4A's ADVOCACY TALENT IMPACT
What you need to compete.

November 8, 2021

Submitted via email to drohn@marylandtaxes.gov

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

RE: Request for Public Comments on Proposed Regulations under COMAR 03.12.01.01 to 03.12.01.06

Dear Mr. Rohn,

The 4A's provides the following written comments to the Maryland Comptroller's proposed action to adopt regulations .01 through .06 under COMAR 03.12.01 Digital Advertising Tax.

<u>Who We Are</u>

The 4A's was established in 1917 to promote, advance, and defend the interests of our member agencies, employees, and the advertising and marketing industries overall. Today the organization serves more than 600 member agencies across 1,200 offices, which help direct more than 85% of total U.S. advertising spend.

Advertising is a significant contributor to the U.S. economy. By providing consumers with information on products and services, advertising fuels economic growth through its ability to support competitiveness. 2015 research from the IHS Economics & Country Risk found that advertising contributed $3.4 trillion to the U.S. GDP in 2014, comprising 19 percent of the nation's total economic output. Sales of products and services stimulated by advertising supported 20 million jobs, or 14 percent of the total jobs in the country. In addition to directly contributing to the U.S. economy through direct spending, the advertising industry itself is also a major U.S. employer, with over 316,800 American professionals employed in advertising, promotions, and marketing management positions at a median pay of $141,490 per year in May 2020.[1]

Digital advertising has become the financial foundation of most of the free services that people across the U.S. and the world utilize at little or no cost. News sites, online social networks, email services, weather websites, and video and entertainment platforms are primarily funded through online advertising, with national brands and advertisers contributing significant funding to these public services.

Collaborating closely with their nationwide and global advertiser clients, 4A's members are a critical part of the digital advertising ecosystem, serving as the creative visionaries and business strategists behind how digital ads resonate with and effectively reach consumers.

I. Digital Advertising Taxes Are Discriminatory And Counter To Economic Growth

Maryland policy makers' decision to specifically target digital advertising for additional taxes creates an imbalance in the advertising ecosystem, penalizing one type of advertising strategy over another. For Maryland-based and national advertising agencies with specialization in digital advertising and video advertising production, this creates a significant business disadvantage when compared to agencies serving more traditional print advertising, radio advertising, transit billboards, and other non-digital advertising media.

Because businesses strategically utilize advertising to help drive their own revenue growth, targeting the digital advertising industry as a means for pure revenue generation is also bad policy. In fact, we have seen before how imposing state advertising taxes to generate revenue has failed in other states. Florida, Arizona, and Iowa all enacted advertising taxes in the past; however, they learned shortly thereafter that these taxes were counterproductive to economic growth and quickly repealed the laws. Robust studies by the Wharton Econometrics Forecasting Associates found that a tax on advertising reduces local employment and personal income by substantial amounts. When the cost of advertising goes up (due to new taxes), there is less advertising, which lessens the amount of consumer demand for the products or services being advertised. This impedes the economy as a whole, reduces collected sales tax on

[1] Bureau of Labor Statistics, U.S. Department of Labor, Occupational Outlook Handbook, Advertising, Promotions, and Marketing Managers,
at https://www.bls.gov/ooh/management/advertising-promotions-and-marketing-managers.htm (visited October 05, 2021).

products sold due to advertising, significantly curtails its usefulness to the government as a source of revenue.

In 1987, the Florida legislature enacted a five percent tax that covered all advertising distributed in Florida - on local and national television and radio, and in newspapers and magazines - as well as other services provided by other professions. As a result of the tax, many advertisers reduced their media expenditures, including in the state's top six media markets; national spot-TV advertising declined an average of 11.8 percent within six months of the imposition of a sales tax on advertising.

