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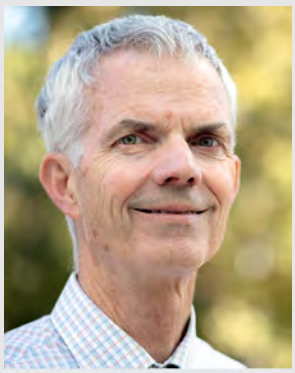

Richard L. Cram

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In this article, Cram examines the South Dakota Supreme Court's decision in *Ellingson Drainage* and the compensatory purpose of the use tax, concluding that the likelihood of the U.S. Supreme Court granting the company's petition for certiorari is remote.

When mobile equipment acquired without payment of any sales or use tax is later used in a state that imposes use tax, does the commerce clause external consistency test[1] require apportionment of the tax based on the time the property was used in the state if a credit is provided for sales or use tax paid to any other state? Ellingson Drainage Inc. raised this question in its pending petition for certiorari to the U.S. Supreme Court, arguing that in addition to the credit, the tax must be apportioned based on the amount of in-state usage time.[2]

The South Dakota Department of Revenue audited and assessed use tax against Ellingson, a Minnesota contractor, on construction equipment it brought into South Dakota to complete approximately 30 drain tile projects during the three-year audit period (2017-2020). Ellingson purchased or rented the equipment in other states without payment of any sales or use tax. Until that assessment, the equipment had not been subject to sales or use tax anywhere. Although Ellingson used some of the construction equipment in South Dakota for only one day, the DOR assessed use tax on the full value of the equipment, depreciated for age. Ellingson challenged the assessment as violating the due process and commerce clauses, arguing that it should have been apportioned given Ellingson's brief usage of some of the equipment in the state, even though South Dakota provides a credit for sales or use tax paid to other states.

The South Dakota Supreme Court affirmed the assessment, declaring that the purpose of use tax is to serve as a "sales tax substitute,"[3] ensuring that all property sold or used in South Dakota is subject to either sales tax or use tax.[4] The court applied the *Complete Auto* four-part test,[5]

[1] *Goldberg v. Sweet*, 488 U.S. 252, 262 (1989) ("The external consistency test asks whether the State has taxed only that portion of the revenues from the interstate activity which reasonably reflects the in-state component of the activity being taxed. We thus examine the in-state business activity which triggers the taxable event and the practical or economic effect of the tax on that interstate activity." (citation omitted)).

[2] *Ellingson Drainage Inc. v. South Dakota Department of Revenue*, Dkt. No. 23-1202, scheduled to be distributed for conference on September 30. The National Taxpayers Union Foundation filed an amicus brief supporting Ellingson. The South Dakota DOR has waived response.

[3] *Ellingson Drainage Inc. v. South Dakota Department of Revenue*, 3 N.W.3d 417, 424 (S.D. 2024) (quoting *Western Wireless Corp. v. Department of Revenue*, 665 N.W.2d 73, 75 (S.D. 2003)).

[4] *Id.*

[5] *Western Wireless*, 665 N.W.2d 73 ("A tax is not an unconstitutional burden on interstate commerce if the taxed activity [1] is sufficiently connected to the state to justify the tax, [2] the tax is fairly related to benefits provided to the taxpayer, [3] the tax does not discriminate against interstate commerce, and [4] the tax is fairly apportioned." (citing *Complete Auto Transit Inc. v. Brady*, 430 U.S. 274, 279 (1977)).

including the internal[6] and external consistency tests under the "fair apportionment" prong, relying on *Jefferson Lines*[7] (holding that sales tax on the price of an interstate bus trip ticket purchased in Oklahoma need not be apportioned based on the trip mileage in Oklahoma) in determining that the use tax did not need to be apportioned, given that South Dakota provides a credit for any sales or use tax paid to other states.[8]

Ellingson conceded that the South Dakota use tax law is internally consistent,[9] but it argues that the state's unapportioned use tax violates the external consistency test, claiming that the credit is not enough because the credit only addresses discrimination concerns.[10] The tax should also be apportioned based on in-state usage time.[11] Ellingson contends that (1) the *Ellingson* court erred in equating use tax and sales tax, because those taxes are different, so the *Jefferson Lines* holding that sales tax on an interstate bus trip need not be apportioned does not apply; and (2) use tax is analogous to an ad valorem property tax, which the court has required to be apportioned when applied to equipment used in interstate commerce (like interstate railroad rolling stock).[12]

