Daniel Rohn
Manager of Internal Audits
Comptroller of Maryland
80 Calvert Street, Room 409A
Annapolis, MD 21401
Sent Electronically

Comments on Proposed Digital Advertising Tax Regulations under COMAR 03.12.01

Dear Mr. Rohn:

The Association of National Advertisers (the "ANA") and the co-signed groups are pleased to submit this comment letter in response to the Comptroller of Maryland's proposal to adopt new regulations .01 through .06 under Code of Maryland Regulations ("COMAR") Section 03.12.01 (the "Proposed Regulations"), which aim to provide guidance on the Digital Advertising Gross Revenues Tax (the "Tax").

The mission of the ANA is to drive growth for marketing professionals, brands and businesses, the industry, and humanity. The ANA serves the marketing needs of 20,000 brands by leveraging the 12-point ANA Growth Agenda, which has been endorsed by the Global CMO Growth Council. The ANA's membership consists of U.S. and international companies, including client-side marketers, nonprofits, fundraisers, and marketing solutions providers (data science and technology companies, ad agencies, publishers, media companies, suppliers, and vendors). The ANA creates Marketing Growth Champions by serving, educating, and advocating for more than 50,000 industry members that collectively invest more than $400 billion in marketing and advertising annually.

We believe that the Tax is invalid for a variety of reasons. It is preempted by the Internet Tax Freedom Act ("ITFA") and violates ITFA's moratorium on discriminatory taxes on electronic commerce, because it imposes a discriminatory tax on advertising services provided over the Internet, while not imposing a tax on similar advertising services through other means.[1] In addition, we believe that the progressive rate structure of the Tax discriminates against interstate commerce in violation of the Commerce and Due Process Clauses of the U.S. Constitution. The tax rate applied to a taxpayer's digital advertising revenue apportioned to Maryland is determined based on the taxpayer's global gross revenue from digital advertising services. Consequently, a taxpayer that derives most of its revenue from digital advertising revenue from Maryland sources will be subject to Tax at a lower effective rate on its digital advertising revenue apportioned to Maryland than a taxpayer that has the same amount of digital advertising revenue apportioned to Maryland but derives a substantial portion of its digital advertising revenue on a national or global basis. Further, singling out one kind of speech (i.e., digital adverting) is a demonstrable violation of the First Amendment. These issues regarding the validity of the Tax are in the process of being resolved in the Courts.

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[1]   Internet Tax Freedom Act, §§ 1101(a)(2), 1105(2), P.L. 105-277, as amended

While we believe that there is a great likelihood that it will eventually be determined that the Tax violates the U.S. Constitution and/or the ITFA, we acknowledge that the Comptroller has an obligation to attempt to enforce the Tax. Our submission of these comments should not be misconstrued as an acceptance of the Tax's validity but rather an attempt to inform the consideration of the Proposed Regulations at this time. The Proposed Regulations fail to produce a workable compliance framework. In fact, the vagueness of some portions of the Proposed Regulations creates a significant risk that they will be applied in a manner that will violate the constitutional requirement of fair apportionment. Clear administrative guidance is essential in the case of the Tax because, unlike virtually every other tax administered by the Comptroller, the Tax's statutory regime fails to provide an administrative remedy to recover an erroneously or mistakenly paid tax.

1. Insufficient Definitions

The definitions included in the Proposed Regulations are vague and, in some cases, circular. Without clearer definitions, the apportionment methodology set forth in the Proposed Regulations will be unworkable.

    a. Proposed COMAR 03.12.01(B)(1) defines "access" to mean "the transmittal, display, embedding, or other availability to a user for viewing or interaction."

        i. This definition will create uncertainty and lead to administrative challenges because it is unclear whether access requires actual interaction with digital advertising (*e.g*., viewing and/or clicking-through). Without clarification, this definition could be read to include the mere potential to reach a device (*e.g*., purchasing a banner-ad on a website that a user might view). An expansive and/or vague definition of "access" will make it impossible for taxpayers to apply the "location" definition and will produce an apportionment percentage that has no reasonable relationship to the manner in which revenue from digital advertising services is earned.

    b. Proposed COMAR 03.12.01(B)(2) is a verbatim recitation of the statute's circular definition of "digital advertising services." Specifically, the term "includes advertisement services on a digital interface, including advertisements in the form of banner advertising, search engine advertising, interstitial advertising, and other comparable advertising services."

        i. This definition fails to define or provide any explanations as to the meaning or scope of critical terms such as "advertisement" or "advertising" services – the very items upon which the tax is imposed.

        ii. This definition fails to clarify what should be considered "other comparable advertising services."

    c. Proposed COMAR 03.12.01(B)(4) defines "location" as "the actual, physical location of a digital interface when a digital advertising service is accessed by a user."

i. This definition fails to address the mobile nature of many devices that are used to access digital advertising services. The physical location of a device may change multiple times over the course of a day, potentially crossing jurisdictional boundaries. This is especially likely with respect to devices in Maryland, which shares land boundaries with four other states and the District of Columbia. In addition, in many cases, the physical location of a device may have no connection to the location of the "user" or the person deriving revenue from digital advertising services.

d. Proposed COMAR 03.12.01(B)(5) defines a "user" to mean "an individual or any other person who accesses a digital interface with a device."

i. This definition will create uncertainty and lead to administrative challenges because it includes persons other than individuals (*i.e.*, legal entities that are often treated as persons under the law) within the scope of "users." This raises questions of how the physical location of access to digital advertising services through devices controlled by legal entities is to be determined. For example, will all digital advertising services accessed through a computer network controlled by a legal entity be sourced to a single location or will they be sourced to the location of the individuals using the network? In addition, treating a legal entity as a user may lead to a distorted apportionment, because access by a device controlled by a legal entity would be treated the same as access by a device controlled by an individual, notwithstanding that individuals in multiple locations may access digital advertising services through a single device controlled by a legal entity.

e. Proposed COMAR 03.12.01(B)(6) defines a "device" to mean "any medium through which digital advertising services may be accessed, including stationary or portable computing devices, tablets, phones, and smart devices."

i. This definition fails to explain what constitutes a "smart device." As more devices and machines are designed to access the Internet, the concept of a "smart device" could capture many objects (e.g., home appliances and automobiles) which are unlikely to be used to access digital advertising services.

ii. This definition is also circular, to the extent that it uses the word "devices" in defining the term "device."