Not surprisingly, the state abandoned this tax on advertising within a year in order to try to reverse its ill-effects on state businesses and ad-supported media. State officials estimated that Florida lost $35 million in convention business and tens of millions of dollars in advertising as a result of this tax.[2] These revenue losses translated into significant jobs lost and economic hardship for business sectors that rely on ad supported funding.

The timing of this new digital advertising tax is also particularly difficult as many agencies made the strategic decision to pivot their business models during COVID-19 into more digital focused advertising strategies. Agencies prosper when advertisers spend - any disincentive to reduce advertising spending, particularly in the ever-growing digital space, hurts agencies and advertisers.

II. <u>More Clarification Needed To Prevent Pass-Through Of The Tax To Small Businesses</u>

The 4A's worries about the possibility of indirect pass-through taxation. While there is language prohibiting direct pass-through taxation, it is still unclear if this tax can be passed on as something other than a fee or surcharge, such as new location-specific pricing models that do not overtly tack on additional price increases or fees due to the new tax. Large platforms have very complex and differing pricing models that are attuned to individual country's advertising markets; therefore, large platforms could conceivably develop different pricing structures for different U.S. states that have enacted or will enact digital advertising taxes in the future.

[2] "Associated Press. "Florida to Repeal Controversial Tax on Services." *The Los Angeles Times Archives*, 11 Dec. 1987, https://www.latimes.com/archives/la-xpm-1987-12-11-mn-19003-story.html. Accessed 2 Nov. 2021.

To shield smaller businesses (and their affiliated agency partners) from any direct pricing surges associated with implicit tax pass-throughs, Maryland's proposed digital advertising regulations should include additional clarity. While SB 787 prohibits direct add-on fees or additional surcharges as an attempt to prevent digital ad tax pass throughs to small businesses, current proposed regulations do not enumerate how these measures will be enforced by the Comptroller's office.[3]

Recognizing that a more direct price control approach would be impossible to implement and enforce, the Maryland Comptroller must do all that it can to ensure that the real-world implementation of this new tax does not inadvertently harm the small businesses that have come to rely on digital advertising to attract new customers and fuel their post-pandemic recovery.

III. Disadvantage To Maryland Residents And Agencies

Within the state, Maryland advertising agencies are critical partners in the development and deployment of digital advertising for national brands. Often, local agencies, both independent and the local offices of large agency holding companies, have the best understanding of local or in-state consumer markets, the strongest relationships with local publishers, media outlets, and influencers, and significant overall knowledge of the competitive landscape for certain industries within a state or metropolitan region.

Because of this specific competitive advantage, national brands or local businesses will hire these local agencies at higher rates for advertising campaigns targeted at Maryland-specific audiences. For Maryland agencies, the market effects of this new tax, especially if combined with the addition of other state digital advertising taxes, will be a serious agency job killer and force agencies to reassess their pricing models, and business strategies to pivot to a different world, less reliant on digital advertising, and one where the cost of advertising is not artificially inflated by unnecessary taxes.

As currently written in HB 0732 and in the proposed regulations, digital advertising taxpayers will face higher taxes in Maryland when they earn more total revenue, regardless of where their revenue is earned. To address the higher cost of doing business in the state due to these higher

[3] SB 787, Maryland State Senate, 2021 Reg. Sess. (MD 2021). https://mgaleg.maryland.gov/2021RS/Chapters_noln/CH_669_sb0787e.pdf

taxes, digital advertisers may make an educated business decision to end or dramatically limit their digital advertising spending for Maryland-based devices.

A taxpayer could have many Maryland-based devices viewing content without earning revenue above the threshold from business in Maryland, which may still result in tax liability. Avoiding paying taxes on digital ads that do not even generate significant revenue could further reduce a brand's desire to serve ads in Maryland, thereby further putting Maryland agencies at a disadvantage. This effect will also likely be compounded if higher prices for digital advertising reduces quantity demanded for digital advertising in Maryland among brands and businesses.

