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SC TECHNICAL ADVICE MEMORANDUM #89-17

TO: Mr. Marvin N. Davant, Director
Field Services Division

FROM: Jerry B. Knight, Manager
Tax Policy and Procedures Department

DATE: June 7, 1989

SUBJECT: The Drink
(Soft Drink Tax)

REFERENCE: S.C. Code Ann. Section 12-21-1860 (1976)
S.C. Code Ann. Section 12-21-1750 (Supp. 1988)
S.C. Code Ann. Section 12-21-1840 (Supp. 1988)
S.C. Code Ann. Section 12-21-1850 (Supp. 1988)
S.C. Code Ann. Section 12-21-2120 (Supp. 1988)

AUTHORITY: S.C. Code Ann. Section 12-3-170 (1976)
SC Revenue Procedure #87-3

SCOPE: A Technical Advice Memorandum is a temporary document issued to an individual within the Commission, upon request, and it applies only to the specific facts or circumstances related in the request. Technical Advice Memoranda have no precedential value and are not intended for general distribution.

Question:

Is a product known as "The Drink" subject to the South Carolina Soft Drink Tax, pursuant to Code Section 12-21-1860?

Facts:

Company of South Carolina ("Company") produces a natural, soft frozen, lemon-flavored product, known as "The Drink." The Drink is made fresh daily from the entire lemon, with no preservatives or additives. The consistency of the product is similar to applesauce or snow; and, is made in a forty-quart ice cream freezer. The product is subsequently in five mil polyethylene bags and stored immediately in a walk-in cooler at twenty-eight degrees fahrenheit. The Drink is perishable and has an approximate shelf life of four days.

The product is delivered by a refrigerated truck the same day it is made, or the following day, to retail locations. Wholesale sales to such locations account for approximately forty to fifty percent of the Company's business. The Company sells the product at retail via push-carts, which accounts for the remaining business. At the retail locations or the push carts, The Drink is placed into a stainless steel dipping tank and, when sold to a consumer, ladled into a cup. The consumer is given a plastic spoon, in order to consume the product.

South Carolina imposes a tax on "bottled soft drinks," and "syrups", "powders" and "bases" used to make a soft drink. Code Section 12-21-1860 defines "bottled soft drinks," "bottle" or "bottles" and "bottled drinks", and reads:

> "Bottled soft drinks," as the term is used in this chapter, means any complete, finished, ready to use, nonalcoholic drink, whether carbonated or not, including, but not limited to, soda water, ginger ale, nu-grape, coca-cola, lime-cola, pepsi-cola, budwine, any product having an alcohol content of less than one-half percent of weight or volume, fruit juice, vegetable juice, milk drinks when any flavoring or syrup is added, cider, cordials, bottled carbonated water and all bottled preparations commonly referred to as soft drinks of whatever kind or description.
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> "Bottle" or "bottles," as used in this chapter, means in every instance any closed or sealed glass, metal, paper, or other type of bottle or container, regardless of the size of the container. "Bottled drinks" as used in this chapter, means in every instance soft drinks in any closed or sealed glass, metal, paper, or any other type of bottle or container, regardless of the size of the container.

"Syrup," "powders" and "bases" are defined in Code Sections 12-21-1750 and 12-21-1840; however, the Company does not use such items to produce The Drink. Therefore, Sections 12-21-1750 and 12-21-1840 are not applicable.

Furthermore, the Company has conceded that The Drink does not qualify for the exemptions found in the Soft Drink Tax Code of Laws.

Code Section 12-21-1850 imposes the tax on bottled soft drinks, and reads:

> Any person offering soft drinks for sale in a sealed container shall pay the license tax at the rate of one cent for each twelve ounces or fractional part thereof.

However, Code Section 12-21-2120 reads:

> Each manufacturer, wholesaler, distributor, or retailer first receiving untaxed bottled soft drinks, syrups, premixed soft drink, or powders and bases for sale or disposition in this State is subject to a tax at the rate of one dollar and twenty-two cents a gross for each one cent of face value in the case of bottled soft drinks and a tax at the rates prescribed in this article for syrups, pre-mixed soft drink, or powders and bases. Each manufacturer, wholesaler, distributor, or retailer required to pay the tax shall make a report to the Commission, in the form as the Commission may prescribe, of all bottled soft drinks,

> syrups, premixed soft drink, powders and bases sold or disposed of in this State and pay the taxes due thereon not later than the twentieth day of the month next succeeding the month of the sale or disposition.

Discussion:

The issue in question is whether or not The Drink is a soft drink.

The "License Agreement," entered into by the Company (The Drink of South Carolina) and the Licensor (The Quench Co., Inc.), reads, in part:

> "Licensed Product" shall mean a non-carbonated, slush-ice product with a lemon flavor (or such other flavor as authorized in writing by Quench) made in accordance with a proprietary recipe and using other proprietary information and know-how to be disclosed to Licensee on a confidential basis under this License Agreement.

In a letter to the The Drink franchise in North Carolina, dated January 14, 1985, the Food Service Manager of the Carowinds amusement park stated the following:

> Our The Drink location was placed about 20 yards from a location that sold only soft drinks. A comparison of the operating results for this drink location over the past three seasons makes it appear as though The Drink will not affect soft drink sales because of its' uniqueness.

