

V.I. Loses Latest Round in Excise Tax Legal Battle

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Robert Moore **December 16, 2019**

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Port of Long Beach. By. Bloomberg News

The Government of the Virgin Islands and Bureau of Internal Revenue lost another round in the high-stakes federal lawsuit over the constitutionality of the territory's excise tax.

U.S. District Court Judge Curtis V. Gomez last week denied the territory's second appeal to lift an earlier court ruling invalidating the excise tax the government had levied on virtually all goods, merchandise and commodities made in or imported into the territory. The tax had generated upwards of \$40 million in Fiscal Year 2018, the most recent complete year the tax was imposed on the islands' retailers, manufacturers, artisans and others.

In a 10-page ruling, Judge Gomez said the central government presented no legal basis to reverse the earlier court ruling suspending application of the tax. "The GVI, just as it failed to do so when

it first asked for a stay, now fails to offer a basis to lift or stay the injunction,” Judge Gomez wrote.

At the heart of the case is a 2014 lawsuit filed by Reefco Services Inc., a Virgin Islands-based company that paid excise taxes on parts and materials shipped in for refrigeration systems installed in boats. Reefco argued that it should not have to pay the tax because the certain boat parts are exempt from excise tax under V.I. law. The company successfully argued that the tax is a violation of the Commerce Clause of the U.S. Constitution. The court initially dismissed most of the counts, but later vacated its dismissal of the Commerce Clause argument and ruled the excise tax indeed violated the Commerce Clause, which gives Congress authority to regulate interstate commerce.

The courts also found in original rulings on the case that the territory discriminated against the businesses of other states in its application of the excise tax. In November 2018, the G.V.I. filed a motion with the Third Circuit Court of Appeals to stay the District Court’s invalidation of the excise tax, and to lift the injunction, which would allow the government to resume collecting excise taxes. A month later, however, the appeals court agreed with Judge Gomez’s order and denied the government’s motion. The territory was later given until March 2019 to file briefs in another appeal, this time arguing that a restructured collection scheme would allow the excise tax to continue legally.

Judge Gomez wrote in last week’s opinion that the government excise tax structure continued to treat local businesses differently than non-local businesses. "With respect to the other factors that the Court must consider when weighing a motion to lift or stay an injunction, in the Court’s view, those factors are similarly unchanged from what the Court found in its Nov. 26, 2018, opinion ... The new proposed scheme continues to discriminate against interstate commerce in its effect.”

Reefco Services was assessed excise taxes in accordance with 33 Virgin Islands Code, Section 42, which was enacted in 1959. The section of the law calls for 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 42 of the law outlined the procedure for collection of taxes on foreign imports and 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 Sept. 28 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, an appeals court said in its ruling of the *JDS Realty Corp. v. Gov’t of Virgin Islands* matter.

The District Court's Sept. 28 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]."

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