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Opinion No. 11-67

Retailers' Sales Tax Act and Import and Export Taxes

QUESTION

Does the Retailers' Sales Tax Act, Tennessee Code Annotated §§ 67-6-101 *et seq.*, impose a tax on imports and exports in violation of Article I, Section 9, Clause 5 and Article I, Section 10, Clause 2 of the United States Constitution?

OPINION

No. The Retailers' Sales Tax Act imposes a privilege tax on the retail sale and use of tangible personal property in Tennessee. The Act does not impose a tax on imports from and exports to foreign countries in violation of the United States Constitution.

ANALYSIS

The Retailers' Sales Tax Act, Tennessee Code Annotated §§ 67-6-101 *et seq.*, imposes a tax "on the sales price of each item or article of tangible personal property when sold at retail in this state." Tenn. Code Ann. § 67-6-202(a). The sales tax is a tax on "the privilege of engaging in the business of selling tangible personal property at retail in this state." *Id.* The rate of the tax is seven percent. *Id.* "Retail sale" is defined as "any sale, lease, or rental for any purpose other than for resale, sublease, or subrent." Tenn. Code Ann. § 67-6-102(79). The Act also imposes a tax "at the rate of the tax levied on the sale of tangible personal property at retail by the provisions of § 67-6-202 of the purchase price of each item or article of tangible personal property when the tangible personal property is not sold, but is used, consumed, distributed, or stored for use or consumption in this state; provided, that there shall be no duplication of the tax." Tenn. Code Ann. § 67-6-203(a). "Use" is defined as "the exercise of any right or power over tangible personal property incident to the ownership thereof, except that it does not include the sale at retail of that property in the regular course of business." Tenn. Code Ann. § 67-6-102(97)(A).

Article I, Section 9, Clause 5 (the Export Clause) of the United States Constitution provides, "[n]o tax or duty shall be laid on articles exported from any state." Article I, Section 10, Clause 2 (the Import-Export Clause) of the United States Constitution provides, in pertinent part, "[n]o State shall, without the consent of the congress, lay any imposts or duties on imports or exports, except what may be absolutely necessary for executing its inspection laws."

Neither the Export Clause nor the Import-Export Clause is applicable to purely interstate transactions. Foreign commerce must be involved for either the Export Clause or the Import-Export Clause to be implicated. The Export Clause prohibits the federal government from imposing a tax on exports from a state to a foreign country. The Import-Export Clause prohibits the states from imposing taxes on imports from and exports to a foreign country. Neither of these prohibitions applies to purely interstate transactions. Thus neither Clause prohibits a state from taxing articles brought into it from another state. *See Richfield Oil Corp. v. State Bd. of Equalization*, 329 U.S. 69, 78 (1946); *Dooley v United States*, 183 U.S. 151, 154 (1901).

Although the Export Clause and Import-Export Clause do not apply under the circumstances described, the Commerce Clause may be implicated. States are prohibited from collecting taxes from businesses that do not have sufficient nexus with the taxing state. The nexus requirement stems from the Commerce Clause, not the Export Clause or the Import-Export Clause. Article I, Section 8, Clause 3 of the United States Constitution gives Congress the power "[t]o regulate commerce with foreign nations, and among the several states, and with the Indian tribes." Under the Supreme Court's Commerce Clause jurisprudence, "with certain restrictions, interstate commerce may be required to pay its fair share of state taxes." *D.H. Holmes Co. v. McNamara*, 486 U.S. 24, 31 (1988); *see also Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 623-624 (1981) ("It was not the purpose of the commerce clause to relieve those engaged in interstate commerce from their just share of [the] state tax burden even though it increases the cost of doing business") (internal quotation marks and citation omitted). A tax does not offend the Commerce Clause so long as the "tax [1] is applied to an activity with a substantial nexus with the taxing State, [2] is fairly apportioned, [3] does not discriminate against interstate commerce, and [4] is fairly related to the services provided by the State." *Quill Corp. v. North Dakota ex rel. Heitkamp*, 504 U.S. 298, 311 (1992), *quoting Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977). "[T]he „substantial nexus' requirement is not, like due process' „minimum contacts' requirement, a proxy for notice, but rather a means for limiting state burdens on interstate commerce." *Id.* at 313.

In *Quill*, the Court reaffirmed the bright-line rule that physical presence in the taxing state is required to establish "substantial nexus" for purposes of requiring an out-of-state seller to collect sales and use taxes. Ownership of property or presence of employees, however, is not the only means of establishing the physical presence necessary for nexus. Physical presence by an out-of-state seller can also arise from the activities of its affiliates or independent contractors provided that these activities "are significantly associated with the taxpayer's ability to establish and maintain a market in this state for the sales." *Tyler Pipe Industries, Inc. v. Washington Department of Revenue*, 483 U.S. 232, 250 (1987). The imposition of Tennessee's sales and use taxes on out-of-state businesses with respect to items delivered or used in Tennessee is thus constitutionally permissible, provided that "substantial nexus" is established.

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