No. 23-_____

IN THE

Supreme Court of the United States

ELLINGSON DRAINAGE, INC.,

Petitioner,

v.

SOUTH DAKOTA DEPARTMENT OF REVENUE,

Respondent.

On Petition for Writ of Certiorari to the Supreme Court of South Dakota

PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED

Whether South Dakota's imposition of an unapportioned use tax on the fair market value of Petitioner's movable construction equipment—some of which was used in South Dakota for one day—violates the fair apportionment requirement of the Commerce Clause.

PARTIES TO THE PROCEEDING

All parties to the proceedings below are named in the caption.

CORPORATE DISCLOSURE STATEMENT

Petitioner Ellingson Drainage, Inc. is a wholly owned subsidiary of Ellingson Holdings, Inc. and no publicly held company owns 10% or more of its stock.

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PETITION FOR WRIT OF CERTIORARI

Ellingson Drainage, Inc. ("Ellingson") respectfully petitions for a writ of certiorari to review the judgment of the South Dakota Supreme Court.

INTRODUCTION

Petitioner, a Minnesota company, engages in construction projects in South Dakota and other states. To work on these projects, Petitioner brings its equipment into the state for varying amounts of time, some as short as one day. South Dakota levies a use tax on a taxable use of property in the state. Regardless of how long the equipment is in South Dakota, the state levies the tax on the fair market value of the property. The tax should be apportioned over the period of time in which an asset is used in the state. But because the tax is unapportioned, the amount of time the equipment is used in South Dakota is irrelevant.

Failing to divide the tax base violates this Court's teachings. Apportionment of a state tax is required to comply with the dormant Commerce Clause. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977). To survive this mandate, a tax must be externally consistent. That is, a state tax must "reasonably reflect[] the in-state component of the activity being taxed," *Goldberg v. Sweet*, 488 U.S. 252, 262 (1989), and must not reach "beyond that portion of value that is fairly attributable to economic activity within the taxing State." *Okla. Tax Comm'n v. Jefferson Lines*, 514 U.S. 175, 185 (1995). South Dakota's indifference to the amount of the use of

Petitioner's equipment in the state violates the external consistency requirement.

The South Dakota Supreme Court upheld the tax based on a false syllogism. (1) The purpose of a use tax is to serve as a substitute for the sales tax. (2) A sales tax is not apportioned in the same way as other taxes. (3) Ergo, use taxes do not have to be apportioned either.

For over eight decades, however, this Court has treated a use tax as fundamentally different from a sales tax—they are not jurisprudential twins. *See McLeod v. JE Dilworth Co.*, 322 U.S. 327 (1944); *Gen. Trading Co. v. State Tax Comm'n*, 322 U.S. 335 (1944).

The South Dakota Supreme Court compounds its error that use taxes need not be apportioned by misstating the external consistency doctrine, as well as this Court's precedents.[1]

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[1] Other courts have also misapplied this Court's fair apportionment requirement, *see, e.g.*, *Miller v. Comm'r of Revenue*, 359 N.W.2d 620, 621 (Minn. 1985); *Woods v. M.J. Kelley Co.*, 592 S.W.2d 567, 571 (Tenn. 1980); *Louisville Title Agency for N.W. Ohio, Inc. v. Kosydar*, 43 Ohio St. 2d 109, 330 N.E.2d 899 (1975); *Union Oil Co. v. State Bd. of Equalization*, 60 Cal. 2d 441, 386 P.2d 496 (1963), and even when the taxable property is located and used within the state for only brief periods of the year, *see, e.g.*, *Louisville Title Agency*, 43 Ohio St. 2d 109, 330 N.E.2d 899 (property within state for 1 month); *Randall v. Norberg*, 121 R.I. 714, 403 A.2d 240 (1979) (yacht brought within state periodically for repairs, maintenance, supplies, and brief social visits); *Stetson v. Sullivan*, 152 Conn.

South Dakota provides a credit[2] to Petitioner for any sales or use taxes paid to other states on the equipment brought into the state. But a credit cannot cure the failure to apportion a use tax.[3]

This is a case of first impression; no decision of this Court has examined the constitutionality of an unapportioned use tax on movable assets. But use taxes imposed on intangible property—such as software—and multistate services, have thrust this apportionment issue onto the center stage.

For example, it is common for a taxpayer to license software from a third party. That software is

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649, 211 A.2d 685 (1965) (yacht brought within state for 1 month).