This article will show that although Ellingson is free to make policy arguments that use tax should be apportioned, the fair apportionment prong of the *Complete Auto* four-part test — specifically, the external consistency test — does not require apportionment if the state provides a credit for sales or use tax paid to other states. First, Ellingson misunderstands the purpose of use tax and the national system within which it operates. Use tax compensates the state for lost sales tax revenue when taxable items are purchased out of state without payment of any sales or use tax and are later brought into the taxing state for use. Use tax cannot fulfill that compensatory purpose if it is apportioned. Second, precedents have established that the credit provision fully satisfies the external consistency test and any "fair apportionment" concerns by eliminating the risk of multiple taxation. Third, although the U.S. Supreme Court may not have directly addressed the issue of use tax apportionment based on in-state usage time, *Ellingson* is consistent with the many state court decisions that have done so. Finally, South Dakota's use tax is not analogous to ad valorem property tax because those two taxes serve different purposes and are assessed differently. Ellingson's business is not comparable to an interstate railroad.

Purpose of the Use Tax

Use tax is designed to compensate the state for revenue lost when goods are purchased out of state for use within the state. It is equal to the sales tax applicable if those goods had been purchased in state.[13] Since it is levied to compensate the taxing state for its incapacity to reach the corresponding sale, it is commonly paired with sales tax, and it applies only when no sales tax has been paid, or it is subject to a credit for any such tax paid.[14] States imposing sales and use taxes create a national system under which the first state in which the property is purchased or used imposes the tax. Thereafter, no other state taxes the transaction unless no prior tax has been imposed, or unless the tax rate of the prior taxing state is less, in which case the subsequent taxing state imposes a tax measured only by the differential rate.[15]

The *Ellingson* court accurately described the use tax as a substitute for sales tax. That logically flows from the compensatory purpose of use tax,

[6] *Goldberg*, 488 U.S. at 261 ("To be internally consistent, a tax must be structured so that if every State were to impose an identical tax, no multiple taxation would result." (citation omitted)).

[7] *Oklahoma Tax Commission v. Jefferson Lines*, 514 U.S. 175, 186-187 (1992).

[8] *Ellingson*, 3 N.W.3d at 424-425.

[9] *Id.* at 424.

[10] Petition at 3. Although Ellingson does not clarify what is meant by discrimination concerns, presumably that refers to South Dakota's equal tax treatment of an in-state purchaser versus an out-of-state purchaser.

[11] Petition at 1.

[12] *Id.* at 2, 11-12 (citing *Norfolk & Western Railway Co. v. Missouri State Tax Commission*, 390 U.S. 317 (1968); *Standard Oil Co. v. Peck*, 342 U.S. 382, 383-385 (1952); and *Nashville, Chattanooga, and St. Louis Railway Co. v. Browning*, 310 U.S. 362, 365-366 (1940)).

[13] *D.H. Holmes Co. v. McNamara*, 486 U.S. 24, 28 (1988).

[14] *Jefferson Lines*, 514 U.S. at 193-194.

[15] *Id.* at 194 (quoting *KSS Transportation Corp. v. Baldwin*, 9 N.J. Tax 273, 285 (N.J. Tax Court 1987)). *See Halliburton Oil Well Cementing Co. v. Reily*, 373 U.S. 64, 66 (1963) ("The purpose of such a sales-use tax scheme is to make all tangible property used or consumed in the State subject to a uniform tax burden irrespective of whether it is acquired within the State, making it subject to the sales tax, or from without the State, making it subject to a use tax at the same rate.").

which applies when no sales tax was paid on the purchase of items that are thereafter used in the state. Use tax equals the sales tax that would have been due had those items been purchased in state.

The use tax first received constitutional approval in *Henneford*.[16] Washington imposed use tax on tangible personal property used in the state and bought at retail outside the state with no sales tax having been paid. The Washington use tax law provided a credit for sales or use tax paid to any other state. The Washington Tax Commission notified certain contractors and subcontractors on the Grand Coulee Dam construction project that use tax was due on their equipment, materials, and supplies purchased outside the state, brought into the state for use, and on which no Washington sales tax had been paid. The taxpayers challenged the tax under the commerce clause as a "tax upon the operations of interstate commerce or a discrimination against such commerce obstructing or burdening it unlawfully."[17]

