IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MARYLAND

CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA, *et al.*, *Plaintiffs*, v. PETER FRANCHOT, *Defendant*.	No. 1:21-cv-410-DKC

PLAINTIFFS' SUPPLEMENTAL REPLY BRIEF ADDRESSING THEIR FIRST AMENDMENT CHALLENGE TO THE PASS-THROUGH PROHIBITION

