

**STATE OF TENNESSEE
OFFICE OF THE ATTORNEY GENERAL**

February 26, 2014

Opinion No. 14-22

Authority of County School Board to Compromise Liquor-by-the-Drink Tax Revenue

QUESTIONS

1. Where a municipality receives tax revenue from the liquor-by-the-drink tax imposed by Tenn. Code Ann. § 57-4-301(c) but fails for a period of years to remit a portion of the proceeds to the county school fund, does the county school board have the authority to forgive or compromise any such unremitted tax revenue?

2. Assuming that the county school board lacks the authority to forgive or compromise the municipality's obligation to remit already-collected liquor-by-the-drink tax revenue:

(a) Is the municipality liable for interest on any past-due payments, and, if so, at what rate?

(b) Would a claim by the county school board to recover any past-due payments be subject to any statute of limitations?

(c) May the county school board agree to a payment plan with the municipality for payment of any past-due amounts?

3. Is the municipality entitled to offset its liability for already-collected but unremitted liquor-by-the-drink tax revenue by relying upon local-option sales tax revenue previously remitted for a period of years to the county school system?

4. Is the municipality entitled to offset its liability for already-collected but unremitted liquor-by-the-drink tax revenue by relying upon unpaid water-quality fees previously assessed for a period of years against the county school system, or is the municipality estopped by its previous failure to demand such payment from the county or its supported agencies except the school system?

5. May the municipality reduce future liquor-by-the-drink tax payments to the county school fund by the amount of the county school system's annual water-quality fee established by local ordinance?

OPINIONS

1. The county school board does not have authority to waive its statutory right to receive liquor-by-the-drink taxes under Tenn. Code Ann. § 57-4-306(a)(2)(A).

2(a). No statutory provision exists for the accrual of interest on undistributed liquor-by-the-drink tax revenues.

(b). A county school board's claim for recovery of unremitted liquor-by-the-drink tax revenues is not subject to any statute of limitations. In seeking to recover tax revenues that should have been allocated to the school fund pursuant to state statutes governing education funding, the county would be exercising a sovereign function, and statutes of limitations do not apply to the exercise of such a function.

(c). The county may agree to a payment plan by which the municipality pays the undistributed liquor-by-the-drink tax revenues over a period of time.

3. The municipality is not entitled to offset its liability for collected but undistributed liquor-by-the-drink tax revenues by relying upon the local sales tax revenues that are separately distributed to the county school fund.

4. The municipality may not offset its liability for unremitted liquor-by-the-drink tax revenues by any amounts owed by the county school system for unpaid water-quality fees.

5. The municipality may not reduce future liquor-by-the-drink tax payments to the county school fund by any amounts that the county school system owes in water-quality fees.

ANALYSIS

Tenn. Code Ann. § 57-4-301(c) provides for the levying of a 15% tax on the sales prices of all alcoholic beverages sold for consumption on the premises. This tax, known as the "liquor-by-the-drink tax," is computed on the gross sales receipts and includes each and every retail sale. *Id.* The tax is collected by the Tennessee Department of Revenue and distributed pursuant to a formula that calls for a portion of the tax proceeds to be distributed to municipalities that have authorized the sale of liquor by the drink. Tenn. Code Ann. § 57-4-306(a)(2)(A). "[A]ny proceeds expended and distributed to municipalities which do not operate their own school systems separate from the county are required to remit one half (1/2) of their proceeds of the gross receipts liquor-by-the-drink tax to the county school fund." *Id.*

1. A school district does not have the authority to waive its statutory rights to receive tax revenues. *See* Tenn. Att'y Gen. Op. 97-104 (July 28, 1997) (involving undistributed local-option sales tax). "[T]axes are levied and collected for

the public use and upon public trusts,” and “[i]t is not in the power of the [municipal or county government] to relieve one and impose upon another a public burden, and no laches on its part or that of its officers can defeat the right of the public to have collected and rightfully appropriated, the public taxes.” *City of Memphis v. Looney*, 68 Tenn. 130, 136 (1877); accord *City of Maryville v. Blount County*, No. 03A01-9209-CH-00320, 1993 WL 1887, at *5 (Tenn. Ct. App. Jan. 6, 1993) (no perm. app. filed). Accordingly, a county school board lacks the authority to waive its right to liquor-by-the-drink tax revenue. Moreover, even if a school board’s entitlement to such tax revenue could be waived, it would require the approval of the county commission, since it is the county commission that “has the authority to appropriate the funds necessary to carry out the county education program.” *State ex rel. Weaver v. Ayers*, 756 S.W.2d 217, 222 (Tenn. 1988)¹.