The U.S. Supreme Court held the use tax constitutional, "not upon the operations of interstate commerce, but upon the privilege of use after commerce is at an end,"[18] finding the tax "non-discriminatory in its operation."[19] The in-state purchaser and the out-of-state purchaser are treated equally: One pays the sales tax, and the other pays a complementary use tax, both at the same rate.[20] The Court emphasized the credit feature of the Washington use tax:

> No one who uses property in Washington after buying it at retail is to be exempt from a tax upon the privilege of enjoyment except to the extent that he has paid a use or sales tax somewhere. Everyone who has paid a use or sales tax anywhere, or, more accurately, in any state, is to that extent to be exempt from the payment of another tax in Washington.[21]
>
> . . . .
>
> When the account is made up, the stranger from afar is subject to no greater burdens as a consequence of ownership than the dweller within the gates. . . . Equality exists when the chattel subjected to the use tax is bought in another state and then carried into Washington.[22]

South Dakota's use tax operates the same way as Washington's in *Henneford*. South Dakota use tax law treats equally in-state purchasers and out-of-state purchasers that later use those items in the state. Both will owe either South Dakota sales tax or use tax at the same rate. In *Ellingson*, South Dakota was the first state to impose the tax on the property, since Ellingson paid no sales or use tax on it to any other state. Ellingson owed use tax on the full value of that equipment used in the state — even if used for only one day. Use tax cannot fulfill its compensatory purpose if, while a credit against it for sales or use tax paid to any other state is available, the tax must also be apportioned. If South Dakota apportioned its use tax based on Ellingson's one day of equipment usage in the state, the state would never see full compensation for the lost sales tax revenue that use tax was intended to compensate for. The disincentive that use tax was intended to provide against purchasing items free of sales tax outside the taxing state and then using those items in the taxing state would be defeated.

South Dakota's Credit Eliminates the Risk of Multiple Taxation

As *Jefferson Lines* emphasized, the fair apportionment prong focuses on the threat of multiple taxation.[23] The external consistency test asks, "Has the taxpayer shown that the challenged tax presents a real threat of multiple taxation?"[24] As the decisions below illustrate, the South Dakota use tax credit for sales or use tax paid to any other state resolves any risk of multiple taxation, making apportionment unnecessary.

[16] *Henneford v. Silas Mason Co.*, 300 U.S. 577 (1937).
[17] *Id.* at 581.
[18] *Id.*
[19] *Id.* at 582-583.
[20] *Id.* at 587.
[21] *Id.* at 583-584.
[22] *Id.* at 584.
[23] *Jefferson Lines*, 514 U.S. at 184-185.
[24] *Id.* at 185.

General Trading[25] authorized Iowa to impose a use tax collection duty on an out-of-state seller using sales representatives to solicit sales in Iowa. The Court pointed out that Iowa's use tax law allowed "an offsetting credit if another use or sales tax has been paid for the same thing elsewhere"[26] and found the tax to be nondiscriminatory.[27] In his concurring opinion, Justice Rutledge identified the commerce clause concern raised when two states attempt to tax the same interstate transaction: the risk of multiple taxation.[28] The Iowa credit resolved that risk. "Either one tax must fall or . . . be required to give way to the other by allowing credit as the Iowa tax does, or there must be apportionment."[29] Either the credit or apportionment resolves the risk of multiple taxation; both are not required.

In *D.H. Holmes*,[30] the Louisiana DOR assessed use tax on the cost of catalogs that D.H. Holmes, a large retailer located in Louisiana, paid to printers located outside of the state for design, printing, and mailing services to Louisiana addresses provided by the company. D.H. Holmes paid no sales tax on the catalog production and distribution costs. The company unsuccessfully contested the assessment in state court, arguing that it had not "used" the catalogs in the state and that the tax violated the commerce clause. The U.S. Supreme Court affirmed the assessment, applying the *Complete Auto* four-part test. In addressing the fair apportionment prong, the Court stated: "The Louisiana taxing scheme is fairly apportioned, for it provides a credit against its use tax for sales taxes that have been paid in other States."[31]

Goldberg[32] and *Jefferson Lines* addressed the question whether excise tax imposed on an interstate transaction needs to be apportioned. Both decisions determined that apportionment was not required, given the availability of credits.