IV. Definitional Ambiguity

HB 732 defines digital advertising service as "including advertisement services on a digital interface". It is not fully clear what is considered to be a digital interface because it is vaguely defined as "any type of software, including website, part of a website, or application."[4] This definition could be as broad as to include audio ads served through podcast or radio station applications on mobile devices. Other types of advertising that could be covered under this extremely broad definition include all advertising served on smart TV, streaming devices including Roku, AppleTV+, Amazon Fire Stick etc., or cable programming streamed through apps such as YouTube TV, Apple TV, Hulu, Sling TV, etc. It seems discriminatory that linear advertising served over the air would not incur tax liability, but ads served in Maryland during the same program viewed through a cable application streaming a linear broadcast channel would be taxed.

In addition, under the definition of digital advertising, taxable ads could include banner, search engine ads and very broadly, "other comparable" ads. There is no further explanation of what makes an ad "comparable". For example, would influencer content be considered digital advertising, with tax obligations attributable to the brands being promoted? If it is, influencers will need to routinely provide data to digital advertising companies (or their agency proxies) to ensure proper yearly tax compliance.

Better definitional clarity on the types of digital advertising activities that are taxable will also give agencies more knowledge to help advertisers make informed decisions about the best

[4] HB 732, Maryland General Assembly, 2020 Reg. Sess. (MD 2020). https://mgaleg.maryland.gov/2020RS/bills/hb/hb0732E.pdf

types of advertising campaigns to utilize to maximize brands' return on investment for their advertising expenditures.

V. Implementation Challenges

Sourcing Maryland digital advertising impressions for the purpose of assessing an advertiser's tax liability remains one of the most difficult operational challenges of this regulation. It is not uncommon for advertisers to delegate full digital advertising campaign administration to their hired agency partners. Given this reality, it is highly likely that the collection and processing of digital ad sourcing data for the purposes of Maryland digital tax compliance will fall on brands' agency partners, who will transfer said digital ad data to their clients' tax or accounting departments for final processing and tax filing. Within agencies, the ad operations, finance, reporting and analytics and technical teams would all likely be involved in assisting clients with digital ad impression reconciliation and data processing for ad tax compliance. This cross-agency coordination and processing would be complicated and labor intensive and could drive up costs for agencies.

Operationalizing impression level analysis of all digital ad data coming from every buying platform will be a significant logistical challenge for all agencies. Most agencies do not collect and store impression level data in their reporting platforms, even if they have the ability to do so. Even assuming that every impression was available with location details, agencies would have to store and review impression level details for billions of records. Moreover, for brands' national digital ad campaigns, agencies that receive log level data usually receive it for the entirety of an advertiser's investment; thus, in order to help brands compile ad tax compliance data, agencies would have to painstakingly parse through all the data logs for the entire U.S. market to identify Maryland-specific records. This painstaking process requires an agency to review billions of impressions. When also considering that this data has to be reconciled across partners for impression adjustments for fraud, the cost of doing this data analysis and the cost to store this much data will be cost prohibitive for all but the largest digital advertisers.

Below are two other major implementation issues with the current proposed regulations that will impact how agencies attempt to standardize and accurately process digital ad tax data on behalf of their clients.

Addressing Conflicting Data Points

The current draft regulations do not speak to how a taxpayer should handle conflicting data points for the location of where a digital ad was viewed. It merely states that "taxpayers will determine the location of a device using the totality of the data within their possession or control"[5] to determine sourcing for the digital advertising tax. If a taxpayer is supposed to use "the totality of data within their possession," prioritization of data points must be specified when two or more types of a consumer's location data do not align. We feel strongly that unless modified, there will be uneven application of process in this scenario, causing confusion for digital advertisers (and their agency partners) as they attempt to comply in good faith with proper data collection and processing for tax compliance.

