American Advertising Federation of Baltimore
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March 2, 2020

WRITTEN TESTIMONY TO HOUSE WAYS AND MEANS COMMITTEE
RE: HOUSE BILL 1628: Sales and Use Tax – Rate Reduction and Services

FROM:
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TO:

Delegates Luedtke, B. Barnes, D.E. Davis, M. Jackson, Kaiser, McIntosh, and Washington

Members of the Ways and Means Committee

Dear Members of the Ways and Means Committee:

On February 20, 2020, Delegates Luedtke, B. Barnes, D.E. Davis, M. Jackson, Kaiser, McIntosh, and Washington introduced House Bill 1628 (HB1628) titled “Sales and Use Tax - Rate Reduction and Services.” In summary, the bill calls for:

> Altering the definitions of "taxable price" and "taxable service" for the purposes of certain provisions of law governing the sales and use tax to impose the tax on certain labors and services; altering the rate of the sales and use tax; altering the percentage of gross receipts from vending machine sales and from certain sales of dyed diesel fuel to which the sales and use tax is applied; altering the rate of the sales and use tax applied to certain charges made in connection with sales of alcoholic beverages; etc.

On behalf of our members and partners throughout the Baltimore Metropolitan area, the American Advertising Federation of Baltimore, oppose this bill.

HB 1628 hobbles a key economic engine in Maryland.

Maryland's ad industry helps generate more than $100B in economic activity (APPENDIX I). If this bill is passed in its current form, this will have a deleterious impact on it. Unlike many service industries in Maryland, advertising agencies clientele isn't relegated to the state borders. We must compete for both local and out-of-state clients against with out-of-state agencies. A services tax would hobble Maryland agencies, forcing them to make the impossible decision of choosing to absorb the 5% to avoid pricing themselves out of the market or trying to pass it through to a client who willingly chooses to pay 5% more if they don't have to.

HB 1628 erases profits for advertising and marketing agencies, stifling growth.

Average agency net profit margins in 2019 average just under 6% (APPENDIX II) according to CSIMarket. In effect, a 5% service tax could cut the profit margin of the average agency by more than 80%. Besides meaning less money in the pockets of those in agencies who benefit from profit sharing bonuses, this would lead to instability. With less profit as a buffer, agencies risk becoming. And those that do manage to weather significantly reduced profits will operate far more conservatively when it comes to innovation, growth, and hiring.

And that's a best-case scenario, because it assumes Maryland ad agencies will continue winning business at the same rate after this tax is enacted. The reality is, it won't — not when clients are consistently seeking (and finding) value in a market that includes agencies from Philadelphia, DC, New York, and Delaware.

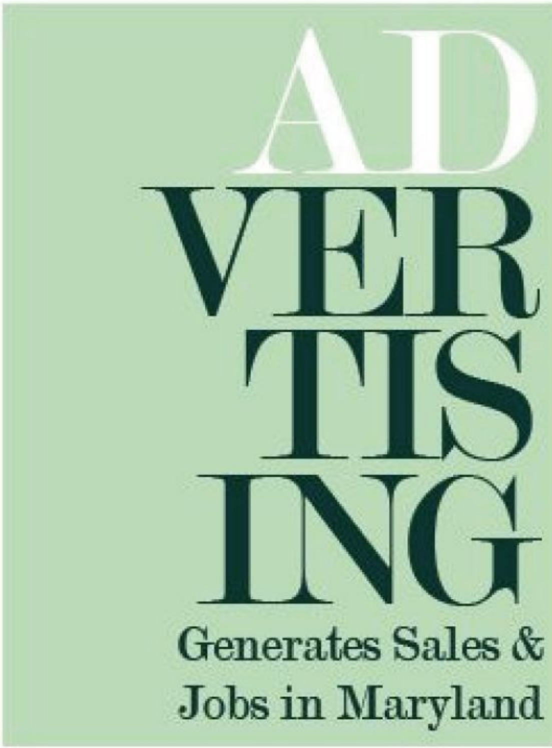
HB 1628 puts agencies at a disadvantage, even in our own state.

