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Maryland: Taxation of digital advertising services; sales and use tax on digital products and services

The Maryland General Assembly on April 12, 2021, passed Senate Bill 787—legislation that revises two digital services tax laws enacted earlier this year. The bill is pending action by the governor (who has 30 days to sign, veto or allow the bill to become law without his action).

Maryland House Bill 732 (2020 session) imposed a special tax on gross revenues received from digital advertising services, and House Bill 932 (2020 session) expanded the sales and use tax base to certain digital products and services.

Senate Bill 787 makes several amendments and technical corrections to those laws including delaying the implementation date of the digital advertising tax.

Amendments to House Bill 732 (2020 session)

Senate Bill 787 would delay the effective date of the digital advertising tax to tax years beginning after December 31, 2021.

Under the current measures, the tax on digital advertising services is effective for 2020, and the first estimated payment of the tax is due April 15, 2021.

Under Senate Bill 787, the first estimated payment would be due April 15, 2022.

Senate Bill 787 also provides that taxable digital advertising services would not include advertisement services on digital interfaces owned or operated by, or operated on behalf of, television or radio broadcast entities or news media entities. A “broadcast entity” includes “any entity primarily engaged in the business of operating a broadcast television or radio station.” The term “news media entity” is defined to include “any entity primarily engaged in the business of newsgathering, reporting, or publishing articles or commentary about news, current events, culture, or other matters of public interest.”

Finally, Senate Bill 787 provides that a person subject to the digital advertising tax could not directly pass on the cost of the tax to a customer by means of a separate fee, surcharge, or line item.

Amendments to House Bill 932 (2020 session)

Under House Bill 932—the “21st Century Economy Sales Tax Act”—Maryland’s sales and use tax was expanded to digital products, digital codes, and streaming services, effective March 14, 2021. The Maryland Comptroller later released Business Tax Tip #29, “Sales of Digital Products and Digital Code,” which took an expansive interpretation of the law, and specified that the tax would be imposed not only on digital books, digital music, and digital audio visual works, but also on other digital products and services, including access to online content, SaaS, software applications, online classes, and prerecorded or live speeches.

In response to feedback from the business community, Senate Bill 787 somewhat narrows the application of tax to certain products and services. Specifically, Senate Bill 787 provides that a “digital product” does not include:

- Prerecorded or live instruction by public or private educational institutions
- Instruction in a skill or profession if the instruction is not prerecorded and features an interactive element
- Seminars, discussions, or similar events hosted by a nonprofit or business association if the event is not prerecorded and features an interactive element
- Professional services obtained electronically or delivered through the use of technology having electrical, digital, magnetic, wireless, optical, electromagnetic, or similar capabilities

Senate Bill 787 also clarifies that tax does not apply to custom computer software—regardless of the method transferred or accessed—or certain services relating to custom computer software. The amendments in Senate Bill 787 clarify that customer computer software includes software that would otherwise be taxable if it is created for a specific person or requires significant creative input to modify or configure standard procedures and routines in the software to enable it to operate in the manner intended and required by the person.

Finally, Senate Bill 787 updates Maryland’s tax code to add the terms “digital products” and “digital code” to various provisions and definitions that already include the terms “tangible personal property” or “taxable service.”

KPMG observation

Although Senate Bill 787 has not yet been enacted, businesses that are currently subject to the digital advertising tax need to be aware of recent guidance that advises them not to remit estimated tax payments to the Maryland Comptroller. The Comptroller recently released Bulletin 21-2 that assumes that Senate Bill 787 would be enacted and confirming that the first estimated payment would be due April 15, 2022.

The Comptroller is expected to publish further guidance on the digital advertising tax and adopt regulations to aid companies in determining who is subject to the tax and how revenue from digital advertising services are sourced—one of the key questions that many businesses and practitioners had about the law.

- Businesses subject to the tax need to track these developments and keep an eye on litigation filed in February 2021 over whether the tax violates the Internet Tax Freedom Act and/or the Due Process and Commerce Clauses.

- Businesses also need to consider the legislative amendments to the statute providing that digital advertising services do not include advertisement services on digital interfaces owned or operated by, or on behalf of, television or radio broadcast entities or news media entities.
- While the exclusion appears to provide that revenues from digital ads displayed on websites and apps owned by broadcast entities or news entities are not subject to the tax, certain entities may be engaged in digital advertising services on interfaces that meet the exclusion, as well as digital interfaces that do not. These entities may need to segregate taxable revenues from excluded services. The definition of a “news media entity” is broad and, in addition to sites traditionally considered news media sites, may include websites or apps that are narrowly tailored to specific types of news or topics of cultural interest. For example, a website that focus or reports on a specific genre of television programming or sport may be considered a news media entity.

Senate Bill 787 also does not dramatically narrow the scope of the original law on sales and use tax on digital products, although the new carve out for certain educational products and software would need to be factored into compliance activities.

- Because Maryland’s approach to taxing digital products and services is unusual and does not follow the approach of most other states (i.e., adopting definitions provided by the Streamlined Sales and Use Tax Agreement), businesses making sales of SaaS, access to online content, video games, customer lists, mailing lists, and all the other types of services and goods that fall under the umbrella of digital products—as set forth in [Tax Tip #29](#) [PDF 312 KB]—may need assistance determining the taxability of products and services that they sell.
- In addition, taxpayers need to monitor whether the Comptroller modifies Tax Tip #29 as a result of Senate Bill 787.
- The effective date of the digital products legislation remains March 14, 2021. However, the Comptroller previously announced the due date of sales and use tax returns and payment of taxes for sales taking place in March, April, and May 2021 is extended to July 15, 2021.

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