For example, the current draft regulations do not describe how a taxpayer (or its agency partner) should handle a scenario where an IP address of a digital ad viewer denotes a Maryland location, while their device registration shows that the device viewing the digital ad is registered in another state entirely. In such a scenario, should the digital advertiser just assume to pay the tax on that particular digital ad view because one data point shows a nexus to Maryland and IP addresses are more up-to-the-minute reflecting a user's location? We ask that the Comptroller add written clarity to the proposed regulations for how taxpayers should handle cases where two or more points of technical information regarding a device's location are in contention, if one of those data points indicates a digital ad impression was served in the state.

Addressing Fraudulent Impressions

Digital advertising fraud is a real and growing phenomenon. Juniper Research estimates that the global digital advertising industry loses approximately $51 million per day due to digital ad fraud and that by 2023 that number will skyrocket to $100 billion annually.[6] This theft significantly impacts the bottom lines of all brands that allocate budget to online advertising. Brands expect their ads to reach an audience so they can demonstrate value and create brand loyalty, which ultimately results in customer engagement and sales.

Due to ad fraud, digital ads on publisher websites may not ever be seen by a single human being. Cybercriminals carry out ad fraud by mimicking human consumer behavior using "bots".

[5] Proposed COMAR 03.12.01.01.B(4) (Aug. 31, 2021)

[6] Alemi, Farnaz M. "How Cybercriminals Are Stealing Your Ad Dollars." Bloomberg Law, 27 May 2021, https://news.bloomberglaw.com/securities-law/how-cybercriminals-are-stealing-your-ad-dollars. Accessed 2 Nov. 2021.

These bots artificially augment digital impressions to increase cybercriminals' payout by making it appear as if digital ads displayed on websites or apps are getting human eyeballs or clicks when this activity is not occurring. Unfortunately, the current proposed regulations do not address whether advertisers (or their agencies) can throw out fraudulent digital ad impressions affirmatively located in Maryland for calculating tax liability or whether these non-human, unverifiable impressions must be considered taxable activity for the sake of the regulation.

Recently the Association of National Advertisers (ANA) and digital security firm WhiteOps (newly rebranded as HUMAN), partnered to examine just how badly bot fraud is impacting digital campaigns for large advertisers. The study included participation from fifty ANA member companies covering digital advertising activity data between August 1, 2018, and September 30, 2018. Utilizing data from 2400 advertising digital ad campaigns and over 27 billion digital impressions, researchers found that eight percent of display advertising impressions are fraudulent, and 14 percent of video ad impressions are fake.[7] Digital ad fraud is a real threat to the digital advertising industry that could have real financial consequences for expected taxpayers in this regulation.

As part of their digital advertising strategies, brand advertisers and their agencies will often utilize ad verification partners on publisher sites for ad delivery optimization and/or as a cost savings tool to prevent the delivery of paid digital ads to user ISPs or accounts that are fraudulent. These ad verification technologies help publishers and marketers cross-reference their ad-buys and can effectively identify inconsistencies. Utilizing this ad fraud data, digital advertising platform managers or their agency partners can back out digital ad impressions from ad management platforms on publisher sites that are flagged as fraudulent or alternatively renegotiate with publishers for better digital advertising contract terms.

Because the regulation already allows advertisers to throw out unassignable digital ad location data from the apportionment calculation, we request that the Comptroller modify the proposed regulations to affirmatively give advertisers (or their agency partners) wide discretion to throw out Maryland geolocated data considered by ad verification technologies or internal digital ad data review processes to be fraudulent. With data unapportioned, tax liability would then not

[7] 2018-2019 Bot Baseline: Fraud in Digital Advertising." ANA, 2019. https://cdn2.hubspot.net/hubfs/3400937/2018-2019%20Bot%20Baseline%20Report.pdf?__hstc=148792360.2a062f113d5b0570248fc4e102f0f906.1635889429840.1635889429840.1635889429840.1&__hssc=148792360.1.1635889429840&__hsfp=2983861036&hsCtaTracking=bdb34cab-eed6-4c35-8d18-29b29f87cf4c%7C17812a62-49fe-4368-a40c-1526ad8f8f08

accrue from this fraudulent data, even if technical data criteria indicate a fraudulent digital ad impression occurred in Maryland.

