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February 16, 2021

The Honorable Bill Ferguson
Senate President
Maryland General Assembly
H-107 State House
Annapolis, Maryland 21401
Via email

Re: Senate Bill 787, "Digital Advertising Gross Revenues Tax – Exemption and Restriction"

Dear President Ferguson:

You asked for advice about SB 787. The bill, among other things, prohibits "[a] person who derives gross revenues from digital advertising services in the State" from "directly pass[ing] on the cost of the tax imposed …to a customer who purchases the digital advertising services by means of a separate fee, surcharge, or line-item." You asked whether the prohibition is legal. As discussed below, I believe the bill is legally sufficient and constitutional.

The prohibition in SB 787 is essentially a ban on the direct charging of a specific fee by the provider of digital advertising services to purchasers of those services. In another context, the Supreme Court has upheld a prohibition on the passing along of a specified tax. *See Exxon Corp. v. Eagleton*, 462 U.S. 176, 194-95 (1983). The state law at issue in that case prohibited a severance tax on oil producers from being passed on to their purchasers. The Court found that despite that the pass through prohibition impacted existing contractual obligations, the provision did not violate the Contract Clause because the statute "did not prescribe a rule limited in effect to contractual obligations or remedies, but instead imposed a generally applicable rule of conduct designed to advance 'a broad societal interest'" of "protecting consumers from excessive prices…" *Id.* at 191. Accordingly, the effect on existing contracts was "incidental to its main effect of shielding consumers from the burden of the tax increase." *Id.*

The Court in *Eagleton* also rejected an equal protection challenge to the pass-through prohibition. The Court explained that when analyzed "under the lenient

standard of rationality that this Court has traditionally applied in considering equal protection challenges to regulation of economic and commercial matters[,]" the "pass-through prohibition plainly bore a rational relationship to the State's legitimate purpose of protecting consumers from excessive prices." *Id*. at 196.

I also considered whether the prohibition is a taking under the State or federal constitution. A pass through prohibition would amount to an unconstitutional taking only if the prohibition makes it impossible for the entity to profitably engage in its business or maintain commercial viability. The Fifth Amendment of the U.S. Constitution and Article III, § 40 of the Maryland Constitution "prohibit the taking of private property for public use without the payment of just compensation to the property owner." *King v. State Roads Commission*, 298 Md. 80, 84 (1983). *See also Keystone Bituminous Coal Ass'n v. DeBenedictis*, 480 U.S. 470 (1987)(clarifying that the two factors that are 'integral parts" of a takings analysis are the nature of the government interest in question and the extent of the diminution of value of investment backed expectations). In *Keystone*, the Court confirmed that a taking does not occur unless the government regulation makes the business being regulated "commercially impracticable." *Id*. at 495 - 96. Accordingly, unless the prohibition prevents the digital ad services provider from recouping its business costs in a commercially viable manner, the prohibition does not amount to an unconstitutional taking.

Further, I considered whether the prohibition on passing on the digital ad tax violates the First Amendment. The Supreme Court has previously opined that a state law that prohibited a merchant imposing a surcharge on a customer using a credit card rather than paying by cash, check, or similar means was a restriction on the speech of the merchant because in application it regulated how the merchant communicated its prices. *See Expressions Hair Design v. Schneiderman*, 137 S. Ct. 1144 (2017). The issue in that case was that the law did not actually prohibit a merchant from charging more to credit card users; rather, as applied, it prevented a "single-sticker" method of pricing. A single-sticker method posts one price but indicates a credit card user may pay more. After reasoning that the law imposed a restriction on speech, the Court remanded the case to the lower court to determine the applicable First Amendment standard.[1]

After remand, in answering a certified question from the federal circuit court, the state's highest court explained that a merchant is in compliance with the state law at issue

> if and only if the merchant posts the total dollars-and-cents price charged to credit card users. In that circumstance, consumers see the highest possible price they must pay for credit card use and the legislative

[1] Applicable First Amendment tests for commercial speech are either the one outlined in *Central Hudson Gas & Elec. Corp v. Public Serv. Comm'n*, 447 U.S. 557 (1980), which applies intermediate scrutiny, or the lesser standard articulated in *Zauderer v. Office of Disciplinary Counsel*, 471 U.S. 626 (1985), which concerns disclosure requirements.

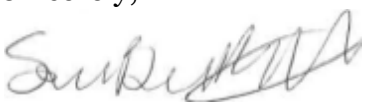
> concerns about luring or misleading customers by use of a low price available only for cash purchases are alleviated. To be clear, plaintiffs' proposed single-sticker pricing scheme – which does not express the total dollars-and-cents credit card price and instead requires consumers to engage in an arithmetical calculation, in order to figure it out – is prohibited by the statute.

Expressions Hair Design, 32 N.Y.3d 382, 393-94 (2018). Thus, the state law in question would fall within the consumer disclosure type laws.

In contrast, the prohibition in SB 787 is not a restriction on speech, in my view. It does not matter what the digital ad services provider calls it, the digital ad tax simply cannot be directly passed on to the purchaser of those services. As a result, SB 787 is prohibiting conduct. Therefore, it is akin to other prohibited fees. *See*, *e.g.*, Real Property Article, § 8A-402 (mobile home park fees); Commercial Law Article, § 12-405(a)(3), § 12-808 (finder fees); Financial Institutions Article, § 12-918 (debt management services).

In conclusion, I believe the prohibition in SB 787 is legally sufficient and constitutional.

Sincerely,



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