Patrick J. Reynolds
Senior Tax Counsel
(202) 484-5218
preynolds@cost.org

January 29, 2020

Senate Budget and Taxation Committee
Maryland General Assembly

Re: In Opposition to Senate Bill 2, Digital Advertising Tax

Dear Chair Guzzone, Vice Chair Rosapepe, and Members of the Committee,

Thank you for the opportunity to submit testimony on behalf of the Council On State Taxation (COST) in opposition to Senate Bill 2, which would impose a gross receipts tax on revenues derived from digital advertising services in the State. This new, controversial, and untested tax would put Maryland at a competitive disadvantage with respect to encouraging businesses to maintain or expand their operations in the State. A similar tax at the international level has already garnered negative reaction and the threat of retaliation from the U.S. Treasury. The digital advertising tax represents unsound tax policy and violates several core tax policy principles—transparency, fairness, and economic neutrality. The tax could also violate the Permanent Internet Tax Freedom Act and several provisions of the U.S. Constitution.

About COST

COST is a nonprofit trade association based in Washington, DC. COST was formed in 1969 as an advisory committee to the Council of State Chambers of Commerce and today has an independent membership of approximately 550 major corporations engaged in interstate and international business. COST's objective is to preserve and promote the equitable and nondiscriminatory state and local taxation of multijurisdictional business entities.

COST's Position on Gross Receipts Taxes and Taxation of Business Inputs

The COST Board of Directors has adopted a formal policy statement opposing both Gross Receipts Taxes and the Sales Taxation of Business Inputs. While the position on business inputs primarily concerns the states' sales taxes, its logic would also apply to this digital advertising tax, which is essentially a gross receipts tax on business inputs. COST's policy positions are:

Gross receipts taxes are widely acknowledged to violate the tax policy principles of transparency, fairness, economic neutrality and competitiveness; generally, such taxes should not be imposed on business.[1]

[1] https://www.cost.org/globalassets/cost/state-tax-resources-pdf-pages/cost-policy-positions/grossreceiptstaxes.pdf

Imposing sales taxes on business inputs violates several tax policy principles and causes significant economic distortions. Taxing business inputs raises production costs and places businesses within a State at a competitive disadvantage to businesses not burdened by such taxes. Taxes on business inputs, including taxes on services purchased by businesses, must be avoided.[2]

Senate Bill 2 represents bad tax policy and violates several tax policy principles—transparency, fairness, and economic neutrality.

- *Transparency.* A transparent tax, like the sales tax on consumer purchases, is obvious to the taxpayer, and its economic effects are easily understood. A gross receipts tax on digital advertising, on the other hand, is a stealth tax that will affect Maryland residents in several unseen ways. The tax will impact residents as purchasers, by imposing hidden taxes and thus making the products they purchase more expensive, and as workers, by depressing investment and thus reducing wages and employment opportunities. Taxing business inputs unfairly hides the true cost of government services by embedding a portion of the sales tax in the final price of goods and services.
- *Fairness.* A fair tax treats similarly situated taxpayers similarly. A gross receipts tax on digital advertising is unfair in that it would impose a significant tax burden on only a small segment of businesses with no relationship to the ability to pay. Businesses are already subject to myriad taxes that are not based on ability to pay—property tax, sales tax, unemployment insurance tax, etc.—another tax should not be added to that list.
- *Economic Neutrality.* An economically neutral tax does not influence business choices (of location, of operational entity, of suppliers, etc.). The gross receipts tax on digital advertising will force companies to either pass their increased costs on to consumers or reduce their economic activity in the State in order to remain competitive with other companies who do not bear the burden of such taxes.

Adopting a Widely Criticized French Approach to Taxing Digital Companies

The Maryland digital advertising tax is a modified version of the French Digital Services Tax which has been widely condemned by both the U.S. government and businesses operating in global markets. Similar to the French tax, the Maryland tax singles out a small number of digital companies for punitive taxation. In the case of Maryland, many of these companies are already subject to the state corporate income tax and there is no rational basis for imposing an additional discriminatory tax solely on digital businesses. If Maryland were to enact the digital advertising tax, it would be the only state in the nation to have such a tax, drawing significant unfavorable attention to the state's business climate.

Potential Violation of Federal Law and Constitution

Finally, a gross receipts tax on digital advertising services, if enacted, would be immediately embroiled in protracted litigation. Since the new tax would apply to digital advertising but not to non-digital advertising, the law would likely violate the federal Permanent Internet Tax Freedom Act. The bill also raises several constitutional questions, including whether the tax

---

[2] https://www.cost.org/globalassets/cost/state-tax-resources-pdf-pages/cost-policy-positions/sales-taxation-of-business-inputs.pdf

would violate the First Amendment, Equal Protection, and Commerce Clauses.

Conclusion

For the foregoing reasons, COST strongly urges members of the committee to please vote “no” on Senate Bill 2.

Respectfully,

Patrick J. Reynolds

cc: COST Board of Directors
Douglas L. Lindholm, COST President & Executive Director