No. __

In the Supreme Court of the United States

DALE W. STEAGER, AS STATE TAX COMMISSIONER OF WEST VIRGINIA,
Petitioner,
v.

CSX TRANSPORTATION, INC.,
Respondent.

ON PETITION FOR WRIT OF CERTIORARI
TO THE SUPREME COURT OF APPEALS
OF WEST VIRGINIA

PETITION FOR WRIT OF CERTIORARI

OFFICE OF THE
ATTORNEY GENERAL
State Capitol
Building 1, Room E-26
Charleston, WV 25305
tjohnson@wvago.gov
(304) 558-2021

PATRICK MORRISEY
Attorney General
ELBERT LIN
Solicitor General
THOMAS M. JOHNSON, JR.
Deputy Solicitor General
Counsel of Record
KATHERINE A. SCHULTZ
Senior Deputy Attorney General
KATLYN M. MILLER
Assistant Attorney General

Counsel for Petitioner

QUESTIONS PRESENTED FOR REVIEW

For 80 years, this Court has "expressly reserved the question" whether, under the dormant commerce clause, "a State must credit a sales tax paid to another State against its own use tax." *Williams v. Vermont*, 472 U.S. 14, 21–22 (1985); see also *Henneford v. Silas Mason Co.*, 300 U.S. 577, 587 (1937). This lack of clarity has led to a split among state courts of last resort about whether a State must credit out-of-state sales taxes against use taxes or whether it can satisfy the dormant commerce clause by other means, such as apportioning a use tax to reach only intrastate activity.

The decision below exacerbates the existing split. West Virginia's use tax on motor fuel is apportioned to tax only mileage traveled in-state *and* provides a credit for sales taxes paid to other States. The Supreme Court of Appeals of West Virginia nonetheless held this tax scheme unconstitutional because it did not also credit sales taxes paid to counties and cities in other States. It so held even though West Virginia forbids its own counties and cities from imposing use taxes on motor fuel, and thus there can be no double taxation on sales taxes paid to other localities. The questions presented are:

(1) Does the dormant commerce clause require a State that imposes a fairly apportioned use tax to also credit sales taxes paid to other States?

(2) Does the dormant commerce clause require a State that does not impose county or municipal use taxes to provide a credit for sales taxes paid to other States' counties or municipalities?

PARTIES TO THE PROCEEDING AND RULE 29.6 STATEMENT

Petitioner here is Dale W. Steager,[1] the Tax Commissioner of the State of West Virginia.

Respondent here and below is CSX Transportation, Inc.

[1] The case below reflects the name of the prior Tax Commissioner of the State of West Virginia, Mark W. Matkovich, who was succeeded by Commissioner Steager in January 2017. See S. Ct. Rule 35.3.

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PETITION FOR A WRIT OF CERTIORARI

Dale W. Steager, West Virginia State Tax Commissioner, respectfully petitions for a writ of certiorari to review the judgment of the Supreme Court of Appeals of West Virginia ("Supreme Court of Appeals") in this case.

OPINIONS BELOW

The decision of the Supreme Court of Appeals is reported at 793 S.E.2d 888 (W. Va. 2016), and is reprinted in the Appendix at App. 1a. The opinion of the Circuit Court of Kanawha County affirming the decision of the West Virginia Office of Tax Appeals is not reported and is reprinted in the Appendix at App. 28a. The decision of the West Virginia Office of Tax Appeals is not reported and is reprinted in the Appendix at App. 50a.

JURISDICTION

This Court has jurisdiction under 28 U.S.C. § 1257. The Supreme Court of Appeals entered judgment on November 16, 2016. On January 25, 2017, the Chief Justice granted Petitioner's application to extend the deadline to file this Petition to April 17, 2017. No. 16A738. This Petition is timely filed within that deadline.

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The Commerce Clause of the United States Constitution provides:

The Congress shall have Power . . . To regulate

> Commerce with foreign Nations, and among the several States, and with the Indian Tribes . . . .

U.S. Const. art. I, § 8, cl. 3.

The West Virginia statutory provisions that authorize the state sales and use tax and credit at issue in this case were quoted in relevant part in the Supreme Court of Appeals' decision and appear in the Appendix at App. 9a–11a & n.6.

STATEMENT

This petition asks this Court to resolve a question that it has reserved in several prior cases dating back eight decades and that has caused at least five state supreme courts to reach conflicting conclusions: Whether the U.S. Constitution requires a State to apply a sales tax credit against its own use tax? The petition further asks that, at minimum, this Court grant review to clarify that, under its case law, no State is required to provide a credit against a tax that the State itself does not assess—here, county and municipal use taxes.

West Virginia assesses a use tax on motor fuel purchased outside the State and transported within the State, but forbids its counties and cities from imposing their own use taxes on motor fuel.[2] States

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[2] Article VI, § 52 of the Constitution of West Virginia requires that all revenues from gasoline and other motor fuel excise and license taxation and all other revenue derived from motor fuels be deposited in the State Road Fund. While municipalities may impose other sales and use taxes as provided in W. Va. Code §§ 8-13C-4 and 5, municipalities are expressly prohibited from

enact such use taxes for two principal reasons. First, use taxes "compensate the taxing State for its incapacity to reach the corresponding sale." *Okla. Tax Comm'n v. Jefferson Lines, Inc.*, 514 U.S. 175, 193 (1995). Second, a use tax functions much as a property tax in that it provides revenue to the State in exchange for the privilege of use and enjoyment of property within the State. *See Silas Mason*, 300 U.S. at 582.

Consistent with these purposes, the dormant commerce clause requires a State to fairly apportion its use tax so as only to reach activity involving the good or service within the State. See *id.* at 183 (quoting *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 270, 279 (1977)). West Virginia's use tax on motor fuel is doubly protective in this regard. First, it uses an apportionment formula that ensures that it only taxes mileage traveled by an interstate carrier within the State. Second, West Virginia provides a credit against its use tax for any sales taxes paid on the same motor fuel to any other State. West Virginia does not, however, provide a credit for out-of-state county and municipal sales taxes, because West Virginia forbids its own localities from imposing use taxes.

Despite these two salutary features, West Virginia's highest court held that this arrangement violated the dormant commerce clause. While the court acknowledged that the State's use tax was fairly apportioned based on mileage, it concluded that the U.S. Constitution requires a credit anyway.

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imposing their sales and use taxes on sale of gasoline and special fuel. W. Va. Code § 8-13C-4(c)(1)(B).

The court further concluded that the State's provision of a credit for sales taxes paid to other States is insufficient, because it excludes sales taxes paid to other States' counties and municipalities.

This decision exacerbates an existing split among state courts of last resort as to whether the dormant commerce clause requires a sales tax credit to offset state use taxes. This Court has never resolved this question, although it has reserved it on multiple prior occasions. This petition presents the Court with an ideal vehicle to resolve the split in authority and clarify that a State that fairly apportions its use tax to reach only intrastate activity need not also provide an offsetting credit.

At minimum, this Court's precedents plainly do not require a State to extend its credit to offset taxes that the State does not itself impose—here, county and municipal use taxes. Under this Court's structural approach to apportionment, known as the "internal consistency" test, West Virginia's system is plainly constitutional. Because West Virginia's counties and municipalities do not charge use taxes, there is no risk of double taxation on sales taxes paid to localities in other States, and hence no conceivable need for an offsetting credit. This petition presents the Court with an opportunity to resolve the conflict between its own cases and the decision below, and make clear that a State does not need to allow credits on taxes that it does not even assess.

I. LEGAL AND FACTUAL BACKGROUND.

A. West Virginia imposes a State sales and use tax on motor fuel. See W. Va. Code §§ 11-15-18b, 11-15A-13a; see also W. Va. Code § 11-14C-5(a). West

Virginia also prohibits its counties and municipalities from imposing their own sales and use taxes on motor fuels. See W. Va. Code §§ 7-22-12(b),[3] 8-13C-4(c)(1)(B), 8-38-12(b), 11-15-9f.

The State calculates its use tax based on the proportion of fuel that an interstate carrier uses when its railroad cars travel through the State. See W. Va. Code §§ 11-14C-5, 11-15A-13a. Through this apportionment formula, the State ensures that motor carriers are only taxed for the mileage that the carrier travels in-state, and not for any usage that occurs in any other State. App. 10a. The formula thus excludes any mileage incurred both in other States that charge a use tax and in States that charge a sales tax based on the carrier's in-state purchase of fuel.

The State also provides a credit to interstate motor carriers against its use tax for sales taxes paid on motor fuel to other States. W. Va. Code §§ 11-15A-10a, 11-15A-13a. Because West Virginia's counties and municipalities cannot impose their own sales and use taxes on motor fuels, the State does not credit any sales taxes paid to other States' counties and cities. W. Va. Code §§ 11-15A-10a, 11-15A-13a; 11-15-9f. And because West Virginia apportions its use tax based on mileage, it provides no credit for

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[3] W. Va. Code §§ 7-22-12 and 8-38-12 allow counties and municipalities, with Legislative approval, to impose a special district excise tax that is the mirror image of the State sales tax. During the period of time that the special district excise tax is in effect, vendors in the district collect from customers the district excise tax rather than the State sales tax. The district excise tax, however, does not apply to sales of motor fuels. W. Va. Code § 11-15-9f.

use taxes paid by an interstate carrier to other states.

B. CSX Transportation, Inc. is an interstate railroad carrier that transports goods throughout the eastern United States. App. 4a. CSX uses motor fuel in West Virginia as it travels through the state by rail. App. 4a.

CSX does not purchase any of its motor fuel in West Virginia. WVSC App. vol. II 1077.[4] Rather, CSX purchases fuel in a number of other States. App. 4a; WVSC App. vol. II 1079, 1094. Some of the States in which CSX purchases fuel impose a sales tax on motor fuel, while others do not. WVSC App. vol. II 1079, 1094. The States in which CSX purchases motor fuel do not apportion their sales taxes or provide any credit for taxes paid for fuel use out-of-state. WVSC App. vol. II 1080.

As an interstate railroad carrier, CSX loads its fuel system-wide, which means that it commingles its purchased fuel from each of these locations and does not segregate fuel based on where it was purchased or where it will be used. WVSC App. vol. II 1077, 1093–94. This fuel commingling system makes it impossible to trace the origin of purchase and place of use of fuel actually used in West Virginia. WVSC App. vol. II 1077, 1093–94. In addition, CSX does not track how much fuel it uses in West Virginia or any other State. WVSC App. vol. II 1118.

Accordingly, CSX does not dispute that it must

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[4] Citations to the "WVSC App." refer to the appendix filed with the Supreme Court of Appeals.

use an apportionment formula to determine how much fuel it uses in West Virginia. WVSC App. vol. II 1077, 1118. CSX does not contest that the West Virginia Code provides an appropriate formula to determine the amount of fuel that CSX uses in-state. See App. 6a, 32a.

II. PROCEDURAL HISTORY PRIOR TO THE SUPREME COURT OF APPEALS.

In 2010, the Tax Commissioner conducted a field audit of CSX's rail yards, which revealed that CSX imports fuel that it uses in West Virginia. App. 4a. As a result, CSX was directed to start paying the State use tax on that fuel. App. 4a.

CSX commenced paying the tax and claiming a credit for sales taxes paid to other States, but in 2011, it reviewed its calculations and realized it had never sought a credit for sales taxes paid to other State's counties, cities, or other localities. App. 30a; WVSC App. vol. II 1081. CSX therefore filed amended use tax returns seeking a refund in the amount of local taxes paid in the States of Alabama and Georgia for prior tax periods. App. 30a. The Tax Commissioner denied the refund request. App. 30a–31a.[5]

CSX then filed a petition for refund with the

[5] In the course of reviewing CSX's refund request, the Tax Commissioner concluded that CSX had been improperly calculating its sales tax refund in prior periods, which led to the Commissioner issuing a notice of assessment against CSX and changing its refund methodology. App. 5a. CSX contests this revised calculation. App. 5a. In the interests of judicial economy, OTA has stayed resolution of this calculation issue pending final judgment in this case.

Office of Tax Appeals ("OTA"), challenging the denial of its refund request. App. 5a, 31a. On January 23, 2015, the OTA granted CSX's refund request, on the basis that the dormant commerce clause entitled CSX to a credit for sales taxes paid on motor fuel purchased from counties, cities, and municipalities in other States. App. 5a, 31a–32a.

The Tax Commissioner appealed this determination to the Circuit Court of Kanawha County. App. 6a, 48a–49a. On August 24, 2015, the circuit court affirmed OTA's decision, agreeing that the Tax Commissioner's denial of a credit for sales taxes paid to other States' localities violated the dormant commerce clause. App. 6a, 32a.

Despite this Court's express reservation of the issue on multiple prior occasions, the circuit court held that "for over twenty years, since [this] Court's decision in *Oklahoma Tax Comm'n v. Jefferson Lines, Inc.*, 514 U.S. 175 (1995), it has been clear that a state is constitutionally required to provide a credit against its own use tax for sales or use taxes paid to other jurisdictions." App. 37a. And, relying on one out-of-state case from Colorado, the court concluded that "taxes imposed by a sub-state taxing jurisdiction are imputed to the state," and therefore, West Virginia was constitutionally obligated to provide a credit for sales taxes paid *both* to other States *and* their localities. App. 38a & n.17.

The court acknowledged the Tax Commissioner's argument that, when applying this Court's internal consistency test for determining whether taxes are fairly apportioned, a court should take into account the fact that West Virginia does not itself impose

county or local use taxes. App. 46a. But the court held it was not required to consider that feature of West Virginia's tax system, because "the use tax provision itself is not the offending provision; rather, it is the calculation of the use tax credit without a credit for local sales taxes paid that produces the resulting discriminatory effect on interstate commerce." App. 46a.

III. PROCEEDINGS BEFORE THE SUPREME COURT OF APPEALS.

The Tax Commissioner appealed to the Supreme Court of Appeals, raising two principal arguments. First, the Commissioner argued that the West Virginia use tax was fairly apportioned under this Court's internal consistency test, because West Virginia provides an offsetting credit for other State's sales taxes and forbids its own counties and municipalities from charging sales and use taxes on motor fuels. See Comm'r Sup. Ct. of App. Br. 8–14. Second, the Commissioner argued that in any event the circuit court erred in holding that sales tax credits are constitutionally required. See *id.* at 19–23. In support, the Commissioner noted "the possibility that States, like West Virginia, who have apportioned use taxes, can satisfy the internal consistency required without providing credits for sales taxes imposed by other States." *Id.* at 22.

The Supreme Court of Appeals affirmed. App. 3a. The court held that the dormant commerce clause required the Tax Commissioner to provide a sales tax credit "*both* to sales taxes paid to other states *and* to sales taxes paid to the municipalities of other states." App. 3a.

In reaching that conclusion, the court applied this Court's four-part test for evaluating the constitutionality of a state taxing scheme under the dormant commerce clause, known as the *Complete Auto* test. See *id.* at 13a (citing *Complete Auto*, 430 U.S. at 279). Under that test, a state taxing scheme is constitutional if it (1) has a substantial nexus with the State, (2) is fairly apportioned, (3) does not discriminate, and (4) is fairly related to the services provided by the State. See *Complete Auto*, 430 U.S. at 279.

The court concluded that the state use tax and offsetting credit both met the first and fourth requirements of the *Complete Auto* test. App. 14a–15a, 26a–27a. The court further concluded that the use tax itself was "fairly apportioned," as it "directly correlates to the fuel that [a carrier] uses for the miles it travels within West Virginia." App. 17a. The court also deemed the use tax non-discriminatory, as it is "properly constructed so as to tax only the motor fuel that a motor carrier actually uses within the boundaries of this State." App. 25a.

But the court proceeded to consider the sales tax credit in isolation from the use tax itself, and held that the credit standing alone did not satisfy the second and third *Complete Auto* factors—fair apportionment and non-discrimination—because it only provided an offset for other States' sales taxes, and not for out-of-state county or municipal sales taxes. App. 15a–25a.

Under both *Complete Auto* factors, the court's analysis was essentially the same: It concluded that the Tax Commissioner's failure to provide a credit for

out-of-state county and municipal taxes violated this Court's "internal consistency" test for evaluating the structure of state tax schemes. App. 24a–25a (citing *Comptroller of the Treasury of Maryland v. Wynne*, 135 S. Ct. 1787, 1805 (2015)). The court thus held, in effect, that credits are constitutionally required even where, as here, West Virginia fairly apportions its use tax to reach only intrastate activity. See App. 24a–25a.

In describing the internal consistency test, the court correctly observed that "[t]his test asks nothing about the degree of economic reality reflected by the tax, but simply looks to the structure of the tax at issue to see whether its identical application by every State in the Union would place interstate commerce at a disadvantage as compared with commerce intrastate." App. 15a–16a (quoting *Jefferson Lines*, 514 U.S. at 185). But the court nevertheless proceeded to apply an "economic reality" test that this Court in *Wynne* and prior cases expressly rejected. That is, the court examined possible tax structures that might be adopted by a hypothetical "State A" and "City of Metropolis," and then concluded that a taxpayer doing business in those fictional jurisdictions would have a higher total tax burden on an interstate transaction than an intrastate transaction. See App. 22a–24a.