Goldberg considered a commerce clause challenge against the Illinois telecommunications excise tax, a gross receipts tax imposed on interstate telecommunications calls originating or terminating in Illinois and charged to an Illinois service address. The tax provided a credit for payments of another state's tax on the same call. The Court affirmed the Illinois Supreme Court's determination that the tax satisfied the *Complete Auto* four-part test. The plaintiffs argued that the tax violated the fair apportionment prong in that Illinois imposed the tax on the gross proceeds of each interstate call without apportionment.[33]

The Court determined that the tax passed the internal consistency test because "if every State taxed only those interstate phone calls which are charged to an in-state service address, only one State would tax each interstate telephone call."[34] The Court addressed the risk of multiple taxation under the external consistency test,[35] finding that the credit resolved it: "To the extent that other States' telecommunications taxes pose a risk of multiple taxation, the credit provision contained in the Tax Act operates to avoid actual multiple taxation."[36]

Jefferson Lines considered whether Oklahoma's sales tax on interstate bus travel originating in Oklahoma violated the commerce clause. Applying the *Complete Auto* four-part test, the Court determined that it did not. The case focused on the fair apportionment prong — whether the sales tax should be apportioned based on mileage of the bus trip in the taxing state. The Court noted that the central purpose of the fair apportionment prong "is to ensure that each State taxes only its fair share of an interstate transaction,"[37] and this principle is "the lineal descendant of *Western Live Stock*'s prohibition of multiple taxation."[38] In other words, the fair apportionment prong concerns the risk of multiple taxation.

[25] *General Trading Co. v. State Tax Commission*, 322 U.S. 335 (1944).

[26] *Id.* at 334-335.

[27] *Id.* at 338.

[28] *International Harvester Co. v. Department of Treasury*, 322 U.S. 340, 360 (1944).

[29] *Id.*

[30] *D.H. Holmes*, 486 U.S. 24.

[31] *Id.* at 31.

[32] *Goldberg*, 488 U.S. 252.

[33] *Id.* at 260.

[34] *Id.* at 261.

[35] *Id.* at 261-262.

[36] *Id.* at 264.

[37] *Jefferson Lines*, 514 U.S. at 184 (quoting *Goldberg*, 488 U.S. at 260-261).

[38] *Id.* (referencing *Western Live Stock v. Bureau of Revenue*, 303 U.S. 250 (1938)).

Initially, the Court noted that apportionment concerns generally arise in the context of income tax on interstate business activities, with disputes involving which apportionment formula should apply for dividing a taxable pie among the states in which the taxpayer's activities took place.[39]

But the Court set a different course in the sales tax context.[40] In applying the internal and external consistency tests to sales tax on interstate sales of goods, the Court determined that there was no need to apportion the sales tax because the fact that the sale was consummated in only one state provided a sufficient safeguard against the risk of multiple taxation.[41] The Court also determined that because the sale of goods is treated as unique, the conventional sales tax has been held both internally and externally consistent.[42]

The Court then considered whether sales tax on a service (a bus trip) performed in more than one state raised apportionment concerns. The Court distinguished *Central Greyhound Lines*[43] (holding that New York's gross receipts tax imposed on the seller of interstate bus transportation services required apportionment based on mileage in the taxing state). The Court characterized the New York gross receipts tax as an income tax that exposed the seller-taxpayer to the risk of multiple taxation, so apportionment was required.[44] But as to the Oklahoma sales tax on an interstate bus trip, the Court observed that the buyer of services was no more subject to double taxation than the buyer of goods would be.[45]

The Court declared that lack of external consistency requires "a showing that the threat of multiple taxation must be 'real'"[46] and determined that Jefferson Lines had failed to show exposure to successive taxes requiring reconsideration of whether "an internally consistent tax on sales of services could fail the external consistency test for lack of further apportionment."[47] The Court then hypothesized that if Texas were to impose a gross receipts tax on the portion of the bus ride in that state, that tax would have to respect "well understood constitutional strictures"[48] and grant a credit for sales taxes paid to other states on that same bus ride, citing several use tax cases, including *Henneford*.[49]

The Court discussed the compensatory purpose of the use tax, the national system in which it operates,[50] and the equal treatment that use tax laws give to in-state and out-of-state purchasers by providing credits for other taxes paid, thus satisfying commerce clause concerns:

> Since any use tax would have to comply with Commerce Clause requirements, the tax scheme could not apply differently to goods and services purchased out of state from those purchased domestically. Presumably, then, it would not apply when another State's sales tax had previously been paid, or would apply subject to credit for such payment.[51]

The Court noted that although Oklahoma's sales tax did not provide a credit for other taxes paid, other states imposing use taxes would need to provide credits for Oklahoma sales tax to meet commerce clause requirements, so those credits would eliminate the risk of multiple taxation:

> True, it is not Oklahoma that has offered to provide a credit for related taxes paid elsewhere, but in taxing sales Oklahoma may rely upon use-taxing States to do so. This is merely a practical consequence of the structure of use taxes as generally based upon the primacy of taxes on sales, in that use of goods is taxed only to the extent that their prior sale has escaped taxation.[52]

[39] *Jefferson Lines*, 514 U.S. at 186.
[40] *Id.*
[41] *Id.* at 186-187.
[42] *Id.* at 188.
[43] *Central Greyhound Lines Inc. v. Mealey*, 334 U.S. 653 (1948).
[44] *Jefferson Lines*, 514 U.S. at 190.
[45] *Id.*
[46] *Id.* at 185.
[47] *Id.*
[48] *Id.* at 192, n.6.
[49] *Id.*
[50] *Id.* at 194 (quoting *KSS Transportation*, 9 N.J. Tax at 285).
[51] *Id.* at 194.
[52] *Id.*

The court relied upon the credit feature of use tax imposed by other states in determining that Oklahoma sales tax on an interstate bus trip did not require apportionment. Jefferson Lines had not shown any real risk of multiple taxation, failing its burden of demonstrating by clear and cogent evidence that apportionment by mileage was required.[53]

In *Ellingson*, the external consistency test asks whether South Dakota has imposed its use tax only on that portion of the revenues from the interstate activity reasonably reflecting the in-state component of the activity being taxed. It examines the in-state business activity triggering the taxable event and the practical or economic effect of the tax on that interstate activity.[54] South Dakota taxed Ellingson's use of its construction equipment in South Dakota — an activity that occurred entirely within the state. This activity triggered South Dakota's use tax because Ellingson had paid no sales or use tax to any other state. The practical or economic effect of South Dakota's use tax was to require Ellingson to pay the same amount of tax that it would have paid had it purchased that equipment in South Dakota. That economic effect fulfilled the purpose of the use tax: compensating South Dakota for the sales tax revenue lost when Ellingson purchased that equipment out of state without paying any sales tax and later brought it into South Dakota for use on construction projects.

Ellingson failed to show that it had any real risk of multiple taxation. If it had paid sales or use tax to any other state, it would have received a credit for that amount against its use tax liability. The South Dakota credit provision eliminated the risk of multiple taxation, making use tax nondiscriminatory against interstate commerce by treating in-state and out-of-state purchasers equally. That is all the external consistency test requires; length of in-state use is irrelevant.

Ellingson Is Consistent With Other State Court Decisions

Ellingson is consistent with numerous state court decisions that directly addressed the question whether use tax on the usage of mobile equipment in the taxing state requires apportionment based on in-state time length. Those opinions uniformly determined that no apportionment was required. Ellingson cited some of them in its petition[55]: *Miller*[56] (Minnesota use tax assessment against farmer on full price of farm equipment purchased out of state and used 68 percent of the time in Minnesota upheld, reversing lower court's pro rata reduction of the assessment based on 68 percent of in-state versus out-of-state usage); *Woods*[57] (Tennessee use tax assessment against out-of-state contractor on materials purchased out of state and delivered to in-state construction site for installation by subcontractors upheld); *Louisville Title Agency*[58] (owner of boat purchased out of state and brought into Ohio for repairs, maintenance, and installation of new equipment during two 10-day periods and docked at an Ohio yacht club for three days held liable for use tax on boat price); *Union Oil*[59] (owner purchasing two tankers out of state and leasing them back to seller who then operated them approximately 70 percent of the time in California owed California use tax on the full purchase price of the tankers); *Randall*[60] (Rhode Island resident liable for use tax on use of yacht purchased out of state and brought in state only periodically for repairs, maintenance, supplies, and brief social visits); and *Stetson*[61] (owner of yacht purchased out of state and brought within state for one month held liable for Connecticut use tax on purchase price) ("Even a very brief and limited use . . . is sufficient to justify the imposition of the tax.").

[53] *Id.* at 195-196.

[54] *Goldberg*, 488 U.S. at 262.

[55] Petition at 2, n.1.

[56] *Miller v. Commissioner*, 359 N.W.2d 620, 621-622 (Minn. 1985).

[57] *Woods v. M.J. Kelley Co.*, 592 S.W.2d 567, 571 (Tenn. 1980).

