advertising transactions and the advertising services rendered by Time occur outside of Florida, the State lacks the constitutionally required nexus to impose the tax. Western Live Stock clearly shows that Florida's dominion over the recipients of Time publications does not endow it with the power to tax advertising services rendered outside the State and there is nothing in Complete Auto Transit to cast any doubt on that conclusion.

The Supreme Court's decision in National Bellas Hess v. Illinois Rev. Dept., 386 U.S. 753 (1967), further supports the unconstitutionality of Florida's attempt to impose its proposed service tax on Time's advertising revenue. There, the taxpayer was engaged in sales of goods across State lines through the circulation of mail order catalogues and flyers. Taxpayer owned no property and employed no employees in the State of Illinois. It did mail catalogues and flyers into the State. It did sell substantial quantities of goods to Illinois residents which it shipped into the State by mail or common carrier. Because of the tenuous contacts between the seller and the taxing State and the lack of any local services for which the State could reasonably impose a tax, the Supreme Court held it unconstitutional for Illinois to impose a sales or use tax on the out-of-state seller. Couched in terms of Complete Auto Transit, the State of Illinois failed to meet the first (minimum contacts) and second (reasonable charge for services rendered) tests for the imposition of its use tax. See also Miller Bros. Co. v. Maryland, 347 U.S. 340 (1954).

Time's contacts with the State of Florida through its solicitation and fulfillment of subscriptions and its sales of magazines to distributors for newsstand sale are effected by means identical to those involved in National Bellas Hess in all
relevant respect. Therefore, under the authority of the National Bellas Hess and Miller Bros. cases, Florida lacks the power to impose sales and use taxes even for the revenues derived from the sale of its magazines to Florida residents. It is therefore even clearer that Florida lacks the power to impose its proposed service tax on advertising transactions and services conducted wholly outside the State on the basis of the fact that some Time publications are sold in Florida.

You have advised us that Time proposes to relocate its magazine subscription fulfillment facility to Tampa, Florida. We understand that this facility will employ some 1500 people and will be used for the purpose of distributing magazine subscription solicitations, accepting orders for subscriptions, directing the fulfillment of subscriptions and accepting payment for them. You have asked whether the proposed relocation of that facility would create any risks with respect to the proposed Florida service tax. We believe it would.

We have been advised that notwithstanding the clear unconstitutionality of imposing the proposed Florida service tax on out-of-state advertising services, the Florida tax authorities currently intend to do so. In attempting to impose the Florida tax on out-of-state advertising transactions, the Florida authorities will have to attempt to avoid the constitutional limitations of National Bellas Hess, Complete Auto Transit and Western Live Stock. In doing so, they will have to overcome, among others, the hurdles that: (1) the advertising transaction which they seek to tax is not within their territorial jurisdiction as required by Western Live Stock; (2) the presence of magazine circulation within their "dominion" is insufficient to support imposition of the tax as required by Western Live Stock; (3) they lack the minimum contacts with the advertising transaction constitutionally required by Complete Auto Transit and National Bellas Hess; and (4) the State provides no services for which they may reasonably require the payment of a tax on advertising transactions by Time as required by the cases last cited above.

Under these circumstances, the Florida taxing authorities can be expected to rely upon the existence of the Tampa fulfillment facility as supplying a relevant minimum

\[1/\] This opinion assumes the state of facts that will exist if Florida seeks to impose its proposed service tax on Time's out-of-state advertising revenues. Should that occur, any other incidental activities which Time may conduct in the State shall be terminated.
contact. They can be expected to rely upon the public services furnished to the Tampa facility as providing a service for which they can impose a tax on advertising revenue. Although the Tampa facility will play no role in the performance of advertising services, the State can be expected to argue that the Tampa facility performs services which are in some sense related to the provision of advertising services so as to justify the imposition of the Florida tax on the out-of-state advertising transaction.

Although we believe these arguments will not prevail in the face of existing constitutional authority prohibiting the imposition of the tax, they do create a risk for Time. They also put Time in a difficult procedural posture. Time will be unable to secure a final decision on this matter for some years should the Florida state authorities seek to impose their proposed service tax on the out-of-state advertising transactions.

As an administrative matter, this situation may well force Time to attempt to collect the tax from its advertisers even if the out-of-state application of the tax is ultimately held unconstitutional. This will obviously place Time at a serious competitive disadvantage vis-a-vis its competitors, such as Newsweek, none of whom uses Florida as a base for subscription fulfillment. Since no other State has attempted to impose a tax on out-of-state advertising revenues, no Time competitor will be required to collect such a tax, whether imposed by Florida or any other State, on any of its advertisers. Time will, therefore, be uniquely disadvantaged should it proceed with its decision to relocate its subscription fulfillment facility to Tampa.

Very truly yours,

[Signature]

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