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This Week in State Tax (TWIST)

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South Dakota: High Court Upholds Assessment of Use Tax on Equipment

The South Dakota Supreme Court recently upheld the assessment of use tax on construction equipment purchased out-of-state and brought into South Dakota for use in various projects throughout the three-year audit period. The taxpayer, a Minnesota-based company, did not pay sales tax on the equipment when it was purchased; the Department of Revenue subsequently assessed use tax on the depreciated value of the equipment when brought into South Dakota. The taxpayer objected to the imposition of the tax, arguing that some of the equipment at issue was used in South Dakota for one day only. The taxpayer subsequently filed suit alleging that imposition of the use tax violated the Commerce Clause because the tax was disproportionate to the taxpayer's activity in South Dakota. The taxpayer also made a Due Process Clause argument, but the court noted that the Supreme Court has held that the *Complete Auto* test "encompasses due process standards." In addressing the taxpayer's constitutional challenges under the Commerce Clause, the court applied the four-part test set forth in *Complete Auto*. The taxpayer agreed that two of the prongs of the test were not at issue. The taxpayer had nexus with the state, and the imposition of use tax did not discriminate against interstate commerce. However, the taxpayer asserted that the tax was not fairly related to any benefit it experienced because the equipment was used in South Dakota for a short period only. In other words, the taxpayer asserted it did not receive commensurate value for the tax it paid. The court disagreed, noting that the taxpayer enjoyed the same benefits as any other person or business present in the state. And, having paid the use tax on its equipment that had otherwise not been subject to sales or use tax in another state, the taxpayer was able to bring the equipment back to work on jobs in South Dakota where it would continue to enjoy the privilege of conducting its business without being subject to additional use tax. The taxpayer also made a fair apportionment argument that the imposition use tax offended the external consistency test, which asks whether the state has taxed only the portion of the revenues from the interstate activity that reasonably reflects the in-state component of the activity being taxed. In the taxpayer's view, the use tax was unreasonable because 90 percent of its activities occurred outside the state. The court observed that the taxpayer's concept of external consistency appeared to mean that tax should be applied only when the property has come to rest in South Dakota, with "at rest" meaning that the property is in the state relatively permanently. However, the taxpayer had not identified any authority to support its view of "at rest," and what the court gleaned from other authorities was that tangible personal property is at rest when it is used and is no longer in transit through interstate commerce. The court also observed that the taxpayer's challenge was to the constitutionality of the use tax statute, not whether the statutory text should be applied in a different manner. In conclusion, the court dismissed the taxpayer's constitutional claims. Please contact Nicole Kirk with questions on *Ellingson Drainage, Inc. v. South Dakota Dep't of Rev.*

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