[58] *Louisville Title Agency for N.W. Ohio Inc. v. Kosydar*, 330 N.E.2d 899 (Ohio 1975).

[59] *Union Oil Co. v. State Board of Equalization*, 386 P.2d 496 (Cal. 1963).

[60] *Randall v. Norberg*, 403 A.2d 240 (R.I. 1979).

[61] *Stetson v. Sullivan*, 211 A.2d 685, 687 (Conn. 1965).

In determining that the commerce clause did not require pro rata reduction of use tax on the full purchase price of farm equipment purchased out of state and used in Minnesota for only a portion of the audit period, the *Miller* court stated: "By complementing the sale tax, the use tax eliminates incentive to make major purchases in states with a lower sales tax. This purpose would be substantially frustrated if the allocation formula adopted by the Tax Court were allowed to stand."[62]

Other state courts have found no use tax apportionment requirement based on duration of in-state usage. In *Regency Transportation*,[63] the Supreme Judicial Court of Massachusetts affirmed the commissioner's use tax assessment against a Massachusetts trucking company on the full purchase price of its tractor-trailer fleet purchased out of state and used in conducting interstate freight operations. No sales or use tax had previously been paid.[64] The fleet vehicles, registered in New Jersey, had been used or stored in Massachusetts at various times during the audit period. The company had terminals, warehouses, and maintenance facilities in both Massachusetts and New Jersey. Thirty-five percent of the fleet's maintenance and repair operations were performed in Massachusetts. The trucking company challenged the assessment, contending, among other arguments, that it should have been apportioned based on the fleet's Massachusetts road usage during the audit period. In applying the internal and external consistency tests under the fair apportionment prong of the *Complete Auto* four-part test to determine that use tax need not be apportioned, the court pointed to the Massachusetts use tax credit for sales or use tax paid in other states, which disposed of the risk of multiple taxation.[65] The court emphasized that use tax is intended to prevent the loss of sales tax revenue from out-of-state purchases.[66]

In *General Motors*[67] (Denver use tax assessment against General Motors on cost of parts and materials in motor vehicles used for 1 to 4 percent of their useful lives in the city for testing purposes upheld as externally consistent), the court stated:

> The external consistency requirement does not require that sales and use taxes be apportioned based on the length of time tangible property remains in the taxing jurisdiction.
>
> . . . .
>
> Use taxes are externally consistent if the contested tax contains a credit that operates to eliminate multiple taxation . . . regardless of how long the property remains in the taxing jurisdiction.[68]

In *Whitcomb Construction*[69] (unapportioned Vermont use tax assessment upheld against out-of-state construction contractor's use of airplane in state for 17 percent of its flights in charter operations and ferrying personnel and equipment into the state to perform construction work), the court stated:

> The Commerce Clause does not require apportionment in addition to a tax credit. The rule of *Complete Auto* . . . requiring a tax on interstate commerce to be fairly apportioned is satisfied [where the] the state has provided a credit in lieu of apportionment.

In *PPG Industries*,[70] PPG purchased pace cars and shipped them to various races throughout the country, including Ohio. It also stored and staged those vehicles in Ohio when not in use. The tax commissioner assessed use tax against PPG for its use of the pace cars in Ohio, and PPG challenged

[62] *Miller*, 359 N.W.2d at 622.

[63] *Regency Transportation Inc. v. Commissioner*, 42 N.E.3d 1133 (Mass. 2016).

[64] Many of the states in which the vehicles were purchased provided "rolling stock" sales tax exemptions, but Massachusetts did not.

[65] *Regency*, 42 N.E.3d at 1137-1140.

[66] *Id.* at 1141.

[67] *General Motors Corp. v. City and County of Denver*, 990 P.2d 59, 72 (Colo. 1999).

[68] *Id.* at 72-73.

[69] *Whitcomb Construction Corp. v. Commissioner*, 479 A.2d 164, 168 (Vt. 1984).

[70] *PPG Industries Inc. v. Tracy*, 659 N.E.2d 1250 (Ohio 1996).

the assessment as violating the commerce clause, arguing that lack of apportionment of the use tax violated the external consistency test. The Ohio Supreme Court upheld the assessment, determining that Ohio's law providing a credit for sales or use taxes paid to other states satisfied the external consistency test.

