

COPY

IN THE CHANCERY COURT FOR THE STATE OF TENNESSEE
20TH JUDICIAL DISTRICT, DAVIDSON COUNTY,
AT NASHVILLE

AMERICAN CATALOG MAILERS)
ASSOCIATION and NETCHOICE,)

Plaintiffs,)

v.)

TENNESSEE DEPARTMENT OF)
REVENUE and DAVID GERREGANO,)
in his capacity as the Commissioner of the)
Tennessee Department of Revenue,)

Defendants.)

No. 17-307 IV

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**VERIFIED COMPLAINT
FOR DECLARATORY JUDGMENT**

Pursuant to Tenn. Code Ann. § 4-5-225(a), Plaintiffs American Catalog Mailers Association (“ACMA”) and NetChoice (together, the “Plaintiffs”) bring this Complaint for Declaratory Judgment against the Tennessee Department of Revenue (“Department”) and David Gerregano, in his capacity as Commissioner of Revenue of the State of Tennessee. The Plaintiffs complain and allege as follows:

INTRODUCTION

1. This is an action for declaratory judgment by the ACMA and NetChoice challenging the constitutionality of Tennessee Department of Revenue Regulation 1320-05-01-.129(2) (“Rule 129”). Rule 129 was adopted by the Department with the express understanding that its terms contradict the United States Supreme Court’s decision in *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992), regarding the limitations on state taxing power under

the Commerce Clause of the United States Constitution. The Supreme Court in *Quill* held that a State lacks the authority under the Commerce Clause to impose state sales and use tax collection and reporting obligations upon a seller that has no physical presence in the state, either directly or through third parties, and whose only connection with the state is communicating with customers via the instrumentalities of interstate commerce, *i.e.*, telephone, U.S. mail, common carrier, and now the Internet. *See Quill Corp.*, 504 U.S. at 313-19. Rule 129 imposes the obligation to register for, collect, and remit Tennessee sales tax expressly upon retailers that have no physical presence in the State, but who “engage in the regular or systematic solicitation of consumers in this State through any means” and “make sales that exceed \$500,000 to consumers in this State during the previous twelve-month period.” Because Rule 129 violates the *Quill* physical presence requirement, usurps the role of Congress in regulating interstate commerce, and unlawfully expands the State’s taxing authority over companies, individuals, and organizations located throughout the United States, and potentially the world, based solely on their having customers in Tennessee, Rule 129 is plainly unconstitutional.

THE PARTIES

2. Plaintiff American Catalog Mailers Association is incorporated in Washington, D.C. and is the leading trade association in the United States representing the interests of companies, individuals, and organizations engaged in and supporting catalog marketing.
3. Plaintiff NetChoice is incorporated in Washington, D.C., and is a leading trade association of Internet companies and organizations dedicated to advancing the interests of eCommerce businesses and online consumers.

4. The Department is the state agency responsible for the administration of Tennessee's sales and use tax laws. The Department promulgated Rule 129 and is responsible for its enforcement.
5. Defendant David Gerregano ("Commissioner") is the Commissioner of the Tennessee Department of Revenue and is charged with the enforcement of Rule 129.

JURISDICTION AND VENUE

6. The Court has jurisdiction to adjudicate this action under the Tennessee Uniform Administrative Procedures Act, Tenn. Code Ann. § 4-5-225(a).
7. Pursuant to Tenn. Code Ann. § 4-5-223(a), the Plaintiffs on January 27, 2017, filed with the Department a Petition for a Declaratory Order contesting the validity of Rule 129. The petition asserted that Rule 129 is unconstitutional under the Commerce Clause and *Quill*, and that the Department lacked the authority under Tennessee law to promulgate the rule.
8. On March 3, 2017, in accordance with Tenn. Code Ann. § 4-5-223(a)(2), the Commissioner declined to issue a declaratory order in response to the Plaintiffs' petition, and confirmed that the Plaintiffs could proceed to file this action for declaratory judgment in this Court, in accordance with Tenn. Code Ann. § 4-5-225(a).
9. Venue is also proper in this Court under Tenn. Code Ann. § 4-5-225(a).