Having applied an "economic reality" test to conclude that West Virginia's sales tax credit in isolation was discriminatory and not fairly apportioned, the court was "left with the definite and firm conclusion" that the dormant commerce clause required West Virginia to provide a credit for taxes paid both to other States and to other States'

subdivisions. App. 27a.

REASONS FOR GRANTING THE PETITION

This petition presents two important questions that merit this Court's review concerning the proper application of the dormant commerce clause to state sales and use tax schemes.

First, this Court should grant certiorari to resolve a split in authority among state courts of last resort as to whether the dormant commerce clause requires a State assessing a use tax to provide a credit for out-of-state sales taxes. This Court has repeatedly reserved that same question in prior cases. As a result, state courts have reached different conclusions on how to resolve this question, with courts in Kentucky and Wyoming holding that credits are not required and courts in Arizona and Colorado holding that credits are required. The decision below exacerbates the existing split.

This Court should intervene to clarify that credits are not constitutionally mandated in all cases. Where, as here, a State uses a formula to apportion its use tax so that it only reaches intrastate activity, this Court should conclude that the State taxes a distinct downstream event and does not need to provide a credit for prior taxable events, such as the initial sale. To the extent that statements in this Court's prior cases suggest otherwise, this Court should treat them as dicta or expressly overrule them. Certiorari is required to prevent further confusion among the lower courts on this important question, which affects the ability of the States to raise revenue by assessing apportioned taxes on intrastate activity.

Second, even if this Court wishes to continue to reserve the broader question, it should at minimum grant review to clarify that, under this Court's precedent, a State does not need to provide a credit against taxes that the State does not itself assess—here, county and municipal use taxes. West Virginia's use tax scheme exceeds the constitutional minimum because it is both fairly apportioned by formula and because it provides a credit for sales taxes paid to other States. But the Supreme Court of Appeals held that the credit provision, in isolation, was still deficient because it failed to credit sales taxes paid to other States' counties and cities.

This holding conflicts with multiple decisions of this Court. For example, it disregards this Court's instruction to consider the State's "tax scheme as a whole" to determine whether it places an unfair burden on interstate commerce. *Wynne*, 135 S. Ct. at 1803 n.8. Instead, the Supreme Court of Appeals considered the allegedly offending provision in isolation—the credit—and concluded that it did not sufficiently compensate taxpayers for sales taxes paid to other counties and municipalities. But by focusing solely on the alleged disease, the court turned a blind eye to the cure that West Virginia's tax scheme provides: Taxpayers cannot be exposed to double taxation on local sales taxes assessed in other States because West Virginia's own localities cannot charge use taxes on motor fuel.

Rather than conclude that West Virginia's tax structure was internally consistent, as this Court's cases require, the court also proceeded to apply an "economic reality" test by asking whether interstate taxpayers would be worse off paying hypothetical

taxes to a fictional State A and its City of Metropolis. Because this approach would make the legality of a State's use tax scheme turn on the provisions of innumerable other state and local tax codes, this Court has rightly rejected it and should do so again here.

In short, this Court should also grant certiorari to resolve the conflict between its own cases and the decision below and hold that the U.S. Constitution does not mandate that a State provide a credit against county and municipal taxes that the State itself does not impose.[6]

I. THE DECISION BELOW EXACERBATES AN EXISTING SPLIT ON A QUESTION THIS COURT HAS REPEATEDLY RESERVED, NAMELY, WHETHER THE U.S. CONSTITUTION REQUIRES STATES IMPOSING A USE TAX TO PROVIDE A CREDIT FOR OUT-OF-STATE SALES TAXES.

The decision below deepens an existing split among state courts of last resort over whether the U.S. Constitution requires States to provide credits

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[6] In *Wynne*, this Court called for the views of the Solicitor General in response to Maryland's petition for certiorari, and the United States filed a brief supporting certiorari and arguing that Maryland's tax structure was constitutional. See *Wynne*, 134 S. Ct. 982 (Jan. 13, 2014); Brief for the United States as Amicus Curiae, *Comptroller of the Treasury of Md. v. Wynne*, 135 S. Ct. 1787, No. 13-485, 2014 WL 1348934, at *1, *7–18 (U.S. Apr. 4, 2014); see also *Wynne*, 135 S. Ct. at 1797, 1804–05. West Virginia respectfully suggests that it may be appropriate here too to seek the views of the United States on the unique but related questions posed by this petition.

against their use taxes for sales taxes paid to other States. This Court should grant certiorari to resolve that split and to clarify that where a State like West Virginia fairly apportions its use tax to reach only activity within the State's borders, no offsetting credit is required.

A. This Court has repeatedly reserved the question of whether sales tax credits are constitutionally mandated. But the reasoning in its past cases suggests that credits are not the only means by which States may apportion their use taxes. As Justice Cardozo put it, this Court has been careful "not . . . to imply" that it was "mandatory" to provide an "allowance for taxes paid to other states," because "[a] state, for many purposes, is to be reckoned as a self-contained unit, which may frame its own system of burdens and exemptions without heeding systems elsewhere." *Silas Mason*, 300 U.S. at 587; see also *Williams*, 472 U.S. at 21–22; *Southern Pac. Co. v Gallagher*, 306 U.S. 167, 172 (1939).

While this Court has suggested that one way a State may avoid any potential constitutional infirmity in a use tax is by providing a credit for out-of-state sales taxes on the same goods or services, it has never held that a credit is the *only* means by which a State may render a use tax constitutional.[7] To the contrary, this Court has suggested that apportionment formulas, where feasible, can serve as an alternative to credits.

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[7] See, *e.g.*, *Jefferson Lines.*, 514 U.S. at 193–95; *DH Holmes Co. Ltd. v. McNamara*, 486 U.S. 24, 31 (1988); *Goldberg v. Sweet*, 488 U.S. 252, 264 (1989).

In *Goldberg v. Sweet*, 488 U.S. 252 (1989), for example, this Court noted that it had previously "endorsed apportionment formulas based upon the miles a bus, train or truck traveled within the taxing State." *Id.* at 264 & n.14 (collecting authorities). But the Court also noted that there are cases where an apportionment formula "based on mileage or some other geographic division . . . would produce insurmountable administrative and technological barriers," such as taxes on interstate telephone calls. See *id.* at 264–65. In such cases, a State may avoid the risk of taxing more than its fair share of a transaction through a credit provision. See *id.* at 265.

The conclusion that sales tax credits are not required for use taxes apportioned by mileage respects the multiple purposes served by use taxes. On one hand, use taxes provide compensation to States for the lost opportunity to collect tax on the underlying sale. See *supra* pp. 2–3. But use taxes also compensate States for providing protection to property that enters into and travels through the State. See John E. Nowak and Ronald D. Rotunda, *Sales & Use Tax Credits, Discrimination Against Interstate Commerce, and the Useless Multiple Tax Concept*, 20 U.C. DAVIS L. REV. 273, 278 (1987) ["Nowak & Rotunda"]; *Silas Mason*, 300 U.S. at 582. An apportioned use tax should therefore be considered a tax on a distinct downstream event that is "internally consistent," and satisfies dormant commerce clause scrutiny, regardless of whether the State also provides a sales tax credit. See Nowak & Rotunda at 282, 299-300. This conclusion would be consistent with the general principle that "the Commerce Clause does not forbid the actual

assessment of a succession of taxes by different States on distinct events as the same tangible object flows along." *Jefferson Lines*, 514 U.S. at 187–88.

That said, some courts have mistakenly read dicta in this Court's decision in *Jefferson Lines* as concluding that sales tax credits are constitutionally mandated. In *Jefferson Lines*, this Court held that a state sales tax on the entire price of bus tickets was properly apportioned even though it did not account for the bus's subsequent travel out-of-state. 514 U.S. at 188–91. In so holding, the Court "posited for the sake of argument" that downstream use tax jurisdictions would provide credits that would prevent the possibility of double taxation. See *id.* at 195. But the court did not hold that credits are the only way that a use tax State could comply with the dormant commerce clause.

This Court's various statements on use taxes have nonetheless caused confusion among state courts of last resort that this Court should intervene to resolve. In his treatise on State Taxation, Professor Hellerstein catalogues this split in authority, noting that state supreme courts in Wyoming and Kentucky have both held that credits are not constitutionally required, while courts in Colorado and Arizona have held that they are.[8] The

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[8] See 1 Hellerstein & Hellerstein, *State Taxation*, ¶ 18.09[2][a] & n.663, 2015 WL 1646564, at *3–4 (3d ed. 2000-15). While Professor Hellerstein believes that credits are constitutionally required, he notes that this Court has avoided so holding; he instead derives his conclusion from this Court's adoption of the "internal consistency" test and its "strong statements" in *Jefferson Lines*. *Id.* at *2–3. As explained above, this conclusion

decision by West Virginia's highest court—which cited both the Colorado and Arizona decisions as persuasive authority—deepens the existing split and merits this Court's review.

B. On one hand, at least two state courts of last resort have held that credits are not always required under the dormant commerce clause.

First, the Kentucky Supreme Court has upheld against constitutional challenge a state special use tax on construction equipment, even though the State provided no credit for out-of-state sales taxes. See *Genex/London, Inc. v. Ky. Bd. of Tax Appeals*, 622 S.W.2d 499, 502, 504 (Ky. 1981).[9] Like West Virginia's tax, the Kentucky use tax was assessed using an apportionment formula, which was computed "on the basis of such proportion of the original purchase price of such property as the duration of time of use in this state bears to the total useful life." *Id.* at 502.

In upholding the tax, the state supreme court relied in part on Justice Cardozo's observations in *Henneford v. Silas Mason Co.* that use taxes do not burden interstate commerce so long as they are assessed only after the property enters the State, at which point, "'the stranger from afar is subject to no greater burdens as a consequence of ownership then

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does not follow as a matter of course from this Court's prior precedents.

[9] The Kentucky Board of Tax Appeals (now the Kentucky Claims Commission) reaffirmed the reasoning in this case in 2012. See *Miller Pipeline Corporation v. Dep't of Rev., Fin., & Admin. Cabinet, Comm. of Ky.*, K-21900, 2012 WL 1071408, at *1 (Ky. Bd. Tax App. Mar. 22, 2012).

the dweller within the gates.'" *Genex/London*, 622 S.W.2d. at 504 (quoting *Silas Mason*, 300 U.S. at 584) (internal citation omitted). The court concluded that the Kentucky use tax scheme was constitutional because it was enacted for a legitimate public purpose and was "levied after the property comes to rest in Kentucky." *Ibid.*

Similarly, the Supreme Court of Wyoming affirmed its State's decision not to grant a credit against its use tax to Exxon Corporation for taxes paid to the State of Colorado on a pipe that was refined in Colorado and ultimately shipped to and installed in Wyoming. See *Exxon Corp. v. Wyoming State Bd. of Equalization*, 783 P.2d 685, 685 (Wyo. 1989). In the course of that decision, the Court rejected an argument that the dormant commerce clause required the offsetting credit. *Id.* at 689. The Court reasoned that "the Constitution does not prohibit uniform nondiscriminatory taxes on property merely because that property was subject to tax elsewhere." *Ibid.* (citing Nowak & Rotunda, at 300).

The court reasoned that the Wyoming tax was fairly apportioned simply because "it taxes only the use of the pipe in Wyoming." See *ibid*. The decision drew a dissent that argued at length that the majority should have afforded a credit for taxes paid to Colorado. See *id.* at 694–97 (Urbigkit, J., dissenting).[10]

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[10] Similarly, in *Barringer v. Griffes*, 1 F.3d 1331 (2d Cir. 1993), the Second Circuit noted that this Court "has stopped short of declaring that credits are constitutionally required for all use taxes," and thus also "decline[d] to hold that a credit is

The decisions reached by the state supreme courts in Wyoming and Kentucky cannot be squared with the decision below, which deemed a credit constitutionally required for sales taxes paid to other States.

B. On the other hand, at least two other state courts of last resort have required States to provide a sales tax credit to offset use taxes, whether those sales taxes were paid to States or their localities.

For example, in *Arizona Department of Revenue v. Arizona Public Service Co.*, 934 P.2d 796 (Ariz. Ct. App. 1997), the Arizona Court of Appeals considered whether the State's statute affording a tax credit for sales taxes "imposed . . . under the laws of another state of the United States," applied only to taxes paid to other States or also to counties of other States. *Id.* at 799 (quoting Ariz. Rev. Stat. § 42-1409(A)(2)). The Court concluded that, to avoid constitutional infirmity, the State must credit *both* sales taxes paid to other States *and* taxes paid to those States' localities. See *ibid.* While this Court has held that courts should not inquire into the economic reality of a transaction, see *supra* p.11, the Arizona Supreme Court improperly concluded that "[t]he taxpayer's out-of-pocket expenses determine whether the burdens [imposed on interstate and intrastate commerce] are equal." *Ariz. Dep't of Revenue*, 934 P.2d at 799.

Similarly, in *General Motors Corp. v. City and*

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constitutionally mandated in the instant case." *Id.* at 1337. While the court held that Vermont's use tax on automobiles was not fairly apportioned in that case, it left the choice of remedy to the State Legislature, rather than mandate a credit. See *ibid.*

County of Denver, 990 P.2d 59 (Colo. 1999) (en banc), the Colorado Supreme Court examined a use tax on automobiles imposed by the City and County of Denver that provided a sales tax credit for taxes paid to other municipalities, but not to other States. The Court held that "[i]nternal consistency requires that states impose identical taxes when viewed in the aggregate—as a collection of state and sub-state taxing jurisdictions." *Id.* at 69. Again improperly applying an economic reality test, the Colorado Supreme Court reached its conclusion by stating that "the interstate taxpayer should never pay more sales or use tax than the intrastate taxpayer." *Ibid.*

While the Colorado court ultimately required a credit, one aspect of its reasoning highlights the uncertainty regarding whether credits against use taxes are constitutionally required. The court correctly recognized that "[t]o avoid multiple taxation, a tax upon interstate commerce must either be apportioned to relate the tax to the activity taking place within the taxing state *or* it must allow a credit for other similar taxes paid by the taxpayer in other jurisdictions." *Ibid.* (emphasis added) (citing *Goldberg*, 488 U.S. at 264). The court described both options as "equally suitable" to satisfy the apportionment requirement. *Ibid.*

The court noted, however, that most States opt not to shoulder "the burdens of administering fractional apportionment mechanisms," but instead choose to provide a credit. *Ibid*. The City of Denver, for example, made no effort to apportion its vehicle tax, but instead imposed a tax on the full value of the vehicles' parts once a car entered the City even though some cars spent less than 1% of their useful

lives in Denver. See *id.* at 64. By contrast, West Virginia apportions its use tax so as to isolate and tax only that activity that occurs within the State.

The case thus begs the question whether a State like West Virginia that apportions its use tax by formula also needs to provide a credit for out-of-state sales taxes. This Court should grant certiorari to resolve the split and hold that sales tax credits are not constitutionally mandated.

II. BY CONCLUDING THAT A STATE MUST PROVIDE CREDITS AGAINST COUNTY AND MUNICIPAL TAXES THAT THE STATE DOES NOT ITSELF IMPOSE, THE DECISION BELOW CONFLICTS WITH NUMEROUS DECISIONS OF THIS COURT.

Even if this Court wishes to continue to reserve the question whether sales tax credits are constitutionally required, certiorari would still be warranted because the decision below conflicts with numerous decisions of this Court concerning the appropriate test to apply to determine whether a tax is fairly "apportioned" under the dormant commerce clause. Specifically, the court below failed to adhere to this Court's "internal consistency" test, and instead applied its own test in which it analyzed the allegedly offending provision of West Virginia's use tax scheme in isolation and asked whether its application might lead to a higher interstate burden in other hypothetical jurisdictions. Accordingly, the court reached the unsupportable conclusion that West Virginia needed to provide credits for out-of-state county and municipal taxes that West Virginia's own localities do not impose.

The purpose of the apportionment requirement is to ensure that no State taxes more than its "fair share" of a taxable event or series of events. *Goldberg*, 488 U.S. at 260–61 (citing *Container Corp. of Am. v. Franchise Tax Bd.*, 463 U.S. 159, 169 (1983); see also *Jefferson Lines*, 514 U.S. at 185. If done properly, apportionment ensures that the State identifies and taxes only that activity that takes place within the taxing State. See, *e.g.*, *Jefferson Lines*, 514 U.S. at 184–85; *Goldberg*, 488 U.S. at 263. States have flexibility in deciding how to apportion and this Court has "never required that any particular apportionment formula or method be used." *Jefferson Lines*, 514 U.S. at 195.

Apportionment helps reduce the risk that a taxpayer is exposed to "double taxation," because properly-apportioned taxes exclude out-of-state activity from the tax base. See, *e.g.*, *Wynne*, 135 U.S. at 1794–95; *Jefferson Lines*, 514 U.S. at 184; *Goldberg*, 488 U.S. at 261. But the U.S. Constitution does not guarantee that taxpayers will bear exactly the same tax burden on an interstate transaction as an intrastate transaction. See *Wynne*, 135 S. Ct. 1805. States, for example, are entirely free to adopt their own tax rates, which could lead to a reduced tax burden on a purely intrastate transaction in a more tax-friendly jurisdiction. See, *e.g.*, *Goldberg*, 488 U.S. at 261.