[2] South Dakota provides a reciprocal credit. In other words, it does not provide a credit against its use tax unless the state that imposed a sales tax provides a credit for sales tax paid to South Dakota. *See* S.D. Codified Laws § 10-46-6.1 ("[N]o credit may be given under this section where taxes paid on tangible personal property, any product transferred electronically, or services in another state or its political subdivisions of that state does not reciprocally grant a credit for taxes paid on similar tangible personal property or any product transferred electronically.").

[3] A credit deals with problems of discrimination, not apportionment. Other state cases have blurred this distinction. *See, e.g.*, *Gen. Motors Corp. v. City & Cnty. of Denver*, 990 P.2d 59, 72-73 (Col. 1999); *Int'l Thomson Publ'g v. Tracy*, 79 Ohio St. 3d 415, 420, 683 N.E.2d 1091 (1997); *Ex Parte Fleming Foods of Ala., Inc.*, 648 So. 2d 577, 579 (Ala. 1994); *Whitcomb Constr. Corp. v. Comm'r of Taxes*, 144 Vt. 466, 463, 479 A.2d 164 (1984); *Yamaha Corp. of Am. v. State Bd. of Equalization*, 73 Cal. App. 4th 338, 368 (1999). The South Dakota Circuit Court in this case committed the same error. App. 41a-43a. The source of this confusion might be *D. H. Holmes Co. v. McNamara*, 486 U.S. 24, 31 (1988).

used by remote workers located throughout the country. Taxpayers and the states need guidance on whether use taxes must be apportioned when imposed on property that is used in multiple states.

OPINIONS BELOW

The opinion of the South Dakota Supreme Court is reported at 2024 S.D. 8 and is reproduced in the Appendix ("App.") at 1a. The order and memorandum opinion of the Circuit Court are reproduced at App. 16a and App. 18a. They are unpublished. The final decision of the Office of Hearing Examiners is reproduced at App. 44a. The proposed decision of the Office of Hearing Examiners, which was incorporated into the Final Decision, is reproduced at App. 46a. Both are unpublished.

JURISDICTION

The judgment below, affirming a final judgment on federal constitutional grounds, was entered on February 7, 2024. This Court has jurisdiction under 28 U.S.C. § 1257(a).

CONTITUTIONAL PROVISIONS, STATUTES, AND REGULATIONS INVOLVED

U.S. Const. art. 1, § 8, cl. 3:

> The Congress shall have Power . . . To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes.

U.S. Const. amend. XIV, § 1:

> All persons born or naturalized in the United States, and subject to the jurisdiction thereof, are citizens of the United States and of the State wherein they reside. No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws.

S.D. Codified Laws § 10-45-2:

> There is hereby imposed a tax upon the privilege of engaging in business as a retailer, a tax of four and two-tenths percent upon the gross receipts of all sales of tangible personal property consisting of goods, wares, or merchandise, except as otherwise provided in this chapter, sold at retail in the state to consumers or users.

S.D. Codified Laws § 10-46-2:

> An excise tax is hereby imposed on the privilege of the use, storage, and consumption in this state of tangible personal property purchased for use in this state at the same rate of percent of the purchase price of said property as is imposed pursuant to chapter 10-45.

S.D. Codified Laws § 10-46-3:

> An excise tax is imposed on the privilege of the use, storage or consumption in this state of tangible personal property or any product transferred electronically not originally purchased

for use in this state, but thereafter used, stored or consumed in this state, at the same rate of percent of the fair market value of the property at the time it is brought into this state as is imposed by § 10-45-2. The use, storage, or consumption of tangible personal property or any product transferred electronically more than seven years old at the time it is brought into the state by the person who purchased such property for use in another state is exempt from the tax imposed herein. The secretary may promulgate rules pursuant to chapter 1-26 relating to the determination of the age and value of the tangible personal property or the product transferred electronically brought into this state.

S.D. Codified Laws § 10-46-6.1:

The amount of any use tax imposed with respect to tangible personal property, any product transferred electronically, or services shall be reduced by the amount of any sales or use tax previously paid by the taxpayer with respect to the property on account of liability to another state or its political subdivisions. However, no credit may be given under this section where taxes paid on tangible personal property, any product transferred electronically, or services in another state or its political subdivisions of that state does not reciprocally grant a credit for taxes paid on similar tangible personal property or any product transferred electronically.

S.D. Admin. R. 64:09:01:20:

> For the purposes of the exemption in SDCL 10-46-3, tangible personal property or any product transferred electronically must be more than seven years old as determined by its date of manufacture, if documented, or by the date of the purchase by the person bringing the property into this state. In the absence of independent documentary proof of the value of the tangible personal property or any product transferred electronically at the time it is brought into South Dakota, the value of the property is presumed to be the purchase price reduced by ten percent for each year of use of the property by the person bringing the property into this state. Statements, opinions, or depreciation schedules of the owner of the property are not independent documentary proof of the value of the property.