At the close of the amusement park's season, the Food Service Manager, in a letter dated November 25, 1985 to the North Carolina franchise, stated:

> Thank you for another successful year with the The Drink product. Our sales for 1985 more than doubled those of 1984 and we were very pleased with the quality of the product.
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> We were very surprised that the increase in sales of The Drink were not reflected in a noticeable decrease in sales of any of our other products. I think the fact that it cannot be considered a beverage nor an it be compared to any of our food items results in incremental revenue. I wish that we could find a new product each season that would result in an incremental $.1200 per cap such as The Drink!

The Quench Co., Inc., the licensor of The Drink, also bottles a soft drink known as "Quench". In a letter to the Tax Commission, the Quench Company stated:

> Please be advised that the Quench mark has been in continuous use and Federally registered as the mark of The Quench Company since first registered in 1923. We have an established soft drink franchise business, primarily situated in the Western United States. To be specific, we have 57 franchises and distributors in 10 states with 25 bottling and 4 canning facilities. Many of these franchises have been in operation for 40 plus years.

> Since our entry into the The Drink product franchise line, it was of necessity that this non-carbonated product be completely different from our existing soft drink line. These soft drink licenses are perpetuous. The Drink franchises, within an already existing Quench soft drink franchise, would have immediately triggered franchise violation litigation by the soft drink franchisees. We have had no problems on this issue; therefore, our soft drink franchisees also recognize The Drink as a non-competitive and non-soft drink product.
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> At the very start of product development, we determined that this product was unique and therefore was a new category, not meeting other product criteria. Our choice to establish it as a "soft frozen dessert", in our opinion and that of our trademark attorney, is applicable.

While the Quench Company has not authorized the establishment of a Quench soft drink franchise and a The Drink franchise in the same location, they do not foresee any problems with "franchise violation litigation". In fact, they intend to authorize the establishment of a Quench franchise in a California city with an existing The Drink franchise.

In summary, The Drink is a "slush-ice product" that, at least at a specific amusement park, does not compete with soft drinks. In addition, soft drink franchisees of the Quench Company and the franchiser view The Drink as a unique product, unlike a soft drink.

Furthermore, Section 1 of Regulation 61-32, "Soft Drink Bottling Plants", promulgated by the South Carolina Department of Health and Environment Control ("DHEC"), defines "soft drink", "bottling plant" and "health officer" and reads, in part:

> (a) The term "soft drink" as used in these regulations shall include all "carbonated beverage", "soda" or "soda-water", "still drinks", "fruit juices", "perishable fruit drinks", "root beers", and similar non-alcoholic beverages, carbonated or otherwise, or ingredients used in the preparation of same.
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> (b) The term "Bottling Plant" as used in these regulations shall include all establishments manufacturing, processing, or distributing, "carbonated beverage", "soda", "sodawater", "still drinks", "fruit juices", "perishable fruit drinks", or "root beers", and similar beverages.
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> (e) The term "Health Officer" within the meaning of these regulations shall mean the health authority of the cities and/or the counties, and/or the state, or his authorized representative (emphasis added).

Section 3 of Regulation 61-32 is entitled "Permits", and reads:

> It shall be unlawful for any person to operate a bottling plant in the State of South Carolina who does not possess an unrevoked permit from the Health Officer. Such a

> permit shall be posted in a conspicuous place. Only persons who comply with the requirements of these regulations shall be entitled to receive and retain such a permit.
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> Such a permit may be temporarily suspended by the Health Officer upon the violation by the holder of any of the terms of these regulations, or revoked after an opportunity for a hearing by the Health Officer upon serious or repeated violation.

Notice that the above definition for "soft drink" is very similar to the one found in the tax code. In addition, The Drink of South Carolina is not licensed with DHEC as a soft drink bottling plant.

Furthermore, "The Drink" is marketed and franchised as a type of soft frozen dessert. Customers receive a spoon in order to consume the product.

The courts of this State have held that there is no room for construction when the statute is clear. Where more than one interpretation can be found, the courts have looked for the legislature's intent. However, when neither the statute nor the legislature's intent are clear, it is a well-settled rule of construction that any substantial doubt as to the meaning of a taxing statute should be resolved in favor of the taxpayer, and against the taxing authority. For cases where this rule has been applied, see Clark v. S.C. Tax Commission, 259 S.C. 161, 191 S.E. 2d 23 (1972); Deering Milliken, Inc. v. S.C. Tax Commission, 257 S.C. 185, 184 S.E. 2d 711 (1971); Southeastern Fire Ins. Co. v. S.C. Tax Commission, 253 S.C. 407, 171 S.E. 2d 355 (1969); Ryder Truck Lines, Inc. v. S.C. Tax Commission 248 S.C. 148, 149 S.E. 2d 435 (1966); Coble Dairy Products Co-op., Inc. v. Livingston, 239 S.C. 401, 123 S.E. 2d 301 (1962); Colonial Life and Acc. Ins. Co. v. S.C. Tax Commission, 233 S.C. 129, 103 S.E. 2d 908 (1958); and, Beard v. S.C. Tax Commission, 230 S.C. 357, 95 S.E. 2d 628 (1957). Therefore, any substantial doubt as to the whether or not The Drink is taxable, under the State's soft drink tax, should be resolved in favor of the taxpayer.

Conclusion:

"The Drink" is not marketed or franchised as a soft drink and is not "commonly referred to as [a soft drink]." Therefore, "The Drink" is not a soft drink and is not subject to the State's soft drink tax, pursuant to Code Section 12-21-1860.