This Court has thus focused its apportionment inquiry on whether a State's tax structure inherently burdens interstate commerce. See *Jefferson Lines*, 514 U.S. at 185. If a State's tax structure itself suggests that the State has taxed more than its "fair share" of a transaction, then the structure is

unconstitutional. *Ibid.* If instead any differential tax burden is merely the incidental result of variations in the tax schemes of 50 different state jurisdictions (or a multiplicity of local jurisdictions), there is no dormant commerce clause violation. *See Goldberg*, 488 U.S. at 261.

To aid courts in determining whether a State tax is fairly apportioned, this Court has applied what has become known as the "internal consistency" test. See *Jefferson Lines*, 514 U.S. at 185; *Wynne*, 135 S. Ct. at 1801–03. The internal consistency test "looks to the structure of the tax at issue to see whether its identical application by every State in the Union would place interstate commerce at a disadvantage as compared with commerce intrastate." *Wynne*, 135 S. Ct. at 1802 (quoting *Jefferson Lines*, 514 U.S. at 185).

In applying this test, courts must assume that every other State has adopted the "tax scheme as a whole," as opposed to specific taxes or components in isolation. *Wynne*, 135 S. Ct. at 1803 n.8. This ensures that the court considers the substance of the entire tax scheme holistically in determining whether it is fairly apportioned, as opposed to labels that States might affix to particular taxes. See *ibid.*

Importantly, the internal consistency test "asks nothing about the degree of economic reality reflected by the tax[.]" *Id.* at 1805. That is, courts must not examine the actual tax regimes of the other 49 States to discern whether *in fact* a taxpayer could be charged more if the taxable event implicated more than one jurisdiction. See, *e.g.*, *Goldberg*, 488 U.S. at 261; *Armco v. Hardesty,* 467 U.S. 638, 645 (1984).

Rather, courts must restrict their inquiry to the structure of the tax at issue and ask, "What would happen if all States [imposed] the same [tax structure]?" *Am. Trucking Ass'ns, Inc. v. Mich. Pub. Serv. Comm'n*, 545 U.S. 429, 437 (2005).

The decision below conflicts with these well-established principles in at least two ways that merit this Court's review.

A. The Decision Below Improperly Examined The Allegedly Offending Provision In Isolation, Rather Than The Tax Scheme As A Whole.

First, the decision below reached its conclusion that West Virginia must provide credits for other States' county and municipal sales taxes by analyzing the State's sales tax credit in isolation, rather than considering it in the context of the "tax scheme as a whole." *Wynne*, 135 S. Ct. at 1803 n.8.

Had the Supreme Court of Appeals applied West Virginia's entire tax structure to every other State in the Union, it would plainly be internally consistent. Each State would impose a use tax and have a corresponding credit for any sales taxes paid to other States. In addition, no State would impose county or city use taxes, and accordingly, no county or city sales credits would be required or necessary. Not only is this tax structure fairly apportioned, but it eliminates any potential for double taxation on local taxes.

Instead, the Supreme Court of Appeals assumed *only* that West Virginia's sales tax credit applied to every State, but not the key prohibition on

imposition of local taxes. In so doing, the court essentially adopted the test advanced by the circuit court, namely, that a court need only analyze the structure of the allegedly "offending provision" in isolation. App. 46a.

There is no basis in this Court's case law for this "offending provision" test; to the contrary, it conflicts with this Court's instruction in *Wynne* to consider the tax scheme as a whole. Moreover, as a practical matter, the "offending provision" test cannot be correct because it would compel courts in every case to analyze the alleged disease without also inquiring into whether the State had elsewhere provided a cure. As a result, it would become a self-fulfilling prophecy that States must provide an offsetting credit in every case, even in instances where the State had redressed the alleged problem through an alternate mechanism elsewhere in its taxing scheme—here, by eliminating county and municipal taxes. As explained above, the dormant commerce clause does not "box" States in to any specific method of apportionment. The court below, however, did just that.

B. The Decision Below Improperly Applied An Economic Reality Test Rather Than A Structural Test.

Second, and related, the decision below improperly filled the void left by its refusal to assume that all 50 States, like West Virginia, prohibited county and municipal sales taxes, by imagining hypothetical tax schemes enacted by a fictional State A and its City of Metropolis, and then analyzing whether a taxpayer might be worse off

engaging in an interstate transaction involving these fictional jurisdictions than a purely intrastate transaction in West Virginia. The court thus applied an "economic reality" test that this Court has repeatedly rejected and that would make the constitutionality of state use taxes turn on the vagaries of countless potential State, county, and municipal tax schemes.

This table illustrates the assumptions the court made in comparing West Virginia's tax scheme to hypothetical tax schemes in State A and its City of Metropolis:

WV Tax (owed)	**State A Tax (credited)**	Metropolis Tax (owed)	Total Tax Burden
5%	**N/A**	N/A	5%
5%	**5%**	0%	5%
5%	**3%**	2%	7%

App. 22a–23a.

In this table, the first row for reference represents a purely intrastate transaction, in which a taxpayer pays 5% in West Virginia sales tax but pays no taxes and receives no credits for any commerce out of state. The second row represents an interstate transaction involving a hypothetical State A that also happens to impose a 5% state sales tax, but no county or municipal taxes. In that scenario, the taxpayer also pays 5% tax because it receives a

full credit for taxes paid to State A. The third row represents an interstate transaction involving a hypothetical State A that imposes a 3% state sales tax, and a fictional City of Metropolis that imposes a 2% sales tax. Here, the taxpayer receives partial credit for the 3% tax paid to State A, but no credit for the 2% paid to Metropolis, resulting in a total tax burden of 7% (2% paid to West Virginia after the credit, 3% to State A, and 2% to Metropolis). The court concluded that this third possibility rendered West Virginia's tax scheme unconstitutional. App. 24a.

In other words, to reach its conclusion that West Virginia's tax scheme was impermissible, the court adjusted the "economic reality" that might face a taxpayer in different States and showed how that would result in a different "total tax burden" depending on the law that existed in various jurisdictions throughout the nation. See *id.* at 23a–24a. But that is precisely the inquiry that this Court's cases instruct courts *not* to conduct, because it would make the legality of each State's law dependent on the law in 49 other States (and here, countless counties and municipalities). *Goldberg*, 488 U.S. at 261; *Armco*, 467 U.S. at 645.

Had the court adopted and applied the "structural" test prescribed in *Wynne*, the resulting table would look like this:

WV Tax (owed)	**49 Other States (credited)**	City/County Taxes (owed)	Total Tax Burden
5%	**N/A**	N/A	5%
5%	**5%**	N/A	5%

The first row again represents an intrastate transaction, resulting in a 5% total tax burden. The second row represents an interstate transaction and assumes that each State in the nation has West Virginia's tax scheme, that is, imposes a 5% state tax and no county or municipal taxes. Because the taxpayer receives a full credit for the out-of-state tax, its tax burden is also 5%. Applying the "structural" test, interstate and intrastate transactions would be taxed the same. That is, the tax would be fairly apportioned and there would be no risk of double taxation.

Certiorari is warranted to resolve the conflict between this Court's cases and the improper test applied in the decision below.

III. THIS CASE PRESENTS AN IDEAL VEHICLE TO RESOLVE ANY POINTS OF LAW THAT MAY HAVE BEEN LEFT OPEN BY THIS COURT'S DECISION IN *WYNNE*.

The Supreme Court of Appeals' decision was based in part on its misreading of this Court's most recent case applying the "internal consistency" test—*Comptroller of the Treasury of Maryland v. Wynne*, 135 S. Ct. 1787 (2015). This case thus also presents

an ideal vehicle for this Court to clarify several points that were not directly at issue in *Wynne* and provide further guidance to the lower courts on the appropriate legal standard for evaluating whether taxes are fairly apportioned under the dormant commerce clause.

In *Wynne*, this Court reviewed the constitutionality of a Maryland income tax scheme with the following components: (1) a "State" tax on income that residents earned in-state; and (2) a "county" tax that applied to (a) income that residents earned in-state, (b) income that residents earned out-of-state and (c) income that nonresidents earned in-state. 135 S. Ct. at 1792. (For nonresidents, this "county" tax was called a "special nonresident tax." *Ibid.*) Maryland provided a credit for taxes paid out-of-state against the "State" income tax but not the "county" tax. See *ibid.*

This Court, applying the internal consistency test, properly assumed that each State had adopted Maryland's entire tax scheme. See *id.* at 1803–04. Given that scenario, the Court concluded that the "county" tax was not fairly apportioned because residents who earned all their income in-state would be taxed only once—2(a) above—but residents who worked out-of-state would be taxed twice—paying tax 2(b) to Maryland and tax 2(c) to the other State. See *ibid.* Unlike the decision below, in conducting this analysis, the Court did not imagine different taxes applied by other jurisdictions; it simply applied the Maryland system across the board.

Also, the Court did not mandate any specific way for the State to "remedy the infirmity in [the] tax

scheme" in that case. 135 S. Ct. at 1805–06. While the Court noted that Maryland "could cure the problem with its current system by granting a credit for taxes paid to other States, [it did] not foreclose the possibility that it could comply with the Commerce Clause in some other way." *Ibid.*

This case thus provides an opportunity for this Court to clarify that, at minimum, States always have one simple and elegant option for curing any perceived dormant commerce clause violation—namely, eliminating or prohibiting the allegedly offending tax.

Both the majority and the dissent in *Wynne* appeared to agree that, under the Court's analysis, Maryland could "remedy the unconstitutionality of its tax scheme by eliminating the special nonresident tax." *Ibid.*; see also *id.* at 1822 (Scalia, J., dissenting) ("Maryland could eliminate the inconsistency [with its tax scheme] by terminating the special nonresident tax"). Indeed, the Court described it as a "truism" that in every dormant commerce clause case, "[w]henever government impermissibly treats like cases differently, it can cure the violation by either 'leveling up' or 'leveling down.'" *Id.* at 1806.

Here, West Virginia has effectively avoided a potential constitutional problem by "leveling down" its tax structure and forgoing certain potential sources of revenue—namely, county and municipal sales and use taxes. Yet, the Supreme Court of Appeals *still* concluded that the State needed to provide a credit for these same taxes paid to other States' subdivisions.

The analogy would be if Maryland, in the wake of the *Wynne* decision, decided to take up this Court's suggestion and cure the constitutional violation by repealing its "county" tax entirely, only to learn that it still needed to continue providing credits for similar taxes imposed by other States. That result would plainly be inconsistent with both the majority and the dissenting opinions in *Wynne*. This Court should grant certiorari to clarify that a State does not need to provide credits against county and municipal taxes that the State does not itself impose.

Relatedly, this case presents an opportunity for the Court to reject the unsupported premise adopted by some courts that, for purposes of internal consistency, state taxes must be "viewed in the aggregate—as a collection of state and sub-state taxing jurisdictions," *General Motors Corp.*, 990 P.2d at 69; see also *Ariz. Dep't of Revenue*, 934 P.2d at 799; and that "taxes imposed by a sub-state taxing jurisdiction are imputed to the state," App. 38a.

This Court has never held that all state and local taxes are always and everywhere interchangeable. To the contrary, this Court has treated localities as juridical entities separate from their States in a variety of contexts. For example, federal funds granted to localities are theirs alone to collect and use; the separate State entity cannot compel ownership of these funds.[11] Local governments can be sued in their own name,[12] and are independently

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[11] See *Lawrence Cnty. v. Lead-Deadwood Sch. Dist. No. 40-1*, 469 U.S. 256, 258 (1985).

[12] See *Monell v. Dep't of Soc. Servs.*, 436 U.S. 658, 691 n.54 (1978).

liable for resulting judgments.[13] Local governments also have independent duties to adhere to the Voting Rights Act[14] and school desegregation requirements.[15] And local ordinances are not "state action" for purposes of the Sherman Act.[16] Given this distinct treatment throughout numerous areas of law, there is no reason why, in the dormant commerce clause context, localities and States should be treated as indistinguishable. This Court should grant certiorari to make that clear.

IV. THE QUESTIONS PRESENTED ARE OF GREAT PUBLIC IMPORTANCE.

Finally, this Court should grant certiorari because this case presents significant questions of public importance for at least three reasons.

First, this Court's clarification of whether, and in what circumstances, States are obligated to provide a sales tax credit for taxes paid out-of-state will provide much-needed guidance to all 50 States. If this Court does not intervene, taxpayers in other jurisdictions will undoubtedly rely on the Supreme Court of Appeals' decision to demand credits not otherwise permitted under state law. This will only deepen the existing split over whether, and to what extent, sales tax credits are constitutionally required.

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[13] See *Louisiana ex rel. Folsom v. Mayor of New Orleans*, 109 U.S. 285, 288 (1883).

[14] See *Avery v. Midland Cnty., Tex.*, 390 U.S. 474, 480 (1968).

[15] See *Milliken v. Bradley*, 418 U.S. 717, 744–45 (1974).

[16] See *Cmty. Commc'ns Co. v. City of Boulder*, 455 U.S. 40, 53 (1982).

Indeed, faced with the present uncertainty, many States will likely simply default to providing a credit whenever it is unclear that one is required. Indeed, "the vast majority of American jurisdictions" presently provide a credit at least against sales taxes paid to other States, "apparently heeding the warning flag raised [in *Williams*] by the nation's high Court." *Dep't of Revenue v. Kuhnlein*, 646 So.2d 717, 723 (Fla. 1994). This uncertainty has unnecessarily predisposed States to forgo potential streams of income that they might otherwise be able to assess and devote to important public projects.

Second, the rule adopted by the Supreme Court of Appeals is unadministrable and creates significant uncertainty as to the validity of any use tax scheme that any State might adopt. Under the structural test set forth by this Court, both the Tax Commissioner and taxpayers can evaluate whether a tax is internally consistent by assuming that the same law is adopted by all other jurisdictions. But under the economic reality test applied by the Supreme Court of Appeals, internal consistency would involve "comparing [each tax] with slightly different taxes imposed by other States," and thus "the validity of state taxes would turn solely on 'the shifting complexities of the tax codes of 49 other States.'" *Goldberg*, 488 U.S. at 261 (quoting *Armco*, 467 U.S. at 645).

Indeed, the test adopted by the Supreme Court of Appeals would involve even more complexity than the approach rejected in *Goldberg*, as States would not only need to take into account the actual or

hypothetical tax structures of 49 other States, but also those of countless counties and municipalities. That is precisely the result that the internal consistency test was designed to avoid.

The compliance burden would fall heavily not only on States but also on taxpayers. The administration of most tax systems depends on taxpayers self-reporting the correct amount that they owe. It would be costly and unworkable to expect taxpayers to assess the interplay between their State's tax structure and any other state, county, or municipal tax structure prior to claiming a credit. But given the significant sums of money that may be at stake, many taxpayers will invest unnecessarily in legal services to discern whether they might have a meritorious claim. This will place unneeded burdens on both taxpayers and the courts.

Third, and finally, the effect of the decision by the Supreme Court of Appeals will fall disproportionately on smaller and poorer States and cities. For these jurisdictions, the amount of any credit on a particular transaction may meet or exceed the amount of any use tax imposed. This effect will be most keenly felt by municipalities, which are also subject to the dormant commerce clause. See *Dean Milk Co. v. City of Madison, Wisc.*, 340 U.S. 349, 354 n.4 (1951). Under the Supreme Court of Appeals' decision, a cash-strapped city like Detroit might have to provide a full credit for sales taxes paid to the State of California and all of California's various counties and cities. Theoretically, a city's entire sales and use tax on certain transactions could be zeroed out by

constitutionally mandated credits. This Court should intervene to prevent this unnecessary and burdensome result.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

Patrick Morrisey
Attorney General

Elbert Lin
Solicitor General

Thomas M. Johnson, Jr.
Deputy Solicitor General
Counsel of Record

Katherine A. Schultz
Senior Deputy Attorney General

Katlyn M. Miller
Assistant Attorney General

Office of the Attorney General
State Capitol
Building 1, Room E-26
Charleston, WV 25305
tjohnson@wvago.gov
(304) 558-2021

Counsel for Petitioner

April 17, 2017

IN THE SUPREME COURT OF APPEALS
OF WEST VIRGINIA

September 2016 Term

No. 15-0935

MARK W. MATKOVICH,
WEST VIRGINIA STATE TAX COMMISSIONER,
Petitioner Below, Petitioner

V.

CSX TRANSPORTATION, INC.
Respondent Below, Respondent

Appeal from the Circuit Court of Kanawha County
Honorable Louis H. Bloom, Judge
Civil Action No. 15-AA-36

AFFIRMED

Submitted: October 25, 2016
Filed: November 16, 2016

Patrick Morrisey, Esq.
Attorney General
Katherine A. Schultz
Senior Deputy Attorney General

James W. McBride,
pro hac vice
Baker, Donelson, Bearman, Caldwell & Berkowitz, PC

Charleston, West Virginia
Attorneys for the Petitioner

Washington, District of Columbia
Michael P. Markins
Cipriani & Werner PC
Charleston, West Virginia
Attorneys for the Respondent

JUSTICE DAVIS delivered the Opinion of the Court.

SYLLABUS BY THE COURT

1. "In an administrative appeal from the decision of the West Virginia Office of Tax Appeals, this Court will review the final order of the circuit court pursuant to the standards of review in the State Administrative Procedures Act set forth in *W. Va. Code*, 29A-5-4(g) [1988]. Findings of fact of the administrative law judge will not be set aside or vacated unless clearly wrong, and, although administrative interpretation of State tax provisions will be afforded sound consideration, this Court will review questions of law *de novo*." Syllabus point 1, *Griffith v. ConAgra Brands, Inc.*, 229 W. Va. 190, 728 S.E.2d 74 (2012).