STATEMENT OF THE CASE

A. Relevant Facts

Ellingson Drainage, Inc. is a Minnesota company that specializes in installing drain tile for farming and government applications. App. 47a. Ellingson's principal place of business is in West Concord, Minnesota and, from 2017-2019, it worked in more than 20 different states, including South Dakota. *Id.* Ellingson completed approximately 30 jobs in South Dakota, ranging in price from less than $1,000 to $280,000. *Id.*

Ellingson used eleven pieces of equipment in South Dakota. The use of some of these pieces of

equipment in South Dakota was for as little as one day. The exact number of days each piece of equipment was used is irrelevant for South Dakota use tax purposes. The equipment was taxed the same regardless of how long it was in the state because South Dakota's use tax is imposed on the fair market value of the equipment and is unapportioned. App. 49a.

B. Proceedings Below

The South Dakota Department of Revenue (the "Department") conducted an audit of Ellingson's operations in South Dakota from 2017 to 2020 and assessed a use tax, pursuant to S.D. Codified Laws § 10-46-3, on the fair market value of the equipment of $60,665.44 and $14,862.88 in interest. App. 2a-3a. Ellingson appealed the assessment and objected on grounds that, *inter alia*, the tax violates the dormant Commerce Clause because it is an unconstitutional burden on interstate commerce and is not fairly apportioned. App. 2a, 49a-50a. The Office of Hearing Examiners affirmed the assessment and did not address Ellingson's constitutional arguments because "[t]he constitutional question . . . is outside the jurisdiction of [the] Office and the Department." App. 53a.

Ellingson appealed the Office of Hearing Examiners' decision to the Circuit Court of South Dakota, Sixth Judicial Circuit arguing that, *inter alia*, the tax violates the dormant Commerce Clause. App. 19a. The Circuit Court affirmed the assessment, concluding that the application of the use tax was constitutional. App. 43a.

On appeal to the Supreme Court of South Dakota, Ellingson raised two issues for review. App. 4a. First, whether the use tax as applied to Ellingson violates the Due Process Clause of the Fourteenth Amendment. *Id.* Second, whether the use tax as applied to Ellingson violates the Commerce Clause. *Id.* The Supreme Court of South Dakota, affirming the lower court's decision, stated that the tax does not violate the Commerce Clause or the Due Process Clause of the Fourteenth Amendment. App. 15a.

REASONS FOR GRANTING THE PETITION

This Court will sustain a tax under the Commerce Clause so long as it "(1) applies 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 the State provides." *South Dakota v. Wayfair, Inc.*, 585 U.S. 162, 174 (2018) (citing *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977)).

This petition should be granted because this case presents an important federal constitutional issue concerning the second requirement: Must a use tax be fairly apportioned when the tax is imposed on movable property that is temporarily in a state? Although this Court has never directly addressed this specific issue, the South Dakota Supreme Court's decision disregards this Court's external consistency requirement.

I. This Court Requires That a Use Tax Imposed on Property Temporarily in a State Must Be Apportioned to Comply with the Fair Apportionment Requirement of the Commerce Clause.

The use tax imposed on Petitioner by South Dakota does not satisfy the fair apportionment requirement of the dormant Commerce Clause. In fact, it is not apportioned at all. The South Dakota Supreme Court upheld the use tax by equating it to sales tax—a tax on a transaction occurring at a specified location, constituting a "local event"—rather

than a tax on movable property temporarily in the state. This was error.

A. South Dakota's Tax Is Not Fairly Apportioned Because It Reaches Beyond That Portion of Value That Is Fairly Attributable to the State and Violates the External Consistency Doctrine.

This Court has held that to be fairly apportioned, a tax must be "externally consistent." *Jefferson Lines*, 514 U.S. at 185. "External consistency . . . looks to the economic justification for the State's claim upon the value taxed, to discover *whether a State's tax reaches beyond that portion of value that is fairly attributable to economic activity within the taxing State*." *Id.* (emphasis added). South Dakota's use tax easily fails that test.