2. In contrast to this State’s general revenue laws, which impose interest at specific rates on unpaid tax liabilities, *see, e.g.*, Tenn. Code Ann. § 67-1-801, there exists no specific statutory authority for interest to accrue on state tax revenues that have been distributed to a local governmental authority but have not been properly distributed by that authority.²

Under some circumstances not applicable here, general statutes of limitations may apply to actions brought by counties and municipalities. *See, e.g.*, *City of Knoxville v. Gervin*, 169 Tenn. 532, 89 S.W.2d 348 (1935) (holding that 10-year statute of limitations barred city’s suit to enforce paving assessment lien); *State ex rel. Lawrence County v. Hobbs*, 194 Tenn. 323, 250 S.W.2d 549 (1952) (holding that 10-year statute of limitations barred county’s suit against clerk and master for return of allegedly illegal salary payments). General statutes of limitations do not apply, however, when the matter at issue involves the local government’s exercise of a sovereign function. *Gervin*, 169 Tenn. at 536, 250 S.W.2d

¹ In Tenn. Att’y Gen. Op. 97-104, this Office went on to opine that a special school district *could* settle an existing lawsuit against a county involving the school district’s right to receive a portion of local-option sales tax revenue, because “[s]uch a settlement would amount to the resolution of a debt, not the waiver of statutory rights to receive tax revenues.”

[W]hen that entitlement [to local sales tax revenue] and the amount thereof are in litigation, the [school district] can agree upon a sum to resolve the issues about such an alleged debt, with the approval of the court. Thus it is the opinion of this Office that the parties have power to negotiate a settlement of the lawsuit by agreeing to resolve and satisfy an alleged debt but not by an explicit waiver of their statutory entitlement to revenues.

Id. *See State ex rel. Paduch v. Washington Cnty.*, No. 03A01-9311-CH-00397, 1994 WL 421083, at *10 (Tenn. Ct. App. Aug. 12, 1994).

² For matters that are the subject of litigation, prejudgment interest may be awarded by a court in accordance with the principles of equity in an amount not to exceed 10%. Tenn. Code Ann. § 47-14-123.

at 351. “Public education in Tennessee is primarily a state function.” *City of Maryville*, 1993 WL 1887, at *6. In seeking to recover tax revenues that should have been allocated to it pursuant to state statutes governing education funding, the county “acts as an arm of the state and is exempt from the statute of limitations.” *Id.* A general statute of limitations cannot defeat the public’s right to have the taxes allocated to the correct local governmental body. *See id.* (citing *Looney*, 68 Tenn. at 136).³

Although the county school board may not waive its statutory right to receive liquor-by-the-drink tax revenues designated for the county school fund, the county may agree to allow the municipality to pay the undistributed tax revenues over time. Such an agreement would not constitute an unauthorized waiver of the school board’s statutory right to receive those revenues.

3. The municipality is not entitled to offset its liability for collected but undistributed liquor-by-the-drink tax revenues by relying upon the local-option sales tax approved by the voters. The municipality’s obligation to distribute liquor-by-the-drink tax revenues to the county school fund is independent of and separate from its obligation to distribute a portion of local option sales taxes to the school fund. *See* Tenn. Code Ann. § 57-4-306(a)(2)(A) (distributing portion of liquor-by-the-drink taxes to county school fund); Tenn. Code Ann. § 67-6-712(a)(1) (distributing portion of local-option sales taxes to school fund).

4. The municipality may not offset its liability for unremitted liquor-by-the-drink taxes by any amounts owed by the county school system for unpaid water-quality fees. The liquor-by-the-drink taxes are not owed directly to the county school board, but to the county school fund, which is administered by the county trustee and appropriated by the county commission. In contrast, any amounts paid by the county school board to cover the school system’s continuing operations, such as water-quality fees, should be paid out of school-system funds that have already been budgeted and appropriated to the school board by the county commission. Inasmuch as the municipality is dealing with two distinct entities and accounts, it cannot achieve a direct setoff of the amounts due. Instead, the municipality should collect the debt for water-quality fees from the school board just as the municipality would collect any other debt owed to it.⁴

³ The specific six-year statute of limitations applicable to tax collections would not apply to the school board’s claim for tax revenues because the taxes in dispute have already been collected by the Department of Revenue. *See* Tenn. Code Ann. § 67-1-1501. The school board would not be attempting to enforce the collection of liquor-by-the-drink taxes. Rather, the school board would be seeking to vindicate its right to receive a portion of the liquor-by-the-drink tax revenues that were received by the municipality.

⁴ The municipality is not estopped from collecting these fees by any previous failure to collect them from the county or other agencies. This Office assumes that the municipality assessed the water-quality fees pursuant to Tenn. Code Ann. § 68-221-1107(a), which authorizes municipalities to assess

5. For the same reason, the municipality may not offset future liquor-by-the-drink tax payments to the county school fund by the amounts the county school system owes in water-quality fees.

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and collect a storm-water user fee from each user of the municipality's storm-water facilities. The statute requires the municipality to base such fees on the costs of operating and maintaining the facilities and then to impose such fees "based on the user's actual or estimated proportionate contribution to the total storm water runoff from all users." *Id.* This Office has opined that user fees assessed under this statute are not taxes but are authorized user fees that may be assessed against all users of the facilities, including governmental agencies and other tax-exempt entities. *See* Tenn. Att'y Gen. Op. 06-177 (Dec. 19, 2006); Tenn. Att'y Gen. Op. 94-039 (Mar. 21, 1994); Tenn. Att'y Gen. Op. 93-57 (Sept. 3, 1993).