2. "A state tax on interstate commerce will not be sustained unless it: '(1) has a substantial nexus with the State; (2) is fairly apportioned; (3) does not discriminate; and (4) is fairly related to the services provided by the State.' *Maryland v. Louisiana*, 451 U.S. 725, [754], 101 S. Ct. 2114, 2133, 68 L. Ed. 2d 576

(1981)." Syllabus point 1, *Western Maryland Railway Co. v. Goodwin*, 167 W. Va. 804, 282 S.E.2d 240 (1981).

3. The sales tax credit granted by W. Va. Code § 11-15A-10a(a) (2003) (Repl. Vol. 2010) provides a credit for sales taxes paid both to other states and to the subdivisions and municipalities of other states.

Davis, Justice:

The petitioner herein and petitioner below, Mark W. Matkovich, West Virginia State Tax Commissioner ("Tax Commissioner"), appeals from an order entered August 24, 2015, by the Circuit Court of Kanawha County. By that order, the circuit court affirmed a January 23, 2015, decision by the Office of Tax Appeals, which found that the respondent herein and respondent below, CSX Transportation, Inc. ("CSX"), is entitled to a credit under W. Va. Code § 11-15A-10a (2003) (Repl. Vol. 2010) for the sales taxes it paid to other states' subdivisions on its purchases of motor fuel therein. On appeal to this Court, the Tax Commissioner argues that the circuit court erred by allowing CSX a tax credit for all sales taxes it paid to other states' cities, counties, and other municipalities on the purchase of motor fuel therein rather than limiting the credit to sales taxes paid only to other states upon such purchases. Upon a review of the parties' arguments, the appendix record, and the pertinent authorities, we affirm the ruling of the circuit court. In summary, we conclude that the sales tax credit afforded by W. Va. Code § 11-15A-10a applies *both* to sales taxes paid to other states *and* to sales taxes paid to the municipalities of other states.

I.

FACTUAL AND PROCEDURAL HISTORY

The facts giving rise to the case *sub judice* are not disputed by the parties. CSX operates an interstate rail transportation system. Although CSX is a Virginia corporation with its principal place of business in Jacksonville, Florida, CSX also operates trains and maintains rail yards throughout the State of West Virginia. In 2010, an auditor from the West Virginia State Tax Department ("Tax Department") met with a representative of CSX at one of its West Virginia rail yards to conduct a field audit. As a result of this meeting, the auditor determined that CSX imports fuel that it uses in West Virginia, and, thus, CSX was directed to begin paying the West Virginia Motor Fuel Use Tax ("use tax"), imposed by W. Va. Code § 11-15A-13a (2003) (Repl. Vol. 2010),[1] on the fuel it uses in West Virginia.

W. Va. Code § 11-15A-10a (2003) (Repl. Vol. 2010)[2] affords taxpayers a credit for sales taxes paid to other states, which, with respect to the case *sub judice*, offsets the use tax a fuel importer must pay under W. Va. Code § 11-15A-13a. Following the aforementioned assessment, CSX filed amended use tax returns seeking a refund of the sales taxes it had paid on its

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[1] For the relevant statutory language, see Section III, *infra*. It also should be noted that the Legislature amended this statute in 2013; therefore, we will apply the prior version of the statute that was in effect at the time of the events giving rise to the instant proceeding.

[2] See *infra* Section III for the pertinent statutory language.

motor fuel purchases to cities, counties, and localities of other states pursuant to W. Va. Code § 11-15A-10a. The Tax Commissioner rejected CSX's refund request. During the evaluation of CSX's refund request, auditors with the Tax Department concluded that CSX had been improperly calculating the sales tax credit it was entitled to claim under W. Va. Code § 11-15A-10a. This inquiry led the Tax Department to issue a Notice of Assessment against CSX in June 2013, as well as the Tax Department's adoption of a new methodology, for most of tax year 2012, of determining how many gallons of motor fuel CSX was deemed to have used in West Virginia and how many of those gallons were purchased in other states.

Thereafter, CSX timely filed a petition for refund with the Office of Tax Appeals ("OTA"), challenging the denial of its refund request, and a petition for reassessment, contesting the June 2013 Notice of Assessment. Both petitions were consolidated, and, by final decision rendered January 23, 2015, the OTA granted CSX's refund request and vacated the 2013 assessment. In summary, the OTA determined that, under the dormant Commerce Clause,[3] CSX was entitled to a credit under W. Va. Code § 1115A-10a for the sales taxes it had paid on motor fuel purchased from the cities, counties, and other municipalities of other states. Otherwise, the OTA opined, a denial of such credit would unconstitutionally discriminate against interstate

[3] For further treatment of the dormant Commerce Clause, see Section III, *infra*.

commerce in violation of the dormant Commerce Clause.

The Tax Commissioner then appealed to the Circuit Court of Kanawha County. By order entered August 24, 2015, the circuit court affirmed the OTA's final decision. In so ruling, the circuit court agreed that the Tax Commissioner's allowance of a credit, to be applied to the use tax due from CSX, for sales taxes CSX paid to other states upon its purchases of motor fuel therein, coupled with a denial of such a credit for the sales taxes CSX paid to the cities, counties, and other localities of such states, unfairly discriminates against interstate commerce in violation of the dormant Commerce Clause. The circuit court further concluded that denying the credit for sales taxes paid to municipalities results in taxpayers potentially paying greater taxes on interstate purchases of motor fuel than on similar intrastate purchases.[4] From this adverse ruling, the Tax Commissioner appeals to this Court.

II.

STANDARD OF REVIEW

The sole issue presented by the case *sub judice* concerns the proper interpretation and application of the use tax credit provided by W. Va. Code § 11-15A-10a. Procedurally, the instant matter comes to this Court as an appeal from the Office of Tax Appeals

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[4] The circuit court additionally ordered the parties to submit calculations of the refund requested and the proper assessment of the subject taxes CSX is required to pay for 2012.

that was affirmed by the circuit court. We previously have explained the standard of review applicable to such a proceeding as follows:

> In an administrative appeal from the decision of the West Virginia Office of Tax Appeals, this Court will review the final order of the circuit court pursuant to the standards of review in the State Administrative Procedures Act set forth in *W. Va. Code*, 29A-5-4(g) [1988].[5] Findings of fact of the administrative law judge will not be set aside or vacated unless clearly wrong, and, although administrative interpretation of State tax provisions will be afforded sound

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[5] W. Va. Code § 29A-5-4(g) (1998) (Repl. Vol. 2015) defines the scope of judicial review of contested cases as follows:

> The court may affirm the order or decision of the agency or remand the case for further proceedings. It shall reverse, vacate or modify the order or decision of the agency if the substantial rights of the petitioner or petitioners have been prejudiced because the administrative findings, inferences, conclusions, decision or order are:
>
> (1) In violation of constitutional or statutory provisions; or
> (2) In excess of the statutory authority or jurisdiction of the agency; or
> (3) Made upon unlawful procedures; or
> (4) Affected by other error of law; or
> (5) Clearly wrong in view of the reliable, probative and substantial evidence on the whole record; or
> (6) Arbitrary or capricious or characterized by abuse of discretion or clearly unwarranted exercise of discretion.

> consideration, this Court will review questions of law *de novo*.

Syl. pt. 1, *Griffith v. ConAgra Brands, Inc.*, 229 W. Va. 190, 728 S.E.2d 74 (2012) (footnote added). Moreover, we previously have held that "[i]nterpreting a statute or an administrative rule or regulation presents a purely legal question subject to *de novo* review." Syl. pt. 1, *Appalachian Power Co. v. State Tax Dep't of West Virginia*, 195 W. Va. 573, 466 S.E.2d 424 (1995). *Accord* Syl. pt. 1, *Chrystal R.M. v. Charlie A.L.*, 194 W. Va. 138, 459 S.E.2d 415 (1995) ("Where the issue on an appeal from the circuit court is clearly a question of law or involving an interpretation of a statute, we apply a *de novo* standard of review."). In keeping with these standards, we proceed to consider the parties' arguments.

III.

DISCUSSION

Despite the numerous errors assigned in this case, the crux of the Tax Commissioner's argument can be distilled into a single issue: is a taxpayer, who is required to pay the motor fuel use tax imposed by W. Va. Code § 11-15A-13a, entitled to a sales tax credit, under W. Va. Code § 11-15A-10a, for sales taxes paid both to other states and to the municipalities of other states? Both the OTA and the circuit court determined that, to be constitutional under the dormant Commerce Clause, said credit must be granted for *both* sales taxes paid to other states *and* for sales taxes paid to the municipalities of other states. We reach the same conclusion.

The specific tax at issue in this proceeding is a use tax. Simply stated, "[a] use tax is collected when a good is sold from an out-of-state supplier for use within a state." *J.C. Penney Co., Inc. v. Hardesty*, 164 W. Va. 525, 530, 264 S.E.2d 604, 608 (1979). Pursuant to W. Va. Code § 11-15A-13a (2003) (Repl. Vol. 2010), a use tax is imposed upon taxpayers who purchase motor fuel outside of West Virginia but who use such fuel within this State.[6]

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[6] In pertinent part, W. Va. Code § 11-15A-13a(a) (2003) (Repl. Vol. 2010) imposes the motor fuel use tax as follows:

> (2) *On purchases out-of-state subject to motor fuel tax*. – Effective the first day of January, two thousand four, an excise tax is imposed on the importation into this state of motor fuel purchased outside this state when the purchase is subject to the flat rate of the tax imposed by section five [§ 11-14C-5], article fourteen-c of this chapter: Provided, That the rate of the tax due under this article shall in no event be less than five percent of the average wholesale price of the motor fuel, as determined in accordance with said section five, article fourteen-c: Provided, however, That the motor fuel subject to the tax imposed by this article shall comprise the variable component of the tax imposed by the said section five, article fourteen-c, and shall be collected and remitted by the seller at the time the seller remits the tax imposed by the said section five, article fourteen-c.
>
> (3) *On other purchases out-of-state*. – An excise tax is hereby imposed on the use or consumption in this state of motor fuel purchased outside this state at the rate of five percent of the average wholesale price of the motor fuel, as determined in accordance with section five [§ 11-14C-5], article fourteen-c of this chapter: Provided, That motor fuel contained in the fuel supply tank of a motor vehicle that is not a motor carrier shall not be taxable, except that motor fuel imported in the fuel supply tank or

This motor fuel use tax is calculated pursuant to W. Va. Code § 11-15A-13a(c)(1):

> (c) *Computation of tax due from motor carriers*. – Every person who operates or causes to be operated a motor carrier in this state shall pay the tax imposed by this section on the average wholesale price of all gallons of motor fuel used in the operation of any motor carrier within this state, under the following rules:
>
> (1) The total amount of motor fuel used in the operation of the motor carrier within this state is that proportion of the total amount of motor fuel used in a motor carrier's operations within and without this state, that the total number of miles traveled within this state bears to the total number of miles traveled within and without this state.[7]

(Footnote added).

Also at issue herein is the sales tax credit afforded to taxpayers for sales taxes they have paid

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> auxiliary tank of construction equipment, mining equipment, track maintenance equipment or other similar equipment, is taxed in the same manner as that in the fuel supply tank of a motor carrier.

See supra note 1.

7 Additional subsections of W. Va. Code § 11-15A-13a(c) regarding the calculation of the subject tax are not at issue in this proceeding.

to another state. Pursuant to W. Va. Code § 11-15A-10a (2003) (Repl. Vol. 2010),

> (a) [a] person is entitled to a credit against the tax imposed by this article on the use of a particular item of tangible personal property, custom software or service equal to the amount, if any, of sales tax lawfully paid to another state for the acquisition of that property or service: Provided, That the amount of credit allowed does not exceed the amount of use tax imposed on the use of the property in this state.
>
> (b) For purposes of this section:
>
> (1) "Sales tax" includes a sales tax or compensating use tax imposed on the use of tangible personal property or a service by the state in which the sale occurred; and
>
> (2) "State" includes the District of Columbia but does not include any of the several territories organized by Congress.

This sales tax credit operates as an offset to the motor fuel use tax with which CSX was assessed. The controversy in this case relates to the extent of the sales tax credit allowed by W. Va. Code § 11-15A-10a, *i.e.*, whether such credit is limited to sales taxes paid *only* to other states or whether such credit is granted for sales taxes paid *both* to other states *and* the subdivisions of other states.

Our consideration of this issue is guided by the Commerce Clause, the dormant Commerce Clause, and the cases analyzing these provisions.

> The Commerce Clause grants Congress power to "regulate Commerce . . . among the several States." [U.S. Const.] Art. I, § 8, cl. 3. . . . Although the Clause is framed as a positive grant of power to Congress, "we have consistently held this language to contain a further, negative command, known as the dormant Commerce Clause, prohibiting certain state taxation even when Congress has failed to legislate on the subject." *Oklahoma Tax Comm'n v. Jefferson Lines, Inc.*, 514 U.S. 175, 179, 115 S. Ct. 1331, [1335,] 131 L. Ed. 2d 261 (1995).
>
> . . . .
>
> Under our precedents, the dormant Commerce Clause precludes States from "discriminat[ing] between transactions on the basis of some interstate element." *Boston Stock Exchange v. State Tax Comm'n*, 429 U.S. 318, 332, n. 12, 97 S. Ct. 599, [608, n. 12,] 50 L. Ed. 2d 514 (1977). This means, among other things, that a State "may not tax a transaction or incident more heavily when it crosses state lines than when it occurs entirely within the State." *Armco Inc. v. Hardesty*, 467 U.S. 638, 642, 104 S. Ct. 2620, [2622,] 81 L. Ed. 2d 540 (1984). "Nor may a State impose a tax which discriminates against interstate commerce either by providing

> a direct commercial advantage to local business, or by subjecting interstate commerce to the burden of 'multiple taxation.'" *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450, 458, 79 S. Ct. 357, [362,] 3 L. Ed. 2d 421 (1959) (citations omitted).

Comptroller of the Treasury of Maryland v. Wynne, ___ U.S. ___, ___, 135 S. Ct. 1787, 1794, 191 L. Ed. 2d 813 (2015).

To determine constitutionality under the dormant Commerce Clause, the United States Supreme Court has developed a test, known as the *Complete Auto* test,[8] wherein the Court "considered not the formal language of the tax statute but rather its practical effect" and provided a list of criteria a reviewing court should consider. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279, 97 S. Ct. 1076, 1079, 51 L. Ed. 2d 326 (1977). We adopted this test in Syllabus point 1 of *Western Maryland Railway Co. v. Goodwin*, 167 W. Va. 804, 282 S.E.2d 240 (1981), holding:

> A state tax on interstate commerce will not be sustained unless it: "(1) has a substantial nexus with the State; (2) is fairly apportioned; (3) does not discriminate; and (4) is fairly related to the services provided by the State." *Maryland v. Louisiana*, 451 U.S. 725, [754], 101 S. Ct. 2114, 2133, 68 L. Ed. 2d 576 (1981).

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[8] *See Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 97 S. Ct. 1076, 51 L. Ed. 2d 326 (1977).

While this test is phrased in terms of a tax that is charged to a taxpayer, it has been applied with equal force to credits afforded to taxpayers. *See generally Comptroller of the Treasury of Maryland v. Wynne*, ___ U.S. ___, 135 S. Ct. 1787, 191 L. Ed. 2d 813; *Arizona Dep't of Revenue v. Arizona Pub. Serv. Co.*, 188 Ariz. 232, 934 P.2d 796 (Ct. App. 1997); *General Motors Corp. v. City & Cnty. of Denver*, 990 P.2d 59 (Colo. 1999) (en banc).

A. Substantial Nexus

With respect to the first factor, "substantial nexus with the State,"[9] we have recognized that

> when a direct relationship can be demonstrated between the tax and the cost to the State of the benefits and protections it affords, there is a sufficient nexus for taxation, but the opposite is not true, i.e., nexus may exist even if the in-state activities are not shown to cost the State as much as the amount of the taxes.

Western Maryland, 167 W. Va. at 809, 282 S.E.2d at 244 (citations omitted). Therefore, "purposive, revenue generating activities in the State are sufficient to render a person liable for taxes" and to satisfy the nexus requirement. *Id.*

Under the facts of the case *sub judice*, we conclude that both the use tax imposed by W. Va. Code § 11-

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[9] Syl. pt. 1, in part, *Western Maryland Railway Co. v. Goodwin*, 167 W. Va. 804, 282 S.E.2d 240 (1981) (internal quotations and citations omitted).

15A-13a and the sales tax credit allowed by W. Va. Code § 11-15A-10a satisfy this first requirement of "substantial nexus with the State." The parties do not dispute that CSX operates its rail service through the State of West Virginia and that it purchases fuel outside of West Virginia which it uses in its operations in this State.

B. Apportionment

Next we consider the apportionment requirement, which "ensure[s] that each State taxes only its fair share of an interstate transaction." *Jefferson Lines*, 514 U.S. at 184, 115 S. Ct. at 1338, 131 L. Ed. 2d 261 (internal quotations and citation omitted). *Accord Japan Line, Ltd. v. Los Angeles Cnty.*, 441 U.S. 434, 446-47, 99 S. Ct. 1813, 1820, 60 L. Ed. 2d 336 (1979) ("In order to prevent multiple taxation of interstate commerce, this Court has required that taxes be apportioned among taxing jurisdictions, so that no instrumentality of commerce is subjected to more than one tax on its full value." (internal citations omitted)).