STANDING

10. The ACMA and NetChoice each have standing to bring this complaint on behalf of their members who are affected by Rule 129.
11. The ACMA and NetChoice each have at least one member that would be required to register, collect, and remit Tennessee sales and use tax under Rule 129, despite the fact that the affected member(s) lack any physical presence in Tennessee.

12. Protecting their members from state regulations that violate constitutional protections is an interest germane to the purpose of both the ACMA and NetChoice.
13. The ACMA and NetChoice challenge Rule 129 as unconstitutional, on its face. Neither the claims they assert on behalf of their respective members, nor the declaratory relief they seek on behalf of their respective members, requires the participation of individual members in this lawsuit.

ALLEGATIONS

14. The United States Supreme Court, in *Quill*, held that sellers “who do no more than communicate with customers in the State by mail or common carrier as a part of a general interstate business” lack the necessary “substantial nexus” with a State for the State to require such out-of-state sellers to collect and remit the State’s sales and use taxes. 504 U.S. at 307, 313-319.
15. The Court in *Quill* reaffirmed that in order for a State to have the authority under the “substantial nexus” standard of the Commerce Clause to require an out-of-state seller to collect or report the State’s sales and use taxes, the seller must have a “physical presence” in the state. *Id.* at 314, 317-18.
16. The United States Supreme Court has not overruled, superseded, or limited its decision in *Quill*.
17. The physical presence requirement of *Quill* currently remains the law of the land under the United States Constitution. The States, and all state agencies and officials, including the Defendants, are bound by *Quill*.
18. The Defendants promulgated Rule 129, which provides, in pertinent part:
 - (2) Out-of-state dealers who engage in the regular or systematic solicitation of consumers in this state through any means and make sales

that exceed \$500,000 to consumers in this state during the previous twelve-month period also have a substantial nexus with this state.

(a) By March 1, 2017, these dealers, if they have not already done so, shall register with the Department for sales and use tax purposes and thereby affirmatively acknowledge that they will collect and remit sales and use taxes to the Department July 1, 2017. Beginning July 1, 2017, unless a later date is established by the Department by notice, these dealers shall report and pay the appropriate tax to the Department on sales of tangible personal property and other taxable items delivered to consumers in this state.

Rule 1320-05-01-.129(2).

19. Rule 129 requires affected retailers to register for Tennessee sales tax by March 1, 2017, and to collect and remit Tennessee sales and use taxes to the Department by July 1, 2017.
20. On its face, Rule 129 runs afoul of the *Quill* physical presence standard. By the plain terms of the rule, an out-of-state seller may be required to collect and remit Tennessee sales and use tax based solely on soliciting sales from outside of Tennessee and making sales in excess of the statutory minimum of \$500,000. No physical presence in the State is required. As a result, Rule 129 is unconstitutional.
21. The Defendants do not contest that *Quill* remains controlling precedent and that Rule 129 is at odds with *Quill*. The Department asserted in its response to the comments it received from the ACMA during the Department's rulemaking process contesting the constitutionality of Rule 129 that the Department "believes that there is a strong possibility that the Supreme Court will distinguish or reconsider *Quill*." The Department in adopting Rule 129 thus relied not on current law, but on a hoped-for future change in the *Quill* physical presence standard by the United States Supreme Court. An anticipated change in law cannot be the basis for an administrative regulation that contravenes existing Supreme Court precedent.

22. The Defendants lack the authority to disregard the Supreme Court’s controlling precedent in *Quill* based on the conclusion that subsequent developments may have undermined it.

As the Supreme Court has repeatedly made clear:

We reaffirm that “if a precedent of this Court has direct application in a case, yet appears to rest on reasons rejected in some other line of decisions, [lower courts] should follow the case which directly controls, leaving to this Court the prerogative of overruling its own decisions.”

Agostini v. Felton, 521 U.S. 203, 237 (1997) (citing *Rodriguez de Quijas v. Shearson/Am. Express, Inc.*, 490 U.S. 477, 484, (1989) [brackets added]. The same is plainly true of state administrative agencies and officials, including the Defendants.

