



**March 7, 2024**

House Committee on Ways and Means  
Room 131  
House Office Building  
Annapolis, MD 21401

**RE: HB 1372, “Health and Taxation - Digital Social Media Services and the Mental Health Care Fund for Children and Youth” (Unfavorable)**

Dear Chair Atterbeary and Members of the House Committee on Ways and Means:

On behalf of the Computer & Communications Industry Association (CCIA), I write to respectfully oppose HB 1372 in advance of the House Committee on Way and Means hearing on March 7, 2024.

CCIA is an international, not-for-profit trade association representing a broad cross-section of communications and technology firms.<sup>1</sup> Proposed regulations on the interstate provision of digital services therefore can have a significant impact on CCIA members. CCIA holds a firm conviction that children are entitled to a higher level of security and privacy in their online experiences and understand and support the General Assembly seeking to invest resources to support children and youth access to mental health services.

However, under HB 1372, a “digital social media service” would be subject to a tax on annual gross revenues, ranging from 5% of the assessable base for the lowest threshold (annual gross revenues of \$500 million to \$1 billion) up to 10% under the highest defined bracket (gross revenues above \$10 billion). This raises a variety of legal and policy concerns, as further detailed below.

**HB 1372 conflicts with Federal law and is likely to lead to costly litigation.**

The tax proposed under HB 1372 conflicts with the Federal Internet Tax Freedom Act (ITFA) which prohibits states from imposing “discriminatory taxes on electronic commerce”. Given that HB 1372 only targets a tax to a “digital social media service”, it is clear that the bill’s provisions are likely to only target online business activities in a way that cannot be applied to offline activities, and therefore falls under the scope of a “discriminatory tax”.

As you know, in 2021, Maryland enacted the “Digital Advertising Gross Revenues Tax”, first-in-the nation legislation to impose a tax on digital advertisements. Since its enactment, the law has been challenged at both the state and federal levels. In October 2022, a Maryland state court<sup>2</sup> struck down the law citing several instances in which it is unconstitutional, which also appear similarly applicable with the proposed tax under HB 1372. First, the court ruled

<sup>1</sup> For more than 50 years, CCIA has promoted open markets, open systems, and open networks. CCIA members employ more than 1.6 million workers, invest more than \$100 billion in research and development, and contribute trillions of dollars in productivity to the global economy. A list of CCIA members is available at <https://www.ccianet.org/members>.

<sup>2</sup> *Comcast v. Comptroller of Maryland*, No. C-02-CV-21-000509 (Md. Cir. Ct. 2022).

that the law violates the ITFA by imposing a discriminatory tax on online advertising services, but not traditional offline advertisements. Second, the ruling stated that the law also violates the Commerce Clause as the digital advertising tax imposes greater tax liability to businesses that participate in interstate commerce and maintain an out-of-state presence.

As such, Maryland’s “Digital Advertising Gross Revenues Tax” has been tied up in litigation since its enactment. At a time when Maryland is facing a significant budget shortfall of around \$760 million<sup>3</sup>, it would be imprudent to advance legislation that is likely to face a similar costly fate.

## HB 1372 will harm innovation and business growth.

HB 1372 violates multiple of the basic economic principles that should guide tax policy design. The guiding star of tax policy is that revenue should be raised in an efficient manner. Imposing taxes tends to create incentives that distort behavior and produce deadweight losses for the economy, so taxes should be designed to minimize the size of deadweight losses and harmful distortions. To this end, well-designed taxes are usually neutral and broad-based, generally avoid marginal tax rate “cliffs,” and usually focus on income/profits rather than intermediate flows like revenue. HB 1372 fails on all three counts.

HB 1372 is a targeted tax that aims to collect taxes from a relatively small number of taxpayers in a specific industry. It is designed with a non-neutral, narrow tax base that creates inefficiencies and incentivizes costly efforts to avoid the tax. This is a significant general failure of the tax proposal in the bill.

HB 1372 also violates the common-sense tax design prescription against “cliffs” in marginal tax rates. “Cliffs” that result in sudden surges in the effective marginal tax rate for tiny increases in revenue are a policy design disaster. They incentivize all kinds of inefficient behavior to avoid sudden surges in tax burdens, and may even drive businesses out of the jurisdiction imposing the “cliff.”

Specifically, the structure of the proposed tax under HB 1372, while seemingly targeted to larger and higher-profit businesses, would result in penalizing other smaller and growing businesses for exceeding certain revenue thresholds. For example, if a Maryland-based startup’s revenue increases from \$499,999,999 to \$500,000,000, the startup would face a whopping \$25 million in tax liability associated with just one extra dollar of additional gross global revenue—the first “cliff” in the bill. That is a 2.5 billion percent marginal tax rate on the last dollar earned, and a major disincentive to grow businesses in Maryland.

HB 1372 bill is designed with two *additional* “cliffs” at the \$1 billion revenue threshold and the \$10 billion revenue threshold. For startups with limited capital “runway,” creating enormous tax burdens for crossing arbitrary growth thresholds can be ruinous.

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<sup>3</sup> “Budget crunch presents early test of Moore administration” Maryland Matters (Dec. 18 2023), <https://www.marylandmatters.org/2023/12/18/budget-crunch-presents-early-test-of-moore-administration/#:~:text=Maryland%20faces%20a%20%24761%20million,from%20declining%20sales%20tax%20collections.>



Such “cliffs” in effective marginal tax rates create enormous incentives for companies to avoid crossing relevant thresholds, which may lead to behavior that is extremely inefficient from companies operating in Maryland, and may even drive startups out of Maryland.

Finally, the tax base for HB 1372 is on *revenues* rather than *profits* or *income* which is the case for most taxes in the United States and other advanced OECD countries. Taxes on revenues hit firms with thin profit margins much harder than highly profitable firms with wide margins. In particular, taxes on revenues tend to be terrible for startups that are still growing, as many such startups are not yet profitable (and may even be pre-monetization) and are operating on a fixed capital runway.

In combination, the tax design failures of HB 1372 would generate enormous inefficiencies for Maryland consumers and businesses, and would make Maryland much less appealing for startups.

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We appreciate your consideration of our comments and stand ready to provide additional information as the General Assembly considers proposals related to technology policy.

Sincerely,

Khara Boender  
State Policy Director  
Computer & Communications Industry Association