To evaluate whether a tax is "fairly apportioned," the United States Supreme Court ascertains whether the taxing scheme in question is internally consistent and externally consistent.

> Internal consistency is preserved when the imposition of a tax identical to the one in question by every other State would add no burden to interstate commerce that intrastate commerce would not also bear. This test asks nothing about the degree of economic reality

> reflected by the tax, but simply looks to the structure of the tax at issue to see whether its identical application by every State in the Union would place interstate commerce at a disadvantage as compared with commerce intrastate. A failure of internal consistency shows as a matter of law that a State is attempting to take more than its fair share of taxes from the interstate transaction, since allowing such a tax in one State would place interstate commerce at the mercy of those remaining States that might impose an identical tax. . . .
>
> External consistency, on the other hand, looks not to the logical consequences of cloning, but 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. at 185, 115 S. Ct. at 1338, 131 L. Ed. 2d 261 (citations omitted).

> In considering the apportionment criterion, we have observed that
>
> [a] tax on a person involved in both wholly intrastate commerce and interstate commerce with in-state aspects, must be tailored so as to attach primarily to revenue derived from in-state activities. In the case of transportation, it is true most of the time that a tax related to

> cargo or passenger miles traveled in state or to the miles of the line in state will be valid.

Western Maryland, 167 W. Va. at 809, 282 S.E.2d at 244 (citations omitted).

Applying these standards to the facts of the case *sub judice*, we conclude that the subject use tax is fairly apportioned. Consistent with our recognition in *Western Maryland*, the use tax herein is calculated with specific reference to the amount of motor fuel CSX uses in its West Virginia operations:

> The total amount of motor fuel used in the operation of the motor carrier within this state is that proportion of the total amount of motor fuel used in a motor carrier's operations within and without this state, that the total number of miles traveled within this state bears to the total number of miles traveled within and without this state.

W. Va. Code § 11-15A-13a(c)(1). Thus, the use tax charged to CSX directly correlates to the fuel that it uses for the miles it travels within West Virginia; as such, the use tax is fairly apportioned.

However, we cannot reach the same conclusion with respect to the Tax Commissioner's interpretation of the corresponding sales tax credit. Pursuant to W. Va. Code § 11-15A-10a(a),

> [a] person is entitled to a credit against the tax imposed by this article on the use of a particular item of tangible personal property, custom

> software or service equal to the amount, if any, of sales tax lawfully paid to another state for the acquisition of that property or service: Provided, That the amount of credit allowed does not exceed the amount of use tax imposed on the use of the property in this state.

Other than indicating that the word "State" includes the District of Columbia but none of the United States' territories, the statute is silent as to the scope of the sales tax credit allowed. *See* W. Va. Code § 11-15A-10a(b)(2). In his arguments to the Court, the Tax Commissioner contends that the sales tax credit applies only to sales taxes that CSX has paid to other *states* on its motor fuel purchases. By contrast, CSX argues that it should be permitted to claim the sales tax credit *both* for sales taxes it has paid to other states upon its purchases of motor fuel *and* for sales taxes it has paid to the municipalities of other states upon its purchases of motor fuel. We find CSX's position to be most in keeping with the Supreme Court's internal consistency test and recent cases interpreting the same.

For example, in *Comptroller of the Treasury of Maryland v. Wynne*, ___ U.S. ___, 135 S. Ct. 1787, 191 L. Ed. 2d 813, the Supreme Court reviewed a Maryland income tax scheme that allowed a credit to taxpayers for income tax they had paid to another state but did not allow a credit for income tax they had paid to the county of another state. Finding this differential treatment to be invalid under the internal consistency test, the Court considered "not the formal language of

the tax statute but rather its practical effect,"[10] because "[t]he Commerce Clause regulates effects, not motives." *Id.* at ___ n.4, 135 S. Ct. at 1801 n.4, 191 L. Ed. 2d 813. In reaching its decision, the Court further noted that "[t]he critical point is that the total tax burden on interstate commerce is higher," which contravenes the dormant Commerce Clause. *Id.* at ___, 135 S. Ct. at 1805, 191 L. Ed. 2d 813.

Likewise, in *General Motors Corp. v. City and County of Denver*, 990 P.2d 59 (Colo. 1999) (en banc), the Colorado Supreme Court examined a use tax levied by the City and County of Denver, Colorado. Under the applicable law, the City and County provided an offsetting sales tax credit, but only for such taxes paid to other states' municipalities. *See* D.R.M.C. § 53-92(c). Evaluating whether the subject tax was valid under the Commerce Clause, the Colorado court observed that

> [a] state tax is internally consistent if it is structured so that if every State were to impose an identical tax, no multiple taxation would result. . . . To avoid multiple taxation, a tax upon interstate commerce must either be apportioned to relate the tax to the activity taking place within the taxing state or it must allow a credit for other similar taxes paid by the taxpayer in other jurisdictions.

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[10] *Comptroller of the Treasury of Maryland v. Wynne*, ___ U.S. ___, ___, 135 S. Ct. 1787, 1795, 191 L. Ed. 2d 813 (2015) (internal quotations and citations omitted).

990 P.2d at 69 (internal quotations and citations omitted). Moreover, the court noted that

> the overwhelming majority of states meet the internal consistency test by providing a credit for sales or use taxes paid to other states. However, the crediting structure must be designed properly. Internal consistency requires that states impose identical taxes when viewed in the aggregate–as a collection of state and sub-state taxing jurisdictions. In other words, the interstate taxpayer should never pay more sales or use tax than the intrastate taxpayer.

Id. (internal quotations, citations, and footnote omitted). Upholding the tax's validity, the Colorado Supreme Court ruled that

> Denver must provide GM with a credit for the sales and use taxes paid to other states and their subdivisions such that GM will pay no more tax on the automobiles than it would have paid by purchasing the component parts in the City and County of Denver, State of Colorado.

Id. at 71. Without such offsetting credit, however, the subject tax would not be constitutionally valid. *See id.*

Finally, in *Arizona Department of Revenue v. Arizona Public Service Co.*, 188 Ariz. 232, 934 P.2d 796 (Ct. App. 1997), the Arizona Court of Appeals considered whether that state's statute affording a tax credit for sales taxes "imposed . . . under the laws of

another state of the United States," Ariz. Rev. Stat. § 42-1409(A)(2), applied only to sales taxes paid to other states or whether it applied also to sales taxes paid to the counties of other states. In determining that the tax credit extends to *both* sales taxes paid to other states *and* to the counties of other states, the court recognized that

> [c]ounties are state-created entities[;] [c]ounties have only the powers that a state gives them[; and] [c]ounties draw their taxing authority from the state constitution.
>
> The derivative relationship between a state and its counties means that when a county imposes a tax, it does so pursuant to a delegation of state tax authority.

Id. at 235, 934 P.2d at 799 (citations omitted). The court then reiterated the governing constitutional tenets:

> The Commerce Clause of the United States Constitution forbids discrimination against interstate commerce. A state may not subject a transaction to a greater tax when it crosses state lines than when it occurs entirely intrastate.
>
> State use taxes typically apply only to the use of goods purchased outside the taxing state and brought into it. A use tax thus inherently discriminates against interstate commerce. Nevertheless, such a tax is valid under the Commerce Clause as a

> "compensatory tax" if the state imposes an intrastate tax such that the burdens imposed on interstate and intrastate commerce are equal. The taxpayer's out-of-pocket expenses determine whether the burdens are equal.

Id. (citations omitted). Considering the tax credit at issue in the case, the Arizona court determined that the tax credit extends *both* to sales taxes paid to other states *and* to sales taxes paid to the counties of other states; otherwise, it reasoned, taxpayers paying both taxes but not receiving credit for both taxes would incur a higher tax burden than an in-state taxpayer who had not made such out-of-state purchases. *Id.*

Applying these authorities to the case *sub judice*, we agree with the circuit court's determination that the sales tax credit afforded by W. Va. Code §11-15A-10a extends *both* to sales taxes CSX has paid to other states on its purchases of motor fuel therein *and* to sales taxes that CSX has paid to the subdivisions of other states when it has purchased motor fuel in such locales. Any other construction of this statute would invariably violate the Commerce Clause's prohibition on subjecting interstate transactions to a greater tax burden than that imposed on strictly intrastate dealings. The easiest way to demonstrate this dichotomy is through a simple math analysis. If, for example, CSX is required to pay a 5% use tax[11] on all

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[11] The figures used in this hypothetical example are for explanation purposes only and are not intended to reflect the precise measure of actual taxes assessed against or paid by CSX in the underlying proceedings.

motor fuel it uses in this State and if it is allowed a corresponding sales tax credit for all fuel it has purchased out of state, such sales tax credit serves as an offset to CSX's use tax liability. Thus, in this example, if CSX pays 5% sales tax to State A, it would receive a 5% sales tax credit that completely offsets its use tax liability.

If, however, CSX pays 3% sales tax to State A and 2% sales tax to the City of Metropolis in State A, it still is paying 5% out-of-state sales tax but, under the Tax Commissioner's interpretation of the sales tax credit, CSX would pay substantially more use tax than a taxpayer who had not paid sales taxes to another state's subdivision. This is so because CSX is assessed the same 5% use tax, which is offset by the 3% State A sales tax and yields a residual 2% use tax liability. Because, in this scenario, CSX did not receive a sales tax credit for the additional 2% sales tax it paid to the City of Metropolis, however, CSX essentially is paying 7% in total taxes, *i.e.*, 5% use tax (which is partially offset by 3% credit for sales tax paid to State A) + 2% sales tax paid to City of Metropolis (for which Tax Commissioner did not grant it a sales tax credit) = 7%, simply because CSX transacted business interstate in a jurisdiction that allowed its subdivisions to charge a sales tax. Strictly in-state taxpayers would not incur this additional tax liability, nor would out-of-state taxpayers who paid sales taxes assessed only by states and not their subdivisions.

Thus, because disallowance of the sales tax credit for sales taxes imposed by the subdivisions of other states would produce a "total tax burden on interstate

commerce [that] is higher" than a purely intrastate transaction, *Wynne*, ___ U.S. at ___, 135 S. Ct. at 1805, 191 L. Ed. 2d 813, we find the Tax Commissioner's interpretation of the W. Va. Code § 11-15A-10a sales tax credit to be violative of the dormant Commerce Clause. Accordingly, we hold that the sales tax credit granted by W. Va. Code § 11-15A-10a(a) (2003) (Repl. Vol. 2010) provides a credit for sales taxes paid both to other states and to the subdivisions and municipalities of other states. Thus, we conclude that CSX is entitled to a sales tax credit, under W. Va. Code § 11-15A-10a, for the sales taxes it has paid both to other states and to the subdivisions thereof. As such, we affirm the rulings of the circuit court and the OTA reaching the same conclusion.

C. Discrimination

The third factor examines whether the subject tax scheme discriminates or treats taxpayers differently. *See generally* Syl. pt. 1, *Western Maryland*, 167 W. Va. 804, 282 S.E.2d 240. "Essentially this criterion requires equal treatment of interstate and local commerce[.] No state may impose a tax which discriminates against interstate commerce by providing a direct commercial advantage to local business." *Western Maryland*, 167 W. Va. at 809, 282 S.E.2d at 244 (internal quotations and citations omitted). In other words, "[a] State may not impose a tax which discriminates against interstate commerce by providing a direct commercial advantage to local business. Thus, States are barred from discriminating against foreign enterprises competing with local businesses, and from discriminating against commercial activity occurring

outside the taxing State." *Jefferson Lines*, 514 U.S. at 197, 115 S. Ct. at 1344, 131 L. Ed. 2d 261 (internal quotations and citations omitted).

Applying this query to the facts of the case *sub judice*, we find, as we did with the apportionment requirement, that the use tax imposed by W. Va. Code § 11-15A-13a is properly constructed so as to tax only the motor fuel that a motor carrier actually uses within the boundaries of this State. However, as with our foregoing analysis of the corresponding sales tax credit, we conclude that, under the interpretation afforded to W. Va. Code § 1115A-10a by the Tax Commissioner, allowing the sales tax credit only for sales taxes paid to other states unfairly discriminates against interstate commerce. Therefore, we again determine that the proper, and constitutionally sound, construction to be afforded to this provision requires that it apply with equal force to grant a credit for sales taxes paid *both* to other states *and* to sales taxes paid to the municipalities of other states on purchases of motor fuel therein.

D. Relationship

The fourth and final inquiry examines whether the tax on interstate commerce is "fairly related to the services provided by the State." Syl. pt. 1, in part, *Western Maryland*, 167 W. Va. 804, 282 S.E.2d 240. *Accord Jefferson Lines*, 514 U.S. at 199, 115 S. Ct. at 1345, 131 L. Ed. 2d 261 ("Finally, the Commerce Clause demands a fair relation between a tax and the benefits conferred upon the taxpayer by the State." (citations omitted)). In this regard, we have noted that

> there need not be any direct correlation between the value of benefits afforded the taxpayer by the State and the cost of the tax to the taxpayer. Once the nexus requirement has been met, the fourth criterion imposes the additional limitation that the measure of the tax must be reasonably related to the extent of the contact [and] the activities or presence of the taxpayer in the State. Therefore, when the measure of a tax is reasonably related to the taxpayer's activities or presence in the State[,] the taxpayer will realize, in proper proportion to the taxes it pays, the only benefit to which it is constitutionally entitled[:] that derived from his enjoyment of the privileges of living in an organized society, established and safeguarded by the devotion of taxes to public purposes.

Western Maryland, 167 W. Va. at 810, 282 S.E.2d at 245 (internal quotations and citations omitted). *See also Jefferson Lines*, 514 U.S. at 200, 115 S. Ct. at 1346, 131 L. Ed. 2d 261 ("*Complete Auto*'s fourth criterion asks only that the measure of the tax be reasonably related to the taxpayer's presence or activities in the State." (citation omitted)).

As with our review of the substantial nexus requirement, we likewise conclude that the subject use tax and corresponding sales tax credit are fairly related to the services provided to CSX by this State as well as to CSX's presence and activities herein. In short, CSX maintains an extensive system of railway lines in this State, and West Virginia, in turn, provides emergency

services and other infrastructure related to CSX's operations.

Having considered each of the factors of the *Complete Auto* test, we are left with the definite and firm conclusion that both the OTA and the circuit court ruled correctly in determining that the sales tax credit granted by W. Va. Code § 11-15A-10a extends *both* to sales taxes paid to other states *and* to sales taxes paid to the subdivisions of other states. Accordingly, we affirm the circuit court's order.

IV.

CONCLUSION

For the foregoing reasons, the August 24, 2015, order of the Circuit Court of Kanawha County is hereby affirmed.

Affirmed.

IN THE CIRCUIT COURT OF KANAWHA COUNTY,
WEST VIRGINIA

CSX TRANSPORTATION, INC.,

Petitioner below, Respondent,

v.

MATKOVICH, MARK W., as
STATE TAX COMMISSIONER of
WEST VIRGINIA

Respondent below, Petitioner

Civil Action No. 15-AA-36

Judge Louis Bloom

FINAL ORDER

Pending before the Court is a *Petition for Appeal* filed on March 27, 2015 by the Petitioner, Mark W. Matkovich, State Tax Commissioner of West Virginia ("Tax Commissioner"), by counsel, Katherine A. Schultz, Senior Deputy Attorney General. The Tax Commissioner requests that this Court reverse the final decision of the West Virginia Office of Tax Appeals ("OTA"), specifically, OTA Docket Numbers 12-477 RMFE and 13-278 M. Upon review of the parties' legal memoranda, oral arguments, the record, and the applicable law, the Court finds and concludes as follows:

STANDARD OF REVIEW

The procedures applicable to judicial review of decisions of the Office of Tax Appeals are governed by Section 29A-5-4, *et seq.* of the West Virginia Code, otherwise known as the State Administrative Procedures Act. W. Va. Code § 11-10A-19(f). Specifically, West Virginia Code Section 29A-5-4(g) states as follows:

> The court may affirm the order or decision of the agency or remand the case for further proceedings. It shall reverse, vacate or modify the order or decision of the agency if the substantial rights of the petitioner or petitioners have been prejudiced because the administrative findings, inferences, conclusions, decision or order are:
>
> (1) In violation of constitutional or statutory provisions; or
>
> (2) In excess of the statutory authority or jurisdiction of the agency; or
>
> (3) Made upon unlawful procedures; or
>
> (4) Affected by other error of law; or
>
> (5) Clearly wrong in view of the reliable, probative and substantial evidence on the whole record; or

> (6) Arbitrary or capricious or characterized by abuse of discretion or clearly unwarranted exercise of discretion.[1]

Conclusions of law by the Office of Tax Appeals are reviewed *de novo*.

FINDINGS OF FACT

1. Respondent is a Virginia corporation with its principal place of business in Jacksonville, Florida. The Respondent's business is interstate rail transportation.

2. In October 2010, an auditor with the West Virginia State Tax Department met with a representative of Respondent at one of its rail yards in West Virginia and characterized this meeting as a "field audit." One of the results of this field audit was to set up the Respondent as a fuel importer and to ensure that it began to pay West Virginia Motor Fuel Use Tax under Section 11-15A-13a of the West Virginia Code ("WV Use Tax") on the fuel it was using in West Virginia.

