

## Blog Post

# What's Next For Maryland's Digital Advertising Tax?

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Maryland's controversial Digital Advertising Gross Revenues Tax (the Digital Ad Tax) recently shot back to the top of the headlines when Maryland Circuit Court Judge, Alison Asti, ruled from the bench that the tax is unconstitutional and violates the federal Internet Tax Freedom Act (ITFA). Judge Asti ruled in favor of Verizon and Comcast that the Digital Ad Tax violates the ITFA, the First Amendment and the Commerce Clause due to its selective taxation, and the fact that it is not content neutral.

The Digital Ad Tax disrupted the industry in early 2021 when the Maryland Senate controversially passed the country's first-of-its-kind digital advertising tax in the form of a gross receipts tax on large advertisers ([e.g., large tech companies](#)). The Digital Ad Tax was implemented in the face of strong opposition from all sides, and the law was immediately challenged in both federal and state courts. Despite widespread criticism and multiple legal attacks, Maryland elected to push ahead with enforcing the Digital Ad Tax.

While last week's ruling was welcome news for many (and the impacted digital advertising community, in particular), it is likely that Maryland will appeal the ruling, so the ultimate fate of the Digital Ad Tax remains uncertain. Nonetheless,

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businesses should consider the broad potential impact if this ruling stands.

### Future of the Digital Ad Tax

Pending the results of an eventual appeal, one key question is whether Maryland will attempt to tailor the Digital Ad Tax in an effort to cure its legal defects. Maryland is reportedly reviewing its options following the ruling, but there are some indications that Maryland officials have lost some confidence in their position. For instance, the Maryland Comptroller recently questioned the constitutionality of the Digital Ad Tax, suggesting that the upcoming election could impact its future. Whether the state would announce meaningful changes to the Digital Ad Tax before the litigation is fully resolved is unclear.

### Impact on Previously Filed Returns

Despite the immediate backlash following the law's passing, and the series of lawsuits filed to dispute the validity of the Digital Ad Tax, Maryland nonetheless proceeded with requiring timely filing and payment obligations, starting April 15, 2022. Thus, at this point, at least some payments have likely been made under the new legislation. Companies will need to evaluate whether to file for a refund or wait until a final determination. Those who wait must be mindful of the deadline for filing a claim for refund, if the litigation persists for several years.

Further, companies need to decide how to handle filing and payment for future periods while the case remains unresolved. There are a number of different strategies to consider. Of course, a lot of the ambiguity could be removed if the Maryland Comptroller issues temporary guidance while any appeal of this ruling is pending. Whether it will do so remains to be seen.

### Effect on Other States with Similar Proposed Legislation

Many states (and some cities), have been closely monitoring the fate of the Maryland law to determine whether to move forward with their own digital advertising taxes, and how closely to emulate Maryland's model. This ruling could have significant impact on other jurisdictions' appetite for imposing this tax, and states could decide to halt proposed legislation or alter the approach to taxing this revenue, to avoid falling into the same traps of the Digital Ad Tax. This ruling may serve as a cautionary tale for state legislatures as they consider future tax legislation.

## Reach of the ITFA

One key aspect of the ruling is that the Judge specifically held that the Digital Ad Tax violated the ITFA, a federal law that prohibits discrimination against electronic commerce. The Judge ruled that the law taxed only digital advertising, and did not impose a similar tax on traditional (non-digital) print advertising.[1] The fact that the Judge struck down the law on these grounds is significant, as it adds fuel to the fire in the currently pending federal case brought by the U.S. Chamber of Commerce, which also challenged the law on both constitutional and ITFA grounds.

It is unclear at this stage how the Maryland state court ruling will impact the pending federal case, which has not yet been decided, as this decision did not address all of the issues raised in that case (for instance, the U.S. Chamber of Commerce also challenged the constitutionality of the pass-through prohibition, which prohibits advertisers from passing on the cost of the Digital Ad Tax to their customers on an invoice, and that issue remains open). However, we can expect the Judge's ruling to be used by the Chamber to bolster its arguments for striking down the Digital Ad Tax.

The ruling could also spur more cases using the ITFA as a basis for striking down other digital taxes. If the Digital Tax Act is ultimately determined to

violate the ITFA, could other digital taxes also fall to this same fate? Income and sales taxes directed at digital companies could also be ripe for challenge under the ITFA. As companies increase their digital presence, the ITFA will continue to be an important component of legal challenges to digital taxes.

Thus, critics of the Digital Ad Tax got a big win with last week's ruling, but the future of the Digital Ad Tax remains uncertain in Maryland and elsewhere, as the Digital Ad Tax continues to yield more questions than answers.

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[1] Of note is a parallel case in South Dakota in which the state already taxes print advertising under its gross receipts tax.

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