

The Virgin Islands Consortium

District Court Judgement Deeming Excise Tax In Violation Of Constitution Heads To Third Circuit Court Of Appeals

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The District Court of the U.S. Virgin Islands in a September 28 judgement, ruled that excise taxes exacted on businesses in the U.S. Virgin Islands violated the Commerce Clause of the U.S. Constitution, a decision that could cost the cash-strapped Government of the Virgin Islands tens of millions of dollars annually.

The ruling was immediately appealed to the Third Circuit Court of Appeals, Attorney General Claude Walker told The Consortium Monday. He clarified that a motion to stay the judgement until the Third Circuit Court of Appeals case, scheduled for December, was filed by the government, therefore excise taxes -- long a bone of contention for business owners -- will remain in place until the court rules on it. (Alex Golubitsky, the attorney representing the plaintiff in the case, said he intended to challenge the government's motion to stay.)

If the ruling stands in the Third Circuit Court of Appeals, the territory -- barring a Supreme Court appeal -- would have to relinquish the excise tax it charges, a source of revenue that represents over \$40 million for the local government.

The challenge was first brought by Reefco Services, Inc., a corporation organized in the USVI and engages in the marine refrigeration business, in December 2014. The company installs and provides repair services for refrigeration units, air conditioning units, ice makers, and water makers on boats.

Reefco, which was charged for equipment that it brought into the territory dating back to 2011, contended in its complaint that the taxes violated the Commerce Clause

The complaint included five counts: Count one asserts a claim for an unconstitutional taking; count two asserts that the excise tax violates the Commerce Clause; count three asserts that the excise tax violates the Import/Export Clause; count four asserts a claim for a refund of excise taxes paid; and count five also asserts a claim for an unconstitutional taking.

The District Court in 2015 granted the GVI a motion to dismiss, but only in part, while denying the motion to dismiss relative to counts four and five. In April 2017, however, the court moved to vacate the trial, settling the matter.

But there was reconsideration this year of count two, according to court documents The Consortium has obtained. Count two contends that the excise tax law violates the Commerce Clause of the U.S. Constitution. "The excise tax is facially unconstitutional under the Commerce Clause as the excise tax discriminates against interstate commerce," reads a portion of count two. Citing precedent, the District Court said it was "necessary to reconsider its decision dismissing count two of the amended complaint and revive that count."

According to the latest District Court judgement, Reefco was assessed excise taxes in accordance with 33 Virgin Islands Code, Section 42 for items that Reefco imported into the territory. Section 42 was passed by the Virgin Islands Legislature in 1959. The section says ostensibly, the law requires the payment of "an excise tax on all articles, goods, merchandise or commodities manufactured in or brought into the Virgin Islands for personal use" or "any business use or purpose," unless the items are "specially taxed, exempted or excluded."

In 1984, the Virgin Islands amended Section 42 to require the payment of excise taxes on "all articles, goods, merchandise and commodities manufactured in or brought into or manufactured in the Virgin Islands." Section 42b outlined the procedure for collection of excise taxes on foreign imports, while 42c outlined the procedure for collection of excise

taxes on domestic imports. However, no statutory provision exists outlining the procedures for the collection of excise taxes on locally manufactured goods. Instead, Section 42a directs the director of the Bureau of Internal Revenue to “promulgate rules concerning procedures for the valuation of goods and payment of excise taxes on items manufactured in the Virgin Islands.” According to the District Court, “Significantly, however, such regulations were never promulgated.”

In a separate case cited as precedent in the latest proceedings, an appeal to the Third Circuit Court in *JDS Realty Corp. v. Gov't of Virgin Islands* explained that “[a] cardinal rule of Commerce Clause jurisprudence is that ‘[n]o state, consistent with the Commerce clause, may impose a tax which discriminates against interstate commerce by providing a direct commercial advantage to local business.’”

“By imposing a tax only on imported goods” but not locally manufactured goods, the excise tax did just that, the Third Circuit said in its ruling of the *JDS Realty Corp. v. Gov't of Virgin Islands* matter.

The District Court's ruling noted that the Third Circuit was “hard pressed to imagine a taxing scheme more patently violative of the Commerce Clause than [the excise taxes under Section 42].” Accordingly, the Third Circuit held that, “because the challenged excise tax ha[d] a discriminatory purpose and effect, it violate[d] the commerce clause,” added the District Court.

Depending on the ruling when the new case is heard in the Third Circuit, the repercussions could be significant for the local government, which for years has been struggling with a structural deficit, and is in continuous need of funds to meet its obligations. A diminishing or complete rejection of the excise tax would force the government to look elsewhere to recoup those funds.

See court documents [here](#) and [here](#).

Correction: Oct. 23, 2018

A previous version of this story stated that the excise tax was also being levied on residents for personal items. However, the law with this provision was repealed after a successful challenge by Robert Molloy, who is now a Superior Court judge, according to Bureau of Internal Revenue Director Marvin Pickering.