3. Thereafter, Respondent filed amended West Virginia Motor Fuel Use Tax Returns wherein the Respondent sought a credit for sales taxes paid for locomotive fuel to cities, counties, and other localities in states other than West Virginia under West Virginia Code Section 11-15A-10a. The Tax Commissioner determined that the Respondent was

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[1] W. Va. Code § 29A-5-4(g).

not entitled to a credit for these taxes and issued a Refund Denial.

4. During the process of reviewing the amended returns, the auditor and other Tax Department employees considered what they determined to be a different problem, namely, the way Respondent was calculating the credit it was seeking for fuel taxes paid to other states. This led the auditor to conduct another field audit which led to a Notice of Assessment against the Respondent for WV Use Tax on June 5, 2013. For three quarters in 2012, an auditor in the West Virginia Tax Department utilized a "new" methodology to determine gallons of motor fuel deemed used in West Virginia, and how many of those gallons were purchased in other states and taxed.

5. On December 14, 2012, Respondent timely filed with the OTA a petition for refund. Additionally, as a result of the Notice of Assessment, Respondent also filed a timely petition for reassessment. The two petitions were consolidated before the OTA and an evidentiary hearing was held on April 30, 2014. At the conclusion of the hearing, the parties filed legal briefs.

6. On January 23, 2015, the OTA rendered its Final Decision which granted Respondent's refund request and vacated the Assessment issued by the Tax Department.

7. The OTA determined that the Respondent was entitled to a credit under Section 11-15A-10a of

the West Virginia Code for sales taxes paid to cities, counties, and other localities. The OTA based this determination primarily on its review and analysis of the dormant Commerce Clause jurisprudence. As a result, the OTA opined that "the Tax Commissioner has applied West Virginia's use tax to the Petitioner here in a manner that violates the dormant Commerce Clause because its application is not fairly apportioned and discriminates against interstate commerce."[2]

8. On March 27, 2015, the Tax Commissioner filed the *Petition for Appeal* before this Court, citing eight assignments of error. Respondent filed a Response to the Petition for Appeal, stating that the true issue before this Court is the strictly legal question of whether CSXT is entitled to claim a use tax credit for local taxes paid to cities, counties, and other localities in other states.[3]

9. The Tax Commissioner filed its Memorandum of Law, agreeing that "[t]he only issue on appeal is whether CSXT is entitled to claim a credit for local taxes paid in other states in order to reduce the assessment and obtain a refund."[4] The

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[2] Final Decision, pp. 13-14.

[3] CSXT filed a Response to the Tax Commissioner's Petition for Appeal, which informed the Court that there are no issues as to whether CSXT is entitled to a credit over the 6% tax rate imposed on motor fuel under West Virginia statutes, or whether CSXT is entitled to claim a credit for certain Florida taxes paid. CSXT does not claim any credits above the 6% tax rate imposed on motor fuel in this state, nor a credit for certain Florida taxes paid.

[4] Appellant's Memo. of Law, p. 3.

Tax Commissioner set forth three arguments in its Memorandum of Law, namely that: (1) the OTA's decision ignored the statutory mandate of W. Va. Code § 11-15A-10a; (2) the OTA erroneously found that the Tax Commissioner's application of the use tax credit in Section 11-15A-10a was unconstitutional; and (3) the WV Use Tax does not violate the external consistency test.

10. Respondent filed its Response, countering the Tax Commissioner's position with three arguments in opposition, namely that: (1) dormant Commerce Clause jurisprudence clearly dictates that a failure to allow a credit for local taxes paid in other jurisdictions violated the dormant Commerce Clause; (2) the OTA correctly applied the law and found that not allowing a credit for local sales taxes paid to other jurisdictions ran afoul of the dormant Commerce Clause; and (3) the Tax Commissioner failed to show there was any error in the OTA's final decision.

11. This Court held a hearing on August 6, 2015. At oral argument, Respondent stated that once the legal question of whether it is entitled to a credit for local sales taxes paid to other states is addressed, it would agree to jointly calculate the proper assessment for the three quarters of 2012 and the calculation of the refund request with the Tax Department. Thus, the sole issue before this Court is whether the OTA's final decision was correct on the legal issue of whether the failure to allow a use tax credit for sales taxes paid to cities, counties, and

other localities of another state violates the dormant Commerce Clause.

DISCUSSION AND CONCLUSIONS OF LAW

Whether the Tax Commissioner's application of the use tax credit violates the dormant Commerce Clause

12. This Court will first address the issue of whether the failure to allow a use tax credit for sales taxes paid to cities, counties, and other localities of another state violates the dormant Commerce Clause.

13. Article 1, § 8 of the United States Constitution states that Congress has the authority to "regulate Commerce with foreign Nations, and among the several States." The Supreme Court has determined that, in addition to granting express authority to regulate interstate commerce, the Commerce Clause also prevents state regulations that interfere with interstate commerce by way of the doctrine otherwise known as the "dormant" Commerce Clause.[5]

14. A fundamental principle of the dormant Commerce Clause is that "a state may not subject a transaction to a greater tax when it crosses state

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[5] *See Tax Com'r of State v. MBNA America Bank, NA.,* 640 S.E.2d 226, 229 (W.Va. 2006), citing *South Carolina State Highway Dept. v. Barnwell Bros., Inc.,* 303 U.S. 177 (1938).

lines than when it occurs entirely intrastate."[6] West Virginia courts must utilize the same test as the United States Supreme Court when considering whether a state tax scheme runs afoul of the dormant Commerce Clause. "A state tax on interstate commerce will not be sustained unless it: (1) has a substantial nexus with the State; (2) is fairly apportioned; (3) does not discriminate; and (4) is fairly related to the services provided by the State."[7] This test is referred to as the *Complete Auto* test, as created in *Complete Auto Transit, Inc. v. Brady,* 430 U.S. 274 (1977).

15. The "apportionment" requirement ensures that each state taxes only its fair share of an interstate transaction.[8] Accordingly, "[i]t is a commonplace of constitutional jurisprudence that multiple taxation may well be offensive to the Commerce Clause. In order to prevent multiple taxation of interstate commerce, the Court has required that taxes be apportioned among taxing jurisdictions, so that no instrumentality of commerce is subjected to more than one tax on its full value."[9] To analyze whether a state tax is fairly apportioned, interpreting bodies look to whether "a tax is

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[6] *Associated Indus. of Missouri v. Lohman,* 511 U.S. 641, 646 (1994).

[7] *Griffith v. ConAgra Brands, Inc.,* 728 S.E.2d 74, 80 (W.Va. 2012), citing *Complete Auto Transit, Inc. v. Brady,* 430 U.S. 274 (1977).

[8] *See Goldberg v. Sweet,* 488 U.S. 252, 261 (1989).

[9] *Japan Line, Ltd. v. County of Los Angeles,* 441 U.S. 434, 446-47 (1979).

'internally consistent' and, if so, whether it is 'externally consistent' as well."[10]

16. A state's failure to establish the internal consistency of its tax scheme is fatal because: "A failure of internal consistency shows as a matter of law that a State is attempting to take more than its fair share of taxes from the interstate transaction, since allowing such a tax in one State would place interstate commerce at the mercy of those remaining States that might impose an identical tax."[11] The Supreme Court recently explained the internal consistency test:

> By hypothetically assuming that every State has the same tax structure, the internal consistency test allows courts to isolate the effect of a defendant State's tax scheme. This is a virtue of the test because it allows courts to distinguish between (1) tax schemes that inherently discriminate against interstate commerce without regard to the tax policies of other States, and (2) tax schemes that create disparate incentives to engage in interstate commerce (and sometimes result in double taxation) only as a result of the interaction of two different but nondiscriminatory and internally consistent schemes. . . . The first category of taxes is typically unconstitutional; the second is not. . . . Tax schemes that fail the internal consistency test will fall into the first

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[10] *Oklahoma Tax Comm'n v. Jefferson Lines,* 514 U.S. 175, 185 (1995).

[11] *Id.*

> category, not the second: Any cross-border tax disadvantage that remains after application of the test cannot be due to tax disparities but is instead attributable to the taxing State's discriminatory policies alone.[12]

17. Internal consistency "looks to the structure of the tax at issue to see whether its identical application by every state in the Union would place interstate commerce at a disadvantage as compared with commerce intrastate."[13] With respect to the tax at issue, use taxes are inherently discriminatory against interstate commerce because use taxes are typically only applied to the use of goods purchased outside the taxing state and brought into it.[14] Use taxes are valid, however, if the burdens of the tax imposed on intrastate and interstate commerce are equal.[15] Moreover, for over twenty years, since the Supreme Court's decision in *Oklahoma Tax Commission v. Jefferson Lines, Inc.* 514 U.S. 175 (1995), it has been clear that a state is constitutionally required to provide a credit against its own use tax for sales or use taxes paid to other jurisdictions.[16]

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[12] *Comptroller of Treasury of Maryland v. Wynne*, 135 S. Ct. 1787, 1802 (2015).

[13] *Id.*

[14] *See Ariz. Dept. of Revenue v. Ariz. Public Service Co.*, 934 P.2d 796, 799 (Ariz. Ct. App., 1997).

[15] *Id.*

[16] *See* 1 Hellerstein & Hellerstein, *State Taxation*, ¶ 18.09[2], 2015 WL 1646564, pp. *1-*2 (3d ed. 2000-15).

18. Thus, in the context of a use tax, state tax schemes meet this internal consistency test by providing a credit for sales or use taxes paid to other jurisdictions.[17] And importantly, passing this test "requires that states impose identical taxes when viewed *in the aggregate*-- as a collection of state and sub-state taxing jurisdictions."[18] In other words, taxes imposed by a sub-state taxing jurisdiction are imputed to the state in applying the internal consistency test as being derivative of a state's overall sovereign tax authority.

19. In order to determine whether a tax scheme is internally consistent, courts have consistently utilized a test which hypothetically assumes that every State applies its taxing scheme in the same potentially offending manner to isolate the effect of that state's tax scheme.[19]

20. For example, in *Arizona Dep't of Revenue,* the Court of Appeals of Arizona first discussed the jurisprudence of fair apportionment under the internal consistency test:

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[17] *General Motors Corp. v. City and Cnty. of Denver,* 990 P.2d 59, 69 (Colo. 1999), citing Walter Hellerstein, *Is "Internal Consistency" Foolish?: Reflections On an Emerging Commerce Clause Restraint on State Taxation,* 87 Mich. L. Rev. 138, 160 (1988).

[18] 990 P.2d at 69 (emphasis added).

[19] *See, e.g., Compt. of Treasury of Maryland v. Wynne,* 135 S. Ct. 1787, 1802 (2015); *General Motors Corp. v. City and Cnty. of Denver,* 990 P. 2d at 69; *Ariz. Dept. of Revenue v. Ariz. Public Service Co.,* 934 P. 2d at 799.

> State use taxes typically apply only to the use of goods purchased outside the taxing state and brought into it. A use tax thus inherently discriminates against interstate commerce. Nevertheless, such tax is valid under the Commerce Clause as a 'compensatory tax' if the state imposes an intrastate tax such that the burdens imposed on interstate and intrastate commerce are equal. The taxpayer's out-of-pocket expenses determine whether the burdens are equal. Equal treatment for instate and out-of-state taxpayers similarly situated is the condition precedent for a valid use tax on goods imported from out-of-state.[20]

After citing these principles of dormant Commerce Clause jurisprudence, using a simple math analysis, the Court explained its ruling that the Department of Revenue violated the internal consistency test because if an Arizona company bought coal in Arizona, it would pay 5% sales tax, and by a refusal to provide credit for all of the taxes paid on that same unit of coal, an interstate taxpayer ended up paying a total of 5.25% in taxes for the same amount of coal.[21]

21. The leading treatise on state and local taxation provides further guidance on the internal consistency requirements of the credit provisions in *Arizona Dep't of Revenue*:

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[20] 934 P. 2d at 799.

[21] *Id.*

> An application of the "internal consistency" doctrine to the position of the Arizona DOR demonstrates the soundness of the Arizona court's conclusion from a constitutional standpoint. If every state had a crediting provision limited to state-level sales and use taxes imposed by other states, the interstate enterprise that purchased goods or services in a local taxing jurisdiction in State A and used the goods or services in a local taxing jurisdiction in State B would be placed at a competitive disadvantage to the enterprise that confined its activities to the local taxing jurisdiction in state A or State B. The former enterprise would pay a local sales tax in State A as well as a local tax in State B, whereas the latter enterprise would pay but a single local tax in either State A or State B. That is precisely the type of burden on interstate activity that the "internal consistency" doctrine was intended to prohibit.[22]

22. Another example of the internal consistency test is *General Motors Corp.,* where the highest court in Colorado found that the Denver city and county municipal code section, section 53-92(c)—which only credits sales and use taxes paid to other municipalities—was an internally inconsistent tax scheme.[23] In holding that the credit mechanism had

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[22] 1 Hellerstein & Hellerstein, STATE TAXATION, ¶ 18.09[3][a], 2015 WL 1646564, pp. *6 (3d ed. 2000-15).

[23] 990 P. 2d at 69.

the potential to cause multiple taxation, the Court found:

> For example, if Colorado imposed a 1% sales or use tax and Denver a 2% tax, a purchaser or user would owe a 3% total tax. Similarly, if Michigan collected a 2% sales or use tax and Detroit a 1% tax, a purchaser or user in Detroit would pay a 3% total tax. However, a user who purchased the item in Detroit would be subject to an additional 1% tax upon the storage or use of the item in Denver because section 53-92(c) only credits taxes paid to other municipalities. Thus, Denver's use tax could burden interstate commerce if every other state and municipality employed the same tax structure as Colorado and Denver, but imposed different tax rates.[24]

23. Most recently, the Supreme Court of the United States affirmed the highest court in Maryland's application of the internal consistency test.[25] In *Wynne,* Maryland residents complained about the fact that they received a credit against the Maryland state income tax for state income taxes paid in other states, but did not get a credit for those state taxes paid against Maryland's county taxes on the same income.[26] The Court of Appeals of Maryland undertook the same analysis undertaken by the Arizona Supreme Court

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[24] *Id.* at 70.

[25] *See Compt. of Treasury of Maryland v. Wynne*, 135 S. Ct. at 1807.

[26] *Id.* at 1793.

in *Arizona Dep't of Revenue*.[27] Using the "simple math" of the internal consistency test, the Maryland Court of Appeals determined that a multi-state taxpayer who was unable to obtain a full credit for the taxes paid in other jurisdictions had a net higher tax bill than a comparable resident with only Maryland income.[28]

24. The Supreme Court affirmed the Maryland Court of Appeals, holding that Maryland's failure to allow a credit for state income tax paid in other jurisdictions against Maryland's county income tax on the same income violated the dormant Commerce Clause because it failed the internal consistency test.[29] The Supreme Court stated that the "existing dormant Commerce Clause cases all but dictate the result reached in this case by Maryland's highest court."[30] Using the "simple math" of the internal consistency test and assuming that every State imposed taxes similar to Maryland's with a credit being limited to *state* taxes paid in other jurisdictions, the Supreme Court found that the interstate taxpayer would be subject to double taxation- having to pay an "extra" income tax to his resident state as well as the state in which he earned the income.[31]

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[27] *Id.*

[28] *Id.*

[29] 135 S. Ct. at 1794.

[30] *Id.*

[31] *Id.* at 1803.

25. Now, having reviewed the well-established dormant Commerce Clause jurisprudence and the analysis of the internal consistency test by other jurisdictions, including the United States Supreme Court, this Court finds that the present case reveals a similar internal inconsistency in the application of WV Use Tax without credit for local sales taxes paid as in the above-cited cases.

26. Consumers who use diesel fuel in West Virginia are subject to a 6% WV Use Tax, regardless of where purchased.[32]

27. Section 11-15A-10a provides for a credit for sales taxes paid to another jurisdiction for that same service or property up to the 6% rate. Section 11-15A-10a provides:

> A person is entitled to a credit against the tax imposed by this article on the use of a particular item of tangible personal property, custom software or service equal to the amount, if any, of sales tax lawfully paid to another state for the acquisition of that property or service.[33]

28. However, in states where the state sales tax rate is lower than 6%, but which exact a municipal and county sales tax in addition to a state sales tax, a consumer of diesel fuel who purchases the fuel outside West Virginia pays more than a similar in-state consumer of diesel fuel who purchases all of its

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[32] *See* W. Va. Code § 11-15A-13a(c)(1).

[33] W. Va. Code § 11-15A-10a.

fuel in West Virginia under the Department's interpretation of the credit statute. For example, in a state where there is 4% state sales tax and 2% county sales tax, a taxpayer pays a total of 6% sales tax on the purchase of diesel fuel in that state. If consumers are not given credit for local sales taxes paid, then the consumer purchasing diesel fuel out of state and paying an aggregate 6% sales tax will only get a West Virginia credit for the 4% state sales tax paid in the other jurisdiction. Thus, diesel fuel purchased outside but used inside West Virginia bears an additional 2% on diesel fuel comprised as follows: the 4% out of state sales tax plus the out of state 2% local county sales tax, plus 2% state portion of the WV Use Tax which is the 6% West Virginia rate less the credit for 4% out of state sales tax, for a total of 8%. Meanwhile, fuel purchased and consumed in West Virginia bears only the 6% WV Use Tax. In total, the consumer purchasing diesel fuel out of state and using it in West Virginia will pay more than a similar consumer purchasing in-state, when both consumers should only be paying a total 6% on fuel used in West Virginia.

