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To: Members of the Senate Budget and Taxation Committee

From: DeAndre Morrow, Legislative Committee, Tax Council

Date: January 29, 2020

Subject: **Senate Bill 2 – "Digital Advertising Gross Revenues – Taxation"**

Position: **Oppose**

The Maryland State Bar Association ("MSBA") opposes **Senate Bill #2 – Digital Advertising Gross Revenues – Taxation** (the "Bill").

By way of background, the Bill imposes a new tax on businesses providing "digital advertising services" in Maryland. The Bill defines "digital advertising services" to include "advertisement services on a digital interface, including advertisements in the form of banner advertising, search engine advertising, interstitial advertising and other comparable advertising services." A business provides digital advertising services if either of the following conditions are met: the digital advertising services appear on the device of a user:

(1) with an Internet Protocol Address that indicates that the user's device is located in Maryland; or

(2) who is known or reasonably suspected to be using the device in Maryland.

If either of these conditions are met, the Bill imposes the tax on a business's "annual gross revenues," defined as "income or revenue from all sources, before any expenses or taxes, computed according to generally accepted accounting principles," delivered from digital advertising services in Maryland.

The Bill, as drafted, likely violates the Internet Tax Freedom Act (the "ITFA"). In 1998, Congress enacted the ITFA to prohibit state and local governments from imposing "multiple or discriminatory taxes on electronic commerce."[1] The ITFA specifically defines what constitutes a "discriminatory tax." "Discriminatory tax" is defined to include "any tax imposed by a State . . . on electronic commerce that . . . is not generally imposed and legally collectible by such State . . . on transactions involving similar property, goods, services, or information accomplished

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[1] Pub. L. No. 105-277, Title XI, 112 Stat. 2681 (1998) (enacted as a statutory note to 47 U.S.C. § 151); ITFA § 1101(a). Certain provisions of ITFA were subsequently amended by legislation enacted in 2004 and 2007. See Pub. L. No. 108-435, 118 Stat. 2615 (2004); Pub. L. No. 110-108, 121 Stat. 1024 (2007). All references to the ITFA in this testimony refer to the ITFA in its current form, unless specifically stated otherwise.

Hon. Keith R. Truffer, President | Dana O. Williams, President-Elect | Deborah L. Potter, Secretary | Hon. Mark F. Scurti, Treasurer | Victor L. Velazquez, Executive Director

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through other means. . . ."[2] "Electronic commerce" is defined as "any transaction conducted over the Internet or through Internet access, comprising the sale, lease, license, offer, or delivery of property, goods, services, or information. . . ."[3] If a transaction is generally not taxed when it is conducted through traditional commerce, the ITFA bars a state from taxing a similar transaction when conducted through e-commerce.

If enacted as currently drafted, the Bill would impose a tax on digital advertising services, while not imposing the tax on similar non-digital advertising services. For example, tax could be imposed on the annual gross revenues derived from the advertising of an item on a website, but tax would not be imposed on annual gross revenues derived from the advertising of that same item in magazines or on billboards. This discriminatory treatment is precisely what the plain language of ITFA prohibits. The scenario created by the Bill is eerily similar to the facts in an Illinois State Supreme Court case regarding the legality of a nexus provision that applied to remote sellers who advertised via website but not remote sellers who advertised through traditional commerce (e.g., mail order catalogs, telephone sales, etc.). In *Performance Marketing Association v. Hamer*, Illinois amended a law to require out-of-state internet retailers to collect tax if they had a contract with a person in Illinois who displayed a link on a website that connected an Internet user to that remote seller's website.[4] The taxpayer argued that if it used any advertising method other than the Internet, it would not have an obligation to collect and remit tax on its sales.[5] But for the taxpayer's use of the Internet, there was no collection obligation on its sale. The Illinois Supreme Court found that this law violated ITFA because a tax collection obligation existed only on the party engaged in electronic commerce.[6] The remedy in this case was to declare the amendment "void and unenforceable."[7] If enacted as currently drafted, the Bill may share the same fate.

For the reason(s) stated above, the MSBA **opposes the Bill and urges an unfavorable Committee report**.

If you have questions, please contact DeAndre Morrow at Dmorrow@ReedSmith.com or MSBA's Legislative Office at (410)-269-6464 / (410)-685-7878 ext: 3066 or at Richard@MSBA.org and Parker@MSBA.org**.**

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[2] ITFA § 1105(2)(A)(I).
[3] ITFA § 1105(3).
[4] 998 N.E.2d 54 (Ill. 2013).
[5] *Id*. at 58.
[6] *Id*. at 59.
[7] *Id* at 60.