A use tax is generally imposed on the value or purchase price of tangible property that was used, stored or consumed in this state. *See, e.g.*, S.D. Codified Laws §§ 10-46-2, 10-46-3. The closest analog to the use tax is the property tax, which is also imposed on the value of in-state property. This Court has held that property taxes must be fairly apportioned to comply with the Commerce Clause. *Norfolk & W. Ry. Co. v. Mo. State Tax Comm'n*, 390 U.S. 317 (1968); *see also Standard Oil Co. v. Peck*, 342 U.S. 382, 383-85 (1952). *Norfolk* concerned a Missouri property tax on a railroad's rolling stock. The Court struck down a defective apportionment formula. In *Norfolk*, this Court explained:

> [A] State is not entitled to tax tangible or intangible property that is

> unconnected with the State. . . . The taxation of property not located in the taxing State is constitutionally invalid, both because it imposes an illegitimate restraint on interstate commerce and because it denies to the taxpayer the process that is his due. A State will not be permitted, under the shelter of an imprecise allocation formula or by ignoring the peculiarities of a given enterprise, to project the taxing power of the state plainly beyond its borders.

Id. at 325 (internal citations and quotes omitted); *see also Nashville, Chattanooga, and St. Louis Ry. v. Browning*, 310 U.S. 362, 365-66 (1940). A fortiori, an unapportioned use tax on property used in an interstate enterprise is unconstitutional.

Petitioner's use of equipment in South Dakota is an interstate activity. As such, a use tax must be apportioned to limit the tax imposed to the amount of value used in South Dakota. South Dakota's tax on the entire fair market value of property temporarily in the state, some as short as one day, does not "reasonably reflect" the in-state component of the use of Petitioner's equipment, and "reaches beyond that portion of value that is fairly attributable to economic activity within the taxing State." *Jefferson Lines*, 514 U.S. at 185.

South Dakota's unapportioned use tax applies regardless of the time the equipment is used in the state—whether for one day, one year, or more. The

result is that Petitioner bears "more than a fair share of the cost of the local government whose protection it enjoys." *Cent. Greyhound Lines v. Mealey*, 334 U.S. 653, 663 (1948) (internal quotes omitted).

B. The South Dakota Supreme Court Erred by Equating the Use Tax with a Sales Tax.

The South Dakota Supreme Court rejected the external consistency argument with a faulty syllogism. (1) The purpose of a use tax is to serve as a sales tax substitute. App. 4a-5a. (2) A sales tax is not apportioned. "The taxation of sales has been approved without any division of the tax base among different States." App. 11a (quoting *Jefferson Lines*, 514 U.S. at 186-87) (internal quotes omitted). (3) Ergo, use taxes do not have to be apportioned either.

The difficulty with the syllogism is that sales and use taxes are not jurisprudential twins. Eighty years ago, this Court contrasted the two taxes and struck down a sales tax and upheld a use tax under nearly identical circumstances. In *Dilworth*, 322 U.S. 327, this Court explained that sales taxes and use taxes:

> are different in conception, are assessments upon different transactions, and in the interlacings of the two legislative authorities within our federation may have to justify themselves on different constitutional grounds. A sales tax is a tax on the freedom of purchase—a freedom which wartime restrictions serve to emphasize. A use tax is a tax on the enjoyment of that which was

> purchased. In view of the differences in the basis of these two taxes and the differences in the relation of the taxing state to them, a tax on an interstate sale like the one before us and unlike the tax on the enjoyment of the goods sold, involves an assumption of power by a State which the Commerce Clause was meant to end.

Id. at 330; *see also Gen. Trading*, 322 U.S. 335. This Court has continued to accept that distinction and has never changed its view. *See Nat'l Geographic Soc'y v. State Bd. of Equalization*, 430 U.S. 551 (1977); *Jefferson Lines*, 514 U.S. 175 (1995).

The difference between sales taxes and use taxes has real consequences and is not a mere formalism. Use taxes, for example, cannot be imposed on property owned or used by the federal government or by Indian tribes. Richard D. Pomp*, Overturning Dilworth and the Impact on Tribes*, 108 Tax Notes State 773 (2023). In sharp contrast, a sales tax can be imposed on a vendor selling goods to the federal government or to an Indian tribe. *Id.*

Unlike a use tax, "a sale of goods is most readily viewed as a discrete event facilitated by the laws and amenities of the place of sale." *Jefferson Lines*, 514 U.S. at 186. As such, this Court has consistently approved "taxation of sales without any division of the tax base among different States, and ha[s] instead held such taxes properly measurable by the gross charge for the purchase, regardless of any activity outside the taxing jurisdiction that might have

preceded the sale or might occur in the future." *Id.* In reviewing whether income, gross receipts, excise and property taxes have met the fair apportionment requirement, this Court has had to "set a different course," (*id.*) looking rather to the value of the "in-state component of the activity being taxed." *Goldberg*, 488 U.S. at 262 (citing *Container Corp. of Am. v. Franchise Tax Bd.*, 463 U.S. 159, 169-170 (1983)).