29. Thus, like the tax schemes in *General Motors, Arizona Dep't of Revenue*, and *Wynne*, West Virginia's determination of a use tax credit without accounting for local taxes paid results in an internally inconsistent and a constitutionally suspect state tax structure. Unlike in *Wynne*, here, West Virginia does not impose a local tax. However, West Virginia's refusal to credit local taxes paid to other states results in the same outcome, *i.e.*, both states' taxing schemes favor either income derived

or fuel purchased within its borders. Under Maryland's scheme in *Wynne*, Maryland residents were discouraged from gaining income from other states. Under West Virginia's scheme, using the Commissioner's method, out of state businesses who use fuel in West Virginia are discouraged from purchasing fuel from states that collect local taxes. Accordingly, this Court finds that West Virginia must allow a use tax credit against the WV Use Tax for out of state local sales taxes paid, up to the 6% use tax credit, in order to comply with the dormant Commerce Clause.

Whether the OTA's Final Decision correctly analyzed the issue of whether Respondent is entitled to a use tax credit for sales taxes paid to cities, counties, or other localities of another state

30. Having found that failure to allow a use tax credit for sales taxes paid to other cities, counties, or localities of another state results in an internally inconsistent tax scheme, this Court finds that the OTA's Final Decision was correct in its analysis. Citing to the authority which this Court finds persuasive, this Court holds that the OTA's Final Decision did not contain any errors of law.

31. Furthermore, this Court does not agree with the Tax Commissioner that the OTA's Final Decision incorrectly analyzed the internal consistency test. As stated above, the internal consistency test is calculated by assuming that every state applies the offending tax scheme at issue to see if it results in subjecting an interstate

taxpayer to double taxation while a corresponding intrastate taxpayer pays less.[34] The Tax Commissioner sets forth an internal consistency calculation that is premised solely on the fact that West Virginia does not have a county use tax, but this is an incorrect application of the internal consistency test. Instead, the offending tax scheme is West Virginia's failure to allow a use tax credit under Section 11-15A-10a for sales taxes paid to localities, up to the 6% use tax credit, such that an interstate taxpayer pays more for the use of motor fuel in West Virginia. The fact that West Virginia does not have a county use tax has no relevance to the analysis of internal consistency under the *Complete Auto Transit* test because the use tax provision itself is not the offending provision; rather, it is the calculation of the use tax credit without a credit for local sales taxes paid that produces the resulting discriminatory effect on interstate commerce. The Tax Commissioner's attempt to apply the internal consistency test by ignoring this discrepancy because West Virginia imposes no local tax misses the mark. It misses the mark because the internal consistency test requires accounting for West Virginia tax scheme's failure to provide a credit a portion of another state's tax scheme. This Court finds the Tax Commissioner's argument in this regard unavailing.

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[34] *See, e.g.*, *Compt. of Treasury of Maryland v. Wynne*, 135 S. Ct. at 1802; *General Motors Corp. v. City and Cnty. of Denver*, 990 P. 2d at 69; *Ariz. Dept. of Revenue v. Ariz. Public Service Co.*, 934 P. 2d at 799.

32. The Tax Commissioner, as was recognized below by the OTA, offers no clear rebuttal to the internal inconsistency argument. The Tax Commissioner cites only Supreme Court cases that essentially affirm the viability of the internal consistency test as originally enunciated in *Complete Auto Transit.* For example, the Tax Commission places great reliance on *Armco Inc. v. Hardesty*, 467 U.S. 638 (1984) to suggest that its method of analyzing internal consistency is correct because the Respondent's assessment of internal consistency depends upon taxes imposed by other jurisdictions. But the Tax Commissioner misinterprets *Armco* and misinterprets the OTA's application of the internal consistency test. The OTA's application of the test does not require a court to examine other states' taxes. Rather, a court must suppose the subject state's tax structure was adopted by other states. As explained above, said application of the internal consistency test results in double taxation and disadvantages interstate commerce.

33. In conclusion, applying the internal consistency test to the case *sub judice* and assuming all states that do not impose local taxes also deny tax credits for local taxes paid in other states, the Court is of the opinion that such a scheme inherently discriminates against interstate commerce without regard to the tax policies of other states. As such, the Respondent is entitled to a use tax credit for sales taxes paid to cities, counties, or other localities of another state.

Whether the Tax Commissioner's application of the use tax credit satisfies the external consistency test

34. Having concluded that the State Tax Department's application of the use tax credit under Section 11-15A-10a must include a credit for local sales taxes paid to localities of other states, this Court finds it unnecessary to make any determination regarding the external consistency of the application of the use tax credit in this present case.[35]

DECISION

Applying the *Complete Auto Transit* test, this Court finds that the Tax Commissioner's application of the use tax credit under Section 11-15A-10a of the West Virginia Code is an unconstitutional violation of the dormant Commerce Clause. This Court further finds that the OTA's conclusion was well-founded, well-reasoned, and well-supported by persuasive case law. This Court finds that the legal conclusion in the Final Decision of the OTA is **AFFIRMED** and does **DENY** the instant *Petition.* This Court further **ORDERS** the parties to **JOINTLY SUBMIT** a calculation of the refund requested and the proper assessment for the three quarters of 2012 based upon the determination by this Court that Respondent is entitled to a use tax credit for sales taxes paid to cities, counties, and other localities of other states **WITHIN THIRTY-**

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[35] *Wynne*, 135 S. Ct. at 1805 (affirming decision of Maryland Court of Appeals after finding violation of internal consistency test).

DAYS of the entry of this Order. Once the parties have submitted their joint calculations, this Court does order that the above-styled appeal be **DISMISSED** and **STRICKEN** from the docket of this Court. The Clerk is DIRECTED to send a certified copy of this *Final Order* to the parties and counsel of record.

ENTERED this 24 day of August 2015.

/s/ Louis H Bloom
Louis H. Bloom, Judge

BEFORE THE WEST VIRGINIA OFFICE OF TAX APPEALS

CSX TRANSPORTATION, INC.,
Petitioner,

v.

GRIFFITH, CRAIG A., as **STATE TAX COMMISSIONER** of **WEST VIRGINIA**

AND

MATKOVICH, MARK W., as **ACTING STATE TAX COMMISSIONER of WEST VIRGINIA,**

Respondents[1]

DOCKET NOS. **12-477 RMFE**
13-278 M

ADMINISTRATIVE LAW JUDGE:
A. M. "Fenwick" Pollack
Chief Administrative Law Judge

PETITIONER'S COUNSEL:
James W. McBride, Esq.,
Nicki N. Nelson, Esq.,
John R. Fowler, Esq.

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[1] At the time Docket No. 12-477 RMFE was filed Craig A. Griffith was Tax Commissioner and when 13-278 M was filed Mark W. Matkovich was acting Tax Commissioner.

RESPONDENT'S COUNSEL:
Jan P. Mudrinich, Esq.

EVIDENTIARY HEARING HELD:
April 30, 2014
Charleston, WV

SUBMITTED FOR DECISION:
August 15, 2014

SYNOPSIS

TAXATION
SUPERVISION
GENERAL DUTIES AND POWERS OF COMMISSIONER; APPRAISERS

It is the duty of the Tax Commissioner to see that the laws concerning the assessment and collection of all taxes and levies are faithfully enforced. *See* W. Va. Code Ann. § 11-1-2 (West 2010).

TAXATION
WEST VIRGINIA TAX PROCEDURE AND ADMINISTRATION ACT COLLECTION OF TAX

"The Tax Commissioner shall collect the taxes, additions to tax, penalties and interest imposed by this article or any of the other articles of this chapter to which this article is applicable." W. Va. Code Ann. § 11-10-11(a) (West 2010).

TAXATION
USE TAX
IMPOSITION OF TAX; SIX PERCENT RATE; INCLUSION OF SERVICES AS TAXABLE; TRANSITION RULES; ALLOCATION OF TAX AND TRANSFERS

"An excise tax is hereby levied and imposed on the use in this state of tangible personal property, custom software or taxable services, to be collected and paid as provided in this article or article fifteen-b of this chapter, at the rate of six percent of the purchase price of the property or taxable services, except as otherwise provided in this article." W. Va. Code Ann. § 11-15A-2(a) (West 2014).

TAXATION
USE TAX
TAX ON MOTOR FUEL EFFECTIVE JANUARY 1, 2004

Computation of tax due from motor carriers.—*Every* person who operates or causes to be operated a motor carrier in this state shall pay the tax imposed by this section on the average wholesale price of all gallons or equivalent gallons of motor fuel used in the operation of a motor carrier within this state, under the following rules:(1) The total amount of motor fuel used in the operation of the motor carrier within this state is that proportion of the total amount of motor fuel used in a motor carrier's operations within and without this state, that the total number of miles traveled within this state bears to the total number of

miles traveled within and without this state. W. Va. Code Ann. § 11-15A-13a(c) (West 2014).

TAXATION
USE TAX
CREDIT FOR SALES TAX LIABILITY PAID TO ANOTHER STATE

(a) A person is entitled to a credit against the tax imposed by this article on the use of a particular item of tangible personal property, custom software or service equal to the amount, if any, of sales tax lawfully paid to another state for the acquisition of that property or service: *Provided,* That the amount of credit allowed does not exceed the amount of use tax imposed on the use of the property in this state. (b) For purposes of this section: (1) "Sales tax" includes a sales tax or compensating use tax imposed on the use of tangible personal property or a service by the state in which the sale occurred; and (2) "State" includes the District of Columbia but does not include any of the several territories organized by Congress. W. Va. Code Ann. § 1115A-10a (West 2014).

OFFICE OF TAX APPEALS
CONCLUSION OF LAW

There is no authority under West Virginia law to require motor carriers to prove how much fuel they used in other states prior to seeking a credit pursuant to West Virginia Code Section 11-15A-10a. Therefore, the Tax Commissioner's insistence on such proof was arbitrary and capricious, an error of law, and clearly wrong.

WEST VIRGINIA SUPREME COURT OF APPEALS CASE LAW

The United States Supreme Court has created a four part test to ascertain if a state taxing scheme violates the dormant Commerce Clause. The Court ruled that a tax that: (1) applies to an activity with a substantial nexus with the taxing state; (2) is fairly apportioned; (3) is not discriminatory towards interstate or foreign commerce; and (4) is fairly related to the services provided by the State, will pass muster. Complete Auto Transit Inc. v. Brady, 430 U.S. 274, 279, 97 S.Ct. 1076, 51 L.Ed.2d 326 (1977).

WEST VIRGINIA SUPREME COURT OF APPEALS CASE LAW

"A tax is valid under the Commerce Clause as a "compensatory tax" if the state imposes an intrastate tax such that the burdens imposed on interstate and intrastate commerce are equal. The taxpayer's out-of-pocket expenses determine whether the burdens are equal. Equal treatment for in-state and out-of-state taxpayers similarly situated is the condition precedent for a valid use tax on goods imported from out-of-state." Arizona Dept of Revenue v. Arizona Pub. Serv. Co., 188 Ariz. 232, 235, 934 P.2d 796, 799 (Ct. App. 1997)(intemal citations omitted).

OFFICE OF TAX APPEALS CONCLUSION OF LAW

The Tax Commissioner's denial to the Petitioner of a credit under West Virginia Code Section 11-15A-

10a for taxes other than state taxes paid to other states violates the internal consistency test of the dormant Commerce Clause. As such, his denial was arbitrary and capricious, an error of law, and clearly wrong.

FINAL DECISION

On October 19, 2012, the Fuel Tax Administration Unit of the Tax Account Administration Division of the West Virginia State Tax Commissioner's Office (Tax Commissioner or Respondent) issued a Refund Denial to the Petitioner. This denial notice denied the Petitioner's request for a refund of $907,230.88 in Motor Fuel Use Tax. On December 14, 2012, the Petitioner timely filed with this Tribunal, a petition for refund. Thereafter, on June 5, 2013, the Respondent's Auditing Division issued a Notice of Assessment against the Petitioner for motor carrier tax. The assessment was for the period January 1, 2010, through December 31, 2012, for tax in the amount of $1,560,032.96, and interest in the amount of $189,370.49, for a total assessed liability of $1,749,403.45. On August 2, 2013, the Petitioner timely filed with this Tribunal, a petition for reassessment. This Tribunal later consolidated these two matters. An evidentiary hearing was held on April 30, 2014, at the conclusion of which the parties filed legal briefs. The consolidated matter became ripe for a decision at the conclusion of the briefing schedule.

FINDINGS OF FACT

1. The Petitioner is a Virginia corporation with its principal place of business in Jacksonville, Florida. The Petitioner's business is rail transportation.

2. In October of 2010, an auditor with the West Virginia State Tax Department met with a representative of the Petitioner at one of their rail yards in West Virginia. The auditor characterized this meeting as a field audit. One of the results of this field audit was to set up the Petitioner as a fuel importer and to ensure that it began to pay tax on the fuel it was using in West Virginia.

3. Sometime afterwards, the Petitioner filed amended West Virginia Motor Fuel Use Tax Returns. In these amended returns the Petitioner was seeking a credit for sales taxes paid for locomotive fuel to cities, counties and other localities in states other than West Virginia. The Tax Commissioner determined that the Petitioner was not entitled to a credit for these taxes.

4. The process of carefully reviewing the amended returns revealed what the auditor and other Tax Department employees considered another problem within them, namely, the way the Petitioner was calculating the credit it was seeking for fuel taxes paid to other states, as opposed to cities, counties and other localities.

5. The revelation of this second perceived problem led an auditor to the Petitioner's principal

place of business to conduct another field audit. During this audit the auditor reviewed documents regarding fuel purchased in other states, taxes paid on that fuel and documents showing the miles traveled in these states. The auditor used this review to recalculate how the Petitioner established the amounts of credit it was entitled to for taxes paid on fuel in other states. The auditor determined that the Petitioner had impermissibly been seeking a credit for taxes paid to other states on fuel that was not consumed in West Virginia. It was this determination that led to the June 5, 2013, assessment.

DISCUSSION

Due to the somewhat complicated nature of how locomotive fuel is taxed, we believe that a simple explanation would be beneficial before we turn to the arguments of the parties. The Petitioner, like all Taxpayers in West Virginia, must pay a use tax on all items of tangible personal property it uses during the course of its business here. *See* W. Va. Code Ann. § 1115A-2(a) (West 2014). The personal property at issue in this matter is fuel in the Petitioner's locomotives. Obviously, no state, including West Virginia, stops locomotives when they cross the borders to figure out how much fuel has been used in the state. Instead, the Legislature has come up with a formula to measure the usage. That formula is contained in West Virginia Code Section 11-15A-13a.

> *Computation of tax due from motor carriers.*-- *Every* person who operates or causes to be

> operated a motor carrier in this state shall pay the tax imposed by this section on the average wholesale price of all gallons or equivalent gallons of motor fuel used in the operation of a motor carrier within this state, under the following rules:
>
> (1) The total amount of motor fuel used in the operation of the motor carrier within this state is that proportion of the total amount of motor fuel used in a motor carrier's operations within and without this state, that the total number of miles traveled within this state bears to the total number of miles traveled within and without this state.

W. Va. Code Ann. § 11-15A-13a(c) (West 2014).

At the evidentiary hearing in this matter the Petitioner introduced its exhibit 11, which sought to show how it applies the formula in Section 13a(c). The undersigned asked the witness to take the application of the formula a step further and apply it using simple math. This request led to the creation of Petitioner's Exhibit 12. Exhibit 12 used a fictional railroad with 10,000 miles of track nationwide and 1,000 miles of track in West Virginia, creating a 10% apportionment formula pursuant to Section 13a(c). From there, the witness calculated a fictional amount of fuel used nationwide, 200,000 gallons, and using the 10% apportionment formula found 20,000 gallons to have been deemed used in West Virginia. From there, for the most part, the Petitioner simply

applies the motor fuel tax rate to that 20,000 gallons deemed used, and pays the tax.[2]

It should be noted that the parties are in agreement regarding the process described immediately above, and how the Petitioner calculates its usage in West Virginia and pays use tax. The first disagreement between the parties concerns how the Petitioner seeks a credit for taxes paid on motor fuel purchased in other states. The ability to obtain such a credit is contained in West Virginia Code Section 11-15A-10a.

> (a) A person is entitled to a credit against the tax imposed by this article on the use of a particular item of tangible personal property, custom software or service equal to the amount, if any, of sales tax lawfully paid to another state for the acquisition of that property or service: *Provided,* That the amount of credit allowed does not exceed the amount of use tax imposed on the use of the property in this state.
>
> (b) For purposes of this section:
>
> (1) "Sales tax" includes a sales tax or compensating use tax imposed on the use of tangible personal property or a service by the state in which the sale occurred; and

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[2] There are some other calculations done by the Petitioner, such as accounting for the fuel imported into West Virginia that has already been taxed on the Petitioner's importer returns. However, these calculations are not relevant to our discussion here.

> (2) "State" includes the District of Columbia but does not include any of the several territories organized by Congress.