Use Tax Is Not Analogous to Ad Valorem Property Tax

Ellingson argues that its use of equipment in South Dakota is an interstate activity and that South Dakota's use tax assessment is analogous to ad valorem property tax imposed on that property.[71] Ellingson claims that the assessment should be apportioned, similar to the requirement that an ad valorem property tax assessment on rolling stock of an interstate railroad must be apportioned, citing *Norfolk & Western*[72] (Missouri ad valorem property tax assessment on interstate railroad rolling stock apportioned based on a mileage apportionment formula held unconstitutional under the railroad's facts).[73]

But South Dakota's use tax assessment against Ellingson is not analogous to an ad valorem property tax assessment on interstate railroad rolling stock. First, use tax and ad valorem property tax are not similar. They serve different purposes and are assessed differently. Use tax is a one-time tax triggered by the "privilege of use"[74] of property in the taxing state that was purchased out of state without payment of any sales tax. It protects the state from loss of sales tax revenue and is equal to the sales tax that would have been due had that property been purchased in state. Ad valorem property tax is assessed annually on the owner of property located in the taxing state, and it provides ongoing funding for local governments.[75] Second, although Ellingson may engage in a multistate business, its activity on which use tax was imposed — use of construction equipment in South Dakota to complete drain tile projects— occurred solely within that state.[76] As previously discussed, South Dakota's use tax credit resolves any commerce clause "fair apportionment" concerns.

Conclusion

Ellingson suggests that the Court should grant its petition, saying guidance is needed on whether use tax must be apportioned when imposed on use of property in multiple states, mentioning that remote workers of a software licensee can use that software in multiple states at the same time.[77] But here, South Dakota assessed use tax on Ellingson's usage of construction equipment in only one state. Review of Ellingson's case will not provide any guidance concerning whether or how use tax on software licenses used simultaneously in multiple states should be apportioned.

Ellingson has every right to champion whatever policy arguments it can muster for adopting use tax apportionment, but the commerce clause does not require it. Use tax apportionment would conflict with the purpose of use tax: to compensate the state for lost sales tax on out-of-state purchases made without payment of sales tax when the purchaser brings those items into the state for use. Precedent clearly shows that

[71] Petition at 11.

[72] *Norfolk & Western*, 390 U.S. 317.

[73] *Id.*

[74] S.D. Codified Laws section 10-46-3.

[75] S.D. Codified Laws section 10-6-105; South Dakota DOR, "Property Tax 101" (July 2021). *See Union Oil*, 386 P.2d at 503 (distinguishing the characteristics of use tax versus ad valorem property tax) ("The use tax 'does not fall upon the owner because he is the *owner*, regardless of the use or disposition he may make of the property. It is imposed on certain of the *privileges* of ownership, but not on all of them.'" (emphasis in original)) (quoting *Douglas Aircraft Co. v. Johnson*, 13 Cal.2d 545, 551 [90 P.2d 572] (Cal. 1939)); *see also Ex parte Fleming Foods of Alabama Inc.*, 648 So. 2d 577, 579 (Ala. 1994) (The Alabama Supreme Court reversed the lower appellate court's ruling that the state and local use tax assessment against Fleming Foods on vehicles purchased out of state and on which no sales or use tax had been paid had to be apportioned. The court upheld the assessment without apportionment and distinguished the use tax from ad valorem property tax, stating: "Use tax is . . . an excise tax imposed upon the privilege of storing, using, or otherwise consuming tangible personal property purchased at retail outside the state and domiciled in the state. The use tax is not a recurring annual tax, but is a one-time tax levied at the same rate as the sales tax and is complementary to the sales tax.)." *Fleming Foods*, 648 So. 2d at 579.

[76] *Henneford*, 300 U.S. at 581 (use tax is constitutional "not upon the operations of interstate commerce, but upon the privilege of use after commerce is at an end").

[77] Petition at 3-4.

a credit like South Dakota's for sales or use tax paid to other states eliminates the risk of multiple taxation, satisfying the external consistency test and the fair apportionment prong. The *Ellingson* decision is consistent with the many state courts that answered the question whether use tax should be apportioned based on in-state usage time length, finding no constitutional apportionment requirement. Use tax and ad valorem property tax are not analogous, and South Dakota's use tax assessment on Ellingson's usage of construction equipment solely within South Dakota is not comparable to ad valorem property tax on interstate railroad rolling stock.

Given the strong precedent supporting the DOR's position, the likelihood that the Court will grant Ellingson's petition seems remote. If the Court does grant review, the DOR will be in a strong position to argue that use tax apportionment is not required. ■