2. Reliance on Device Location is Inconsistent With Statute

The statute imposing the Tax mandates that the apportionment fraction used to determine a taxpayer's annual gross revenue derived from digital advertising services in Maryland is to be a ratio of "annual gross revenues … derived from digital advertising services in the State" over "annual gross revenues … derived from digital advertising services in the United States." However, the Proposed Regulations have replaced the above noted revenue-based formula with one that is based on the location of devices. There is no reason to expect that a taxpayer's

revenue from digital advertising services will be directly related to the location of devices accessing such services.

3.   Unclear Sourcing Guidance

    a. Proposed COMAR 03.12.02(B)(3) provides that devices whose location are indeterminate shall be excluded from both the numerator and denominator of the apportionment factor. This "throwout" rule has the potential to produce a distorted apportionment factor. Apportioning all of a taxpayer's digital advertising revenue by reference to less than all of the devices accessing those services is, by its nature, distortive. This distortion is likely to be exaggerated because, for many taxpayers, the location of many of the devices accessing the digital advertising services will be indeterminate. In addition, for some taxpayers, this throwout rule creates the possibility of a factor with a zero denominator.

    b. Proposed COMAR 03.12.02(C) seeks to require a taxpayer to determine the location of a device using the totality of the "technical information and the terms of the underlying contract for digital advertising services" within the taxpayer's possession or control. This approach will create uncertainty and lead to multiple challenges for the following reasons:

        i.   Providers of digital advertising services in many cases do not have direct access to technical data on device location and will not be able obtain access to such data without incurring significant additional cost.

        ii. Many of the sources of technical data referenced in the Proposed Regulations will not produce results that accurately reflect user location (e.g., location data for a "user" that utilizes a virtual private network ("VPN") with servers located in various domestic and international locations could inaccurately reflect the user's location). A taxpayer would have no way to confirm the veracity of the data.

        iii. Obtaining accurate location data for users involves privacy issues. Because many software and application providers allow users to opt out of location tracking in order to protect their privacy, information may well not be available.

        iv. Where the various sources of technical data produce different conclusions regarding device location, taxpayers with access to multiple sources of technical data may, to their legal jeopardy, find themselves subject to alternative interpretations by the Comptroller regarding device location.

        v.   The Proposed Regulations fail to explain how the location of a device is to be determined under the "terms of an underlying contract" and how the location determined under the "terms of an underlying contract" relates to a different location determination based on technical data.

vi. The Proposed Regulations fail to provide adequate guidance or safe harbors for approximating the location of devices to avoid situations where the source of digital advertising revenue is unavailable or ambiguous.

c. Proposed COMAR 03.12.02(D) requires the location of each device to be determined by a totality of the facts and circumstances to be either: (1) within Maryland; (2) not within Maryland, but within the United States; (3) not within the United States; or (4) indeterminate.

i. The Proposed Regulations will create uncertainty and lead to administrative or legal challenges because they fail to clarify what constitutes "indeterminate."

4. Declaration of Estimated Tax

Proposed COMAR 03.12.06 seeks to require a taxpayer who "reasonably expects" to owe Tax of more than $1 million for a calendar year to file a declaration of estimated Tax in the form and manner prescribed by the Comptroller. This approach will create uncertainty and lead to administrative or legal challenges for the following reasons:

a. It fails to provide a standard for what constitutes a reasonable expectation of owing the Tax.

b. The vagueness of this provision will likely result in taxpayers unnecessarily filing declarations. It also may result in taxpayers being penalized for failing to file declarations despite good faith efforts to comply.

5. Economic Impacts

We disagree strongly with the finding by the Comptroller that the Proposed Regulations will have no economic impact on small business. The Tax and, thus, the Proposed Regulations will clearly fall heavily on small businesses already struggling to emerge from the economic difficulties imposed by the pandemic. In addition, businesses and the state will be forced to expend substantial sums to contest the many legal issues raised by the Tax and the Proposed Regulations in the courts. Consequently, we believe that platforms burdened with the Tax and compliance with the Proposed Regulations will experience greater costs, some of which will impact small businesses in the form of higher prices.

We appreciate your consideration of these comments and welcome the opportunity to continue to discuss these matters which are so important to our members.

Respectfully submitted,

Dan Jaffe
Group Executive Vice President,
Government Relations
Association of National Advertisers (ANA)

Chris Oswald
Senior Vice President, Government
Relations
Association of National Advertisers (ANA)

Clark Rector
Executive Vice President, Government
Affairs
American Advertising Federation

Thomas Goodwin
Vice President, Government Affairs
Exhibitions & Conferences Alliance

Cailey Locklair
President
Maryland Retailers Association

Angela Miele
Vice President, State Government Affairs
and Tax Policy
Motion Picture Association