Earlier today, the Maryland legislature passed H.B. 732, which proposes a first of its kind Digital Advertising Gross Revenues Tax. The legislature also passed H.B. 932, which would expand Maryland’s sales tax to sales of digital products (both downloads and streaming). The bills will now be sent to Governor Hogan for signature or veto. If he vetoes H.B. 732, as expected, it will return to the General Assembly for the legislature to attempt to override the veto.

**Background:**

Lawmakers rushed to consider legislation before the legislature adjourned today due to COVID-19 concerns. The House passed H.B. 732 on March 12th and the Senate passed the bill on March 17th by a margin of 29-16. H.B. 732 was then sent back to the House for consideration of the Senate’s amendments. Earlier today, the House concurred with the Senate’s amendments and passed the bill by a margin of 88-47.

**Digital Advertising Gross Revenues Tax:**

H.B. 732 proposes a new tax on the annual gross revenues derived from digital advertising services in Maryland. The definition of “digital advertising services” broadly 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.”

The tax rate varies from 2.5% to 10% of the annual gross revenues derived from digital advertising services in Maryland, depending on a taxpayer’s global annual gross revenues. To be required to pay the tax, a taxpayer must have at least $100,000,000 of global annual gross revenues and at least $1,000,000 of annual gross revenues derived from digital advertising services in Maryland.

Determining whether digital advertising taxes are “in Maryland” is problematic. The introduced version of the digital advertising tax proposed to source (and tax)
digital advertising services to Maryland based on either: (1) a user’s IP address; or (2) the knowledge or reasonable suspicion that a user is using its device (which receives the advertising) in the state. However, the final version of the tax strikes these provisions and instead uses an undeveloped apportionment fraction to apportion the tax to Maryland. The legislation directs the Comptroller to adopt regulations that will entirely determine how to source digital advertising service revenues to the state.

House Debate:

Multiple delegates made a last ditch effort today to derail the bill and expressed their disapproval of the digital advertising tax. The delegates argued:

- The tax revenue would come from Maryland residents;
- The digital advertising tax would violate federal law; and
- The revenues from the proposed digital advertising tax will not support Maryland’s public education reforms because the tax will be tied up in court for years and possibly be found invalid.

What’s Next:

The bill will now head to Governor Hogan, and he has thirty days upon presentment to veto the bill, sign it into law, or allow the bill to become law without his signature. Governor Hogan has been very vocal against any tax increases, and he is expected to veto the legislation. Even if the legislation is vetoed, the General Assembly could override the veto by a three-fifths vote of both chambers’ members. The legislature adjourned sine die today, March 18th, but a special legislative session is tentatively scheduled for the end of May. The lawmakers would then consider any vetoes by the governor.

Eversheds Sutherland Observation: If the bill is enacted, legal challenges will follow. The tax likely violates federal and constitutional law, including the Permanent Internet Tax Freedom Act and the Commerce Clause of the United States Constitution.
Turning now to the numbers, the Maryland Senate has 47 representatives and the House of Delegates has 141 representatives. Lawmakers need 29 out of 47 members in the Senate and 85 out of 141 members in the House of Delegates to override the expected veto. Thus, either 19 members in the Senate or 57 members in the House would be required to sustain the veto.

As H.B. 732 passed with three-fifths support of each chamber, some lawmakers would need to change their mind regarding the new taxes imposed under this bill to defeat a veto override. Given the current economic climate, lawmakers may return to Annapolis with a change of heart in May, as the burdens of these taxes are likely to fall ultimately on Maryland’s small businesses and consumers who are already being hit hard by the struggling economy.

The Eversheds Sutherland SALT Team will continue to follow the Maryland Digital Advertising Gross Revenues Tax and provide updates.

If you have any questions about this legal alert, please feel free to contact any of the attorneys listed under Related People/Contributors or the Eversheds Sutherland attorney with whom you regularly work.