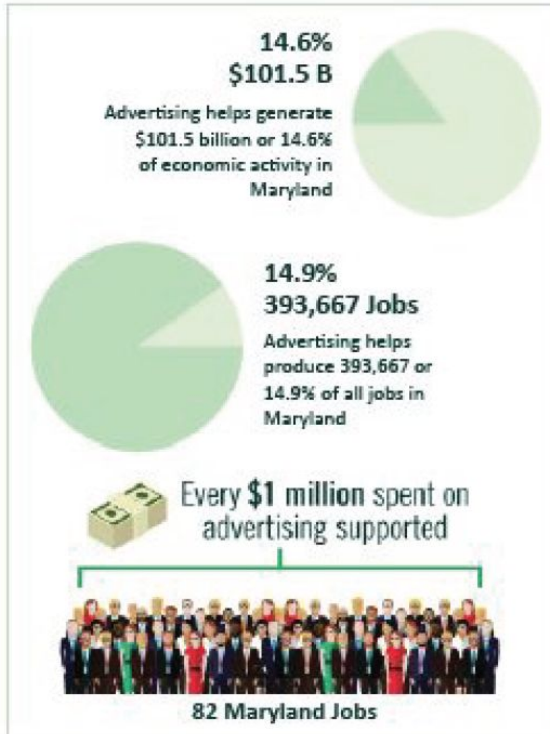
The disadvantage of the tax is magnified further by the procurement processes many potential clients (including state agencies) use in choosing an agency to work with. Procurement decisions are often weighted heavily on the estimates provided by candidates. A 5% difference in proposal estimates between a field of competing agencies may be the difference between winning the work and coming in third place.

And then the ultimate betrayal: Many Maryland state contracts don't have a mandate to choose Maryland advertising and marketing agencies. Based on our earlier observations about procurement practices, this could mean that Maryland will choose out-of-state agencies to fulfill their needs more often, but even favor them.

For these reasons, we urge the committee to issue an unfavorable report on HB 1628.

APPENDIX I – 2019 Impact of Advertising in Maryland from IHS Economics and Country Risk Research





Advertising is a powerful engine that helps drive the economy of Maryland. Advertising expenditures account for $101.5 billion of economic output or sales in Maryland – that is 14.6% of the $693.1 billion in total economic output in the State. Sales of products and services that are driven by advertising help support 393,667 jobs, representing 14.9% of the 2.6 million jobs in Maryland.

Every million dollars spent on advertising in Maryland supports 82 jobs across industries throughout the state. Every direct advertising job also supported 33 other jobs across all industries. Each form of advertising, from print media and radio and television to the Internet, helps businesses efficiently communicate the benefits of their products and services to target audiences.

This profile illustrates the importance of advertising to the economy of Maryland. It is drawn from the latest research in a landmark series of studies prepared for The Advertising Coalition by IHS Economics and Country Risk. IHS uses methodologies developed by Dr. Lawrence R. Klein, recipient of the 1980 Nobel Prize for Economics, as the foundation for this research.

The IHS research measures the impact of advertising spending by quantifying how much the spending stimulates sales, employment, value-added (contribution to GDP), taxes, and labor income. For example, while the agriculture and mining industries may have few direct advertising jobs, their combined economic sectors support many industries that do advertise heavily.

Maryland's economy and the U.S. economy are heavily affected by the health of the consumer sector. The consumer sector represents 68% of the U.S. economy and it continues to expand. For example, while the agriculture industry does little advertising, the food, manufacturing, and retail industries advertise heavily across the country. This creates consumer demand for a chain of products and services from sales of farm machinery to the shipment of agricultural products.

U.S. advertisers in 2014 spent $297 billion on advertising to stimulate consumer demand, and that spending launched a "multiplier effect" throughout the economy. Total advertising expenditures drove $5.8 trillion in total sales. This represents 16% of the $36.7 trillion in total U.S. sales attributable to advertising and means that every dollar of ad spending stimulates almost $19 in sales activity. Just as significant, the total impact of advertising on the U.S. economy represents 19% of U.S. GDP. Every million dollars that is spent on advertising supports 67 American jobs across a range of industries, and every advertising job supports 34 jobs across other industries. Labor income supported by advertising represents 17% of all personal and proprietor income in the U.S.

APPENDIX II – 2019 Advertising Industry Profitability, CSIMarket - accessed February 28, 2020 (https://csimarket.com/Industry/industry_Profitability_Ratios.php?ind=901)

Advertising Industry Net Margin Statistics

Net Margin Comment

Advertising Industry Net Profit grew by **89.07 %** in 4 Q 2019 sequntially, while Revenue increased by **17.01 %**, this led to improvement in Advertising Industry's Net Margin to **10.67 %**, above Advertising Industry average Net Margin.

On the trailing twelve months basis Net margin in 4 Q 2019 grew to **5.98 %**.

Within **Services sector** 4 other industries have achieved higher Net margin. Net margin total ranking has deteriorated compare to previous quarter from to 33.

Net Margin Statistics

High	Average	Low
11.52 %	2.42 %	-8.28 %
4. quarter 2019		3. quarter 2015