23. The Defendants also lack authority to promulgate Rule 129 under Tennessee law.

24. Pursuant to Tenn. Code Ann. § 67-6-102(a), the Commissioner of Revenue is vested with power to prescribe rules and regulations “not inconsistent with law.”

25. Likewise, as to sales and use taxes, the Commissioner has the power “to make and publish reasonable rules and regulations not inconsistent with this chapter or the other laws, or the constitution of this state or the United States, for the enforcement of this chapter and the collection of revenues hereunder.” Tenn. Code Ann. § 67-6-402(a).

26. The Tennessee Legislature has thus expressly limited the authority of the Commissioner and the Department to promulgate rules only to the extent that they are consistent with the U.S. Constitution. Rule 129, however, violates the Commerce Clause.

COUNT I – Declaratory Judgment

27. Plaintiffs incorporate the allegations of paragraphs 1–26 as if fully set forth herein.

28. *Quill* bars a state from requiring sales and use tax collection and reporting by an out-of-state retailer that has no physical presence in the state.

29. Rule 129 expressly requires out-of-state catalog merchants and Internet sellers that do not have a physical presence in the state but engage in the regular or systematic solicitation of Tennessee consumers, and make \$500,000 in Tennessee sales during the prior twelve (12) months, to collect and remit Tennessee sales and use taxes.
30. This Court is empowered under Tenn. Code Ann. § 4-5-225 to determine the validity of Rule 129 under the U.S. Constitution and Tennessee law.
31. Rule 129, on its face, violates the Commerce Clause under *Quill*.
32. This Court is bound to follow and enforce Supreme Court precedent.
33. The Defendants lacked the authority to promulgate Rule 129 under Tenn. Code Ann. §§ 67-6-102(a) and 67-6-402(a), because Rule 129 violates the U.S. Constitution.
34. This Court should declare Rule 129 unconstitutional, invalid, and unenforceable and award such further relief as is just and proper.

COUNT II – Declaratory Judgment

35. Plaintiffs incorporate the allegations of paragraphs 1–34 as if fully set forth herein.
36. The Due Process Clause of the United States Constitution, made applicable to the States through the Fourteenth Amendment, requires a definite link and a minimum connection between the state and a person it seeks to tax.
37. The Supreme Court has not determined whether, for purposes of the Due Process Clause, the prescriptive jurisdiction of a state, *i.e.*, its jurisdiction to impose tax or regulatory obligations, is co-extensive with the state’s adjudicative jurisdiction.
38. The minimum threshold in Rule 129 for asserting prescriptive jurisdiction over sellers that have no physical presence in the state is inconsistent with the requirements of the Due Process Clause.

39. This Court is empowered under Tenn. Code Ann. § 4-5-225 to determine the validity of Rule 129 under the U.S. Constitution and Tennessee law.
40. This Court should declare Rule 129 unconstitutional, invalid, and unenforceable under the Due Process Clause and award such further relief as is just and proper.

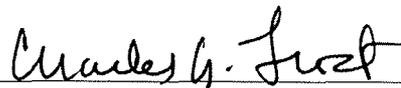
PRAYER FOR RELIEF

WHEREFORE, Plaintiffs respectfully pray that the Court:

- (A) enter a declaration that Rule 129 is unconstitutional, invalid as a matter of Tennessee law, and unenforceable;
- (B) enter judgment for the Plaintiffs;
- (C) award the Plaintiffs their attorneys' fees and costs; and
- (D) grant such further relief as the Court deems just and proper.

DATED this 30th day of MARCH, 2017.

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*Admission *Pro Hac Vice* pending

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VERIFICATION

After first being duly sworn, the undersigned affirms that the factual statements pertaining to the American Catalog Mailers Association in this Complaint are true and correct and based on my personal knowledge, to the best of my information, knowledge and belief.



Hamilton Davison
President & Executive Director
American Catalog Mailers Association

District of Columbia: SS

Sworn and subscribed before me
this 27 day of March, 2017.



NOTARY PUBLIC

My Commission Expires: 09/30/2017