This Court has emphasized other attributes of a sale that distinguish sales taxes from use taxes. *See Jefferson Lines*, 514 U.S. at 190 ("The taxable event comprises agreement, payment, and delivery of some of the services in the taxing State; no other State can claim to be the site of the same combination."); *Goldberg*, 488 U.S. at 262 ("The tax at issue has many of the characteristics of a sales tax. It is assessed on the individual consumer, collected by the retailer, and accompanies the retail purchase of an interstate telephone call"). In *Goldberg*, this Court emphasized that the tax's connection with the value to be taxed was predicated on the calls being billed, paid, or charged to a service address in the state, and provision of the service in the state. These additional considerations make it impossible for another state to claim to be the place of sale, which eliminates the possibility of multiple taxation.[4] Moveable property, however, can be subject to multiple use taxes if it is

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[4] In *Goldberg* there was the possibility of one other state imposing a tax, but Illinois provided a credit that eliminated the possibility of multiple taxation.

used in different states unless the taxes are apportioned.

The tax should be apportioned over the time period in which the equipment is used in South Dakota. The amount of the unapportioned use tax on Petitioner's property, however, disregards the time the equipment is used in South Dakota. Property used for one day in South Dakota is taxed the same as if it were used for its entire useful life. The court below justifies this result by misstating the external consistency test as requiring that a tax be fairly related to *benefits* provided to the taxpayer (App. 9a)—rather than requiring that the tax reasonably reflects the in-state component of the activity being taxed, *Goldberg*, 488 U.S. at 262, or the economic justification for a state's claim upon the value taxed. *Jefferson Lines*, 514 U.S. at 185.

The court then compounds its error by misapplying *Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 623 (1981), for the proposition that the only benefit a taxpayer is entitled to is that "'of living in an organized society.'" App. 9a (quoting *Commonwealth Edison*, 453 U.S. at 623). That statement, however, which would nullify the external consistency test, was issued under the fourth prong of *Complete Auto* and not the second prong that is at issue in this case. Furthermore, *Commonwealth Edison* was decided in 1981, and in the ensuing four decades this Court cited the external consistency test five times. *See, e.g.*, *Gen. Motors Corp. v. Tracy*, 519 U.S. 278, 299 n.12 (1997); *Jefferson Lines*, 514 U.S. at 185; *Trinova Corp. v. Michigan Dep't of Treasury*, 498 U.S. 358, 380-81 (1991); *Goldberg*, 488 U.S. at 262-64

(1989); *Container Corp. of Am. v. Franchise Tax Bd.*, 463 U.S. 159, 169 (1983).

The court below continued its error by shifting its focus to the taxation of the Petitioner's *business*—not the taxable equipment. In response to Petitioner's argument that imposing the entire use tax on equipment in the state for as little as one day violated the external consistency doctrine, the court announced, "while working in South Dakota, Ellingson enjoyed the same benefits as any other person or business present in the state." App. 9a. That Petitioner worked in the state for a longer period of time than the taxable asset was used in the state misunderstands the tax at issue and the application of the external consistency doctrine.

According to the South Dakota Supreme Court, full taxation of equipment is justified because Ellingson "is free to bring the equipment back to work on jobs in South Dakota where Ellingson will continue to enjoy the privilege of conducting its business without being subject to additional use tax." *Id.* Being overtaxed is hardly a *privilege*. And two wrongs—over-apportioning the asset on day one, and under-apportioning it in the future—do not satisfy the external consistency test.

Other states' appellate courts have also misunderstood the need to apportion use taxes on movable property.[5] However, given the absence of clear guidance from this Court, the states have little

[5] *See, supra,* note 1.

incentive to remedy their own revenue-generating constitutional violations.

C. The South Dakota Credit for Sales or Use Taxes Paid to Other States is Not a Substitute for Apportionment.

The availability of a credit for sales or use taxes paid to *other* states cannot cure the failure to apportion South Dakota's use tax. A credit for the amount of tax paid on the purchase of property in a state cannot cure the overtaxation of the property stemming from the failure to divide the tax among those states where the property is used.

CONCLUSION

The South Dakota Supreme Court asserted a false equivalence between sales and use taxes. It compounded this error by misinterpreting this Court's teaching on the external consistency doctrine, misstated one of this Court's precedents, and misunderstood the proper role played by a credit for taxes paid to other states. The South Dakota Supreme Court's holding that the use tax could be applied without regard to the length of time an asset was in South Dakota is unconstitutional and justifies this Court's review.

With the rise in the use of intangible property in interstate commerce, such as the licensing of software, taxpayers and the states need guidance on how the use tax should be applied.

For these reasons, we respectfully request a grant of our petition for a writ of certiorari.

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May 2024