It should be noted that ad verification platforms and internal data review processes utilize proprietary algorithms and confidential data review auditing techniques to try to mitigate digital ad fraud; as such, any comptroller attempts to prescribe specific limitations or to broadly limit the types of impression data that can be considered fraudulent for the sake of calculating Maryland digital advertising tax liability will be unhelpful. If ad fraud adjustments were allowable in a final regulation where some viewability was taking place, clarification may be needed to designate what types of partners could be used for fraud adjustments or viewability adjustments.

Apportionment Calculations Utilizing Device Location Are Burdensome and Differ from Statute

In the current proposed regulations, we also strongly disagree with the Comptroller's decision to change how the tax's apportionment factor is calculated. The current approach changes the formula from revenue generated from digital advertising services in the state (how it was written in HB 732) to the number of devices that have accessed the digital advertising services within the state over total digital ad impressions worldwide. Device impression figures should not be considered a fair stand-in for real, state-specific digital advertising revenue to determine a taxpayer's digital ad tax liability. In 2018 in the US, average viewability for YouTube Ads was 94%, while the average rate for web & app video ads was 66% and 49% for display ads.[8] Should these regulations be enacted, brand advertisers participating in digital advertising in Maryland would be paying taxes on a significant minority of their digital ads that never interacted with a human being.

From a tax compliance and operational perspective, determining digital advertising tax revenues attributable by state (via a population proxy adjustment for total revenue) is a much easier datapoint to calculate than taxpayers (and their agency affiliates) itemizing every digital ad impression in a state per year over all digital ad impressions served annually worldwide. A population proxy approach is rooted in quantifiable, corporate revenue attributed to digital advertising services, as opposed to less reliable digital ad impressions that are not based at all on advertising conversions and can be recorded even if a digital ad is never viewed by a device user. Relying on figures for state-specific digital ad impressions as a surrogate for a state's

[8] "Video AD Viewability Update 2018: Benchmarks Across Countries & Devices." *Marketing Charts*, 14 Mar. 2019, https://www.marketingcharts.com/advertising-trends/creative-and-formats-107766.

digital ad revenue could also be a more linear approach to designing a tax that does not directly decrease overall quantity demanded for digital advertising in Maryland, particularly if ad impression to sale conversion rates for digital ads in Maryland are low.

As such, the Maryland Comptroller should update the draft regulations to give digital advertisers the option to utilize a population proxy method as an alternative to the currently proposed device impression apportionment model. This alternative apportionment approach could help significantly reduce the weighty data collection and processing burdens imposed on digital advertisers (and their agency partners) that are currently required to ensure accurate compliance with the state's digital ad tax; however, retaining an option for digital advertisers to utilize currently proposed device impression calculation method, ensures that digital advertisers who do not significantly target digital advertising to Maryland, but run some national or regional digital advertising campaigns that may touch Maryland-based users, are not unfairly burdened with excess digital advertising tax liability. Regulations that offer both apportionment models to digital advertisers balances a need to lessen massive tax compliance burdens with those affected by uneven over taxation triggered by utilizing population data instead of device-level data.

VI. <u>Sourcing Approach Utilizing Geolocation And Device Tracking Threatens The Larger Public Policy Push Toward Enhancing Consumer Privacy</u>

As currently drafted, the Comptroller's existing regulations require individual device tracking and geotargeting ad impressions as a key determinant of a taxpayer's digital advertising tax liability in Maryland.

Recent state and international policy initiatives and large technology company business decisions to prioritize consumer privacy have reduced the advertising industry's ability to accurately and consistently determine the location of users viewing digital advertising content. These new consumer privacy initiatives and regulations have focused on data minimization and mandating that companies implement affirmative, opt-in consent for the collection of users' sensitive personal information (including IP addresses, device registration information, and geographic location tracking, etc.).

For example, Apple's iOS 13 and iOS 14 privacy controls and location alerts limit the availability of reliable device location data. According to research from location verification company Location Sciences, since the adoption of iOS 13 the company has seen "a 68% decrease in available background location data.[9]"Moreover, a iOS 14 user's decision not to allow in-app tracking, means that third-party apps will only be given approximate location data of app users, limiting location data sent to apps to a general 10-mile region.[10] This could have major ad sourcing implications for digital advertisers targeting digital advertising in the DC-Maryland-Virginia (DMV) which is heavily populated and operates routinely without respect for state borders.

To date, three states, including Maryland's geographic neighbor, Virginia, have enacted consumer privacy legislation that requires express consent for the collection of a user's precise location information, and over half a dozen others to date have expressed interest in exploring similar legislation during the 2022 legislative session.

An apportionment approach that heavily relies on the collection of device geographic location data or other personally identifiable information also contradicts the recent tide of laws and business decisions by private technology companies to require consumers to opt-in to consent for the collection of sensitive personal information. It also ensures that digital advertisers' new yearly tax liability may not be truly reflective of legislators' intent to tax all revenue generated from digital advertising in the state of Maryland.

The advertising industry itself is also giving consumers tools to exercise privacy controls. The Digital Advertising Alliance (DAA), a self-regulatory body of the advertising industry, establishes and enforces responsible privacy practices across industry for relevant digital advertising, providing consumers with enhanced transparency and control through multifaceted industry standards for cross-site targeted advertising and across devices.[11]

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[9] Slade, Mark. *IOS 14 and Its Impact on the Location-Based Advertising Market*, Location Services, Jan. 2020, https://www.locationsciences.ai/blog/ios-14-and-its-impact-on-the-location-based-advertising-market/. Accessed 2 Nov. 2021.

[10] Lacoma, Tyler. "What IOS 14's Hidden 'Approximate Location' Feature Is (and Why It's Important)." *IDropNews*, 27 Aug. 2020, https://www.idropnews.com/news/what-ios-14s-hidden-approximate-location-feature-is-and-why-its-important/141938/. Accessed 3 Nov. 2021.

[11]Digital Advertising Alliance , https://digitaladvertisingalliance.org/

VII. Agency Exemption Needs To Be Codified

Advertisers work with agencies because agencies know the latest trends, best practices, and best tools and strategies that are needed for marketing success. Following industry norms, agencies are generally liable for paying the media outlets, publishers, or online platforms when executing marketing campaigns, with a traditional pass-through and expense structure.

As the proposed regulations are currently written, there is no mention of a much-needed exclusion for advertising agencies who exercise digital advertising campaigns (and associated digital ad buys) on behalf of their clients. This should be remedied in order to ensure agencies are not unfairly taxed for managing digital advertising buys for clients' online marketing campaigns and reselling online advertising space.

Importantly, Senate digital advertising legislation sponsor and President of the Maryland Senate, Bill Ferguson (D-46), indicated that it was not the Maryland Legislature's intent to impose digital advertising taxes on advertising agencies. In an interview with the *Wall Street Journal*, he clarified that he does not believe that the tax should be levied against a company reselling ad space to a marketer client.[12]

On behalf of our members, the 4A's respectfully requests that our recommendations for changes to the draft digital advertising tax regulations be considered.

Sincerely,

Alison Pepper

Alison Pepper
Executive Vice President, Government Relations, 4A's

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[12] McKinnon, John D, and Alexandra Bruell. "Tech Industry Challenges Maryland Online Ad Tax." *Wall Street Journal.*, 18 Feb. 2021, https://www.wsj.com/articles/tech-industry-challenges-maryland-online-ad-tax-11613679371. Accessed 2 Nov. 2021.