W. Va. Code Ann. § 11-15A-10a (West 2014).

The dispute between the parties concerns the gallons deemed used in West Virginia, and how many of those gallons were purchased in other states and taxed. The Petitioner had, for many years prior to this litigation, been calculating the credit from Section 10a the same way it calculated usage when paying the tax, by the apportionment formula. What the Petitioner would do is figure out how many taxable gallons it had purchased nationwide and multiply by the West Virginia apportionment formula. So, using the fictional scenario in Exhibits 11 & 12, out of the 200,000 gallons purchased, 5,000 would have been purchased in taxable states. Using the 10% apportionment factor, the Petitioner would end up with what it called 500 "taxable" or "taxed" gallons eligible for the credit in Section 10a.

The auditor who initially reviewed the Petitioner's returns and who conducted the two field audits felt that the Petitioner was calculating the credit incorrectly. The auditor was of the opinion that before the Petitioner could claim the credit in Section 10a, it would need to "prove" that the 500 gallons discussed above was actually used in West Virginia. During her field audit at the Petitioner's offices, she came up with her own methodology to figure out what the Petitioner had used. She did this by taking the six states where the Petitioner paid

tax on locomotive fuel (the 5,000 gallons in our fictional scenario above) and figured out their "usage" in those states. She arrived at the other six states usage by looking at how much fuel they purchased there versus how much fuel they "used" in those states. We have "used" in quotes because she obviously could not know how much fuel was used in those states. Instead, she apparently used an apportionment formula, total miles system wide versus total miles within the state. The bottom line to these calculations was the auditor informing the Petitioner that when it came time to obtain the credit in Section 10a, it could not have used the number of gallons it claimed to have used in West Virginia because it had already "used" those gallons in other states. It was this recalculation of how the Petitioner sought the Section 10a credit that led to the $1,749,403.45 assessment in this matter. At the evidentiary hearing and in post-hearing briefs the Tax Commissioner takes the position that it is axiomatic that you cannot use fuel in two different places and therefore the Petitioner must do the calculations the auditor did to prove what gallons are entitled to the Section 10a credit. We are unpersuaded by the Respondent's arguments for two reasons. First and foremost, as mentioned above, the parties are in agreement that the Petitioner is correctly using the apportionment formula in West Virginia Code Section 11-15A-13a when it is time to pay use tax. In plain English, using our fictional numbers, the Tax Commissioner has no problem with the Petitioner paying use tax on 20,000 gallons that are deemed to have been used in West Virginia. **But,** when it's time to obtain the credit, the Tax

Commissioner informs the Petitioner that it's deemed usage of 20,000 gallons is out the window. Instead, at the time of the credit a second formula is used, one that significantly lowers the Petitioner's fuel usage in West Virginia. Obviously, such a position is untenable. The Tax Commissioner cannot tell any Taxpayer, "we're going to use two amounts, when it's time to pay we'll use the higher amount, but when it's time for the credit, we'll go with the lower amount". Moreover, the Tax Commissioner has not provided this Tribunal with any authority supporting the methodology used by the auditor. The Legislature has created a formula to establish how much fuel is used in this state by motor carriers like the Petitioner. The Petitioner uses this formula both when paying the tax and when it seeks the credit. The Tax Commissioner cites no authority for deviating from this formula when calculating the credit in Section 10a.

The next argument between the parties concerns whether the Petitioner can obtain a Section 10a credit for taxes paid to cities, counties and other localities. The Tax Commissioner argues that the phrase, "paid to another state," in West Virginia Code Section 11-15A-10a *(supra)* means just what it says. The Petitioner advances a variety of arguments regarding its entitlement to the requested credits, including that the way the Tax Commissioner is applying Section 10a violates the dormant Commerce Clause. We agree with the Petitioner in this regard and therefore do not need to address the parties' other arguments regarding the phrase in question. The constitutional questions

addressed by the parties are well settled. The Commerce Clause of the United States Constitution gives Congress the power to regulate commerce. However, the courts, in particular the United States Supreme. Court, have created a body of law regarding the flip side of Congress' power to regulate commerce, namely the limitations on the individual states ability to regulate/hamper interstate commerce. This body of law is referred to as the dormant Commerce Clause. One of the standard bearer cases on the dormant Commerce Clause is Complete Auto Transit Inc. v. Brady, 430 U.S. 274, 97 S.Ct. 1076, 51 L.Ed.2d 326 (1977). The Complete Auto Court created a four part test to ascertain if a state taxing scheme violates the Clause. The Court ruled that a tax that: (1) applies to an activity with a substantial nexus with the taxing state; (2) is fairly apportioned; (3) is not discriminatory towards interstate or foreign commerce; and (4) is fairly related to the services provided by the State, will pass muster under the dormant Commerce Clause. Id, at 279.

The Petitioner claims that the Tax Commissioner's application of West Virginia Code Section 11-15A-10a violates prong two (and to some extent, three) of the Complete Auto test.[3] It specifically argues that the Tax Commissioner's

[3] We should point out that the Petitioner is not claiming that West Virginia Code Section 11-15-10a is unconstitutional, just that it is being applied to the Petitioner in an unconstitutional manner. As a result, this Tribunal is capable of ruling on this question without raising separation of powers questions. *See* Docket Nos. 12-192 RSW & 12-193 RSW.

application violates the "internal consistency" test, which was first discussed by the U.S. Supreme Court in the 1980's. *See e.g.* Container Corp. of Am. v. Franchise Tax Bd., 463 U.S. 159, 103 S. Ct. 2933, 77 L. Ed. 2d 545 (1983); Am. Trucking Associations, Inc. v. Scheiner, 483 U.S. 266, 107 S. Ct. 2829, 97 L. Ed. 2d 226 (1987); Tyler Pipe Indus., Inc. v. Washington State Dep't of Revenue, 483 U.S. 232, 107 S. Ct. 2810, 97 L. Ed. 2d 199 (1987); Goldberg v. Sweet, 488 U.S. 252, 109 S. Ct. 582, 102 L. Ed. 2d 607 (1989). The test states that "[T]o be internally consistent, a tax must be structured so that if every State were to impose an identical tax, no multiple taxation would result." Goldberg, at 261, 589. The Petitioner claims that it is subject to multiple taxation by its inability to obtain a credit, under Section 10a, for non-state taxes paid in other states.

The Petitioner relies on a variety of cases to discuss both the dormant Commerce Clause in general and how it believes the Tax Commissioner has violated it in this case. We believe two of the cases cited by the Petitioner provide helpful analysis. The first is Arizona Dep't of Revenue v. Arizona Pub. Serv. Co., 188 Ariz. 232, 934 P.2d 796 (Ct. App. 1997). There, an Arizona utility was using coal purchased in New Mexico and paying that state's gross receipts taxes, resources excise taxes and severance taxes for a total tax rate of 5.25%. When the utility sought a credit for these taxes the Arizona Department of Revenue allowed credit for the gross receipts taxes but not for the other taxes. The Court of Appeals of Arizona first discussed the jurisprudence of fair

apportionment under the Clause and the internal consistency test.

> State use taxes typically apply only to the use of goods purchased outside the taxing state and brought into it. A use tax thus inherently discriminates against interstate commerce. Nevertheless, such a tax is valid under the Commerce Clause as a "compensatory tax" if the state imposes an intrastate tax such that the burdens imposed on interstate and intrastate commerce are equal. The taxpayer's out-of-pocket expenses determine whether the burdens are equal. Equal treatment for in-state and out-of-state taxpayers similarly situated is the condition precedent for a valid use tax on goods imported from out-of-state.

Arizona Dep't of Revenue v. Arizona Pub. Serv. Co., 188 Ariz. 232, 235, 934 P.2d 796, 799 (Ct. App. 1997)(internal citations omitted). After this analysis, the Court just used simple math to explain its ruling that the Arizona Department of Revenue had violated the internal consistency test. If an Arizona company bought coal in Arizona it would pay a 5% sales tax. By Arizona's refusal to provide a credit for all of the taxes paid, the utility at the center of the litigation ended up paying a total of 5.25% in taxes for the same amount of coal, hence the violation of the test.

Interestingly, in footnotes, both parties discuss a recent case from Maryland. We say interestingly for two reasons, first the dueling footnotes, indicating that neither party finds the case to be highly

determinative, secondly because in May of 2014, the U.S. Supreme Court granted certiorari. Despite the fact that it is an income tax case, we find Comptroller of the Treasury of Maryland v. Wynne, 431 Md. 147, 64 A.3d 453 (2013) cert. granted, 134 S. Ct. 2660, 189 L. Ed. 2d 208 (U.S. 2014) to be as helpful to our determination as Arizona Dep't of Revenue. In Wynne, Maryland residents had complaints similar to those of the utility in Arizona. These residents were entitled to a credit against the Maryland state income tax for taxes paid on income generated in other states; however they were not entitled to a credit against Maryland's county taxes on that same income. The Court of Appeals of Maryland undertook an analysis almost identical to that undertaken in Arizona. It created two fictional Maryland residents, one who earned $100,000 solely in Maryland and one who earned $50,000 in Maryland and $50,000 in Pennsylvania. Before any credits, both owed identical amounts of Maryland income tax. Again, simple math showed that the resident with multi-state income who was not able to obtain a credit against all the taxes paid in Pennsylvania had a net tax bill higher than the comparable resident, with another corresponding violation of the internal consistency test and the Clause. We find the Wynne case to be determinative precisely because it is a quite recent, clear and cogent analysis of the internal consistency test. We find it interesting because the U.S. Supreme Court granted certiorari.

In their initial brief, the Petitioner connects the dots in similar fashion to the Wynne and Arizona

Dept of Revenue Courts and creates two fictional entities using fuel in this state, one having purchased the fuel in West Virginia and one purchasing fuel elsewhere. Once again, simple math shows that under the Tax Commissioner's application of West Virginia Code Section 11-15A-10a, the company purchasing fuel in states with taxes other than just state taxes will pay more for using the same product in West Virginia.[4]

The Tax Commissioner offers no clear rebuttal to the Petitioner's argument in this regard, merely stating that "[T]he Constitutionality of West Virginia's law cannot depend upon taxes imposed by other jurisdictions." *See* "West Virginia State Tax Commissioner's Reply to Petitioner's Post-Hearing Brief." p. 8. The Tax Commissioner cites Armco Inc. v. Hardesty, 467 U.S. 638, 104 S. Ct. 2620, 81 L. Ed. 2d 540 (1984) as standing for this proposition. What the Armco Court actually said was "[A]ny other rule would mean that the constitutionality of West Virginia's tax laws would depend on the shifting complexities of the tax codes of 49 other States, and that the validity of the taxes imposed on each taxpayer would depend on the particular other States in which it operated". Id, at 644-45, 2623-24. The "rule" the Armco, Court was

[4] The math is so simple we feel no need to clutter the decision with it. Using fictional numbers, if two West Virginia motor carriers travel identical miles and both use a gallon of fuel, one of the gallons purchased in West Virginia and the other purchased in a state with a 4% state sales tax and 2% county tax the carrier using the fuel in West Virginia will pay 6% and the other carrier will pay 6% to the other state but only obtain a credit of 4% with an ensuing extra out of pocket expense of 2%.

speaking of was the internal consistency test and the decision reaffirmed the Court's acceptance of it. To the extent the Tax Commissioner relies on Armco for the proposition that West Virginia need not worry about the taxing schemes in other states, we disagree. In actuality, the Armco Court did exactly what the courts in Maryland and Arizona would do many years later, it applied simple math to compare the tax bills of identically situated Taxpayers. In Armco, like Wynne and Arizona Dep't of Revenue unequal tax bills violated the internal consistency test and therefore, the dormant Commerce Clause.

In summation, we are aware that the U.S. Supreme Court will be hearing the Wynne case in the near future and that the scope of the dormant Commerce Clause may well change. However, as the law of the United States stands today, we are of the opinion that the Tax Commissioner has applied West Virginia's use tax to the Petitioner here in a manner that violates the dormant Commerce Clause because its application is not fairly apportioned and discriminates against interstate commerce.

CONCLUSIONS OF LAW

1. It is the duty of the Tax Commissioner to see that the laws concerning the assessment and collection of all taxes and levies are faithfully enforced. *See* W. Va. Code Ann. §11-1-2 (West 2010).

2. "The Tax Commissioner shall collect the taxes, additions to tax, penalties and interest imposed by this article or any of the other articles of

this chapter to which this article is applicable." W. Va. Code Ann. § 11-10-11(a) (West 2010).

3. "An excise tax is hereby levied and imposed on the use in this state of tangible personal property, custom software or taxable services, to be collected and paid as provided in this article or article fifteen-b of this chapter, at the rate of six percent of the purchase price of the property or taxable services, except as otherwise provided in this article." W. Va. Code Ann. § 11-15A-2(a) (West 2014).

4. *Computation of tax due from motor carriers.--Every* person who operates or causes to be operated a motor carrier in this state shall pay the tax imposed by this section on the average wholesale price of all gallons or equivalent gallons of motor fuel used in the operation of a motor carrier within this state, under the following rules: (1) The total amount of motor fuel used in the operation of the motor carrier within this state is that proportion of the total amount of motor fuel used in a motor carrier's operations within and without this state, that the total number of miles traveled within this state bears to the total number of miles traveled within and without this state. W. Va. Code Ann. § 11-15A-13a(c) (West 2014).

5. (a) A person is entitled to a credit against the tax imposed by this article on the use of a particular item of tangible personal property, custom software or service equal to the amount, if any, of sales tax lawfully paid to another state for the acquisition of that property or service: *Provided,*

That the amount of credit allowed does not exceed the amount of use tax imposed on the use of the property in this state. (b) For purposes of this section: (1) "Sales tax" includes a sales tax or compensating use tax imposed on the use of tangible personal property or a service by the state in which the sale occurred; and (2) "State" includes the District of Columbia but does not include any of the several territories organized by Congress. W. Va. Code Ann. § 11-15A-10a (West 2014).

6. There is no authority under West Virginia law to require motor carriers to prove how much fuel they used in other states prior to seeking a credit pursuant to West Virginia Code Section 11-15A-10a. Therefore, the Tax Commissioner's insistence on such proof was arbitrary and capricious, an error of law, and clearly wrong.

7. The United States Supreme Court has created a four part test to ascertain if a state taxing scheme violates the dormant Commerce Clause. The Court ruled that a tax that: (1) applies to an activity with a substantial nexus with the taxing state; (2) is fairly apportioned; (3) is not discriminatory towards interstate or foreign commerce; and (4) is fairly related to the services provided by the State, will pass muster. Complete Auto Transit Inc. v. Brady, 430 U.S. 274, 279, 97 S.Ct. 1076, 51 L.Ed.2d 326 (1977).

8. "A tax is valid under the Commerce Clause as a "compensatory tax" if the state imposes an intrastate tax such that the burdens imposed on

interstate and intrastate commerce are equal. The taxpayer's out-of-pocket expenses determine whether the burdens are equal. Equal treatment for in-state and out-of-state taxpayers similarly situated is the condition precedent for a valid use tax on goods imported from out-of-state." Arizona Dep't of Revenue v. Arizona Pub. Serv. Co., 188 Ariz. 232, 235, 934 P.2d 796, 799 (Ct. App. 1997)(internal citations omitted).

9. The Tax Commissioner's denial to the Petitioner of a credit under West Virginia Code Section 11-15A-10a for taxes other than state taxes paid to other states violates the internal consistency test of the dormant Commerce Clause. As such, his denial was arbitrary and capricious, an error of law, and clearly wrong.

DISPOSITION

WHEREFORE, it is the final decision of the West Virginia Office of Tax Appeals that the Petitioner's refund request for $907,230.88. of Motor Fuel Use Tax should be and hereby is **GRANTED** and that the assessment, issued on June 5, 2013 for motor carrier taxes for a total liability of $1,749,403.45 is hereby **VACATED.**

WEST VIRGINIA OFFICE OF TAX APPEALS

By: /s/ A. M. "Fenway" Pollack
A. M. "Fenway" Pollack
Chief Administrative Law Judge

Date Entered: 1/25/15

APPEAL PROCEDURES

Any aggrieved party may appeal from this decision with an appropriate West Virginia circuit court within sixty days of the date of service of the decision in accordance with the procedure set forth at West Virginia Code Section 11-10A-19. The Office of Tax Appeals may not be named as a party to the appeal, but must be provided with a copy of the filed petition for judicial review.

West Virginia Code Section 11-10A-19(e) also provides that if the appeal is of an assessment, except a jeopardy assessment for which security in the amount thereof was previously filed with the Tax Commissioner, then within ninety days after the petition for appeal is filed, or sooner if ordered by the circuit court, the petitioner shall file with the clerk of the circuit court a cash bond or a corporate surety bond approved by the clerk.

Within fifteen (15) days after receipt of this written notice of the appeal from the appellant, or within such further time as the circuit court may allow, the West Virginia Office of Tax Appeals will prepare and transmit to the circuit court a certified copy of the entire record in the matter. The West Virginia Office of Tax Appeals will, at the time of transmittal to the Circuit Court: (1) send to the parties a detailed index of the record; (2) send to the appellant a bill, payable within thirty days, for the reasonable costs of preparing the record; and (3) upon payment of such record preparation costs, send to the parties a certified copy of the entire record. Information about this procedure is available in the

Rules of Practice of Procedure before the West Virginia Office of Tax Appeals, at W.Va. C.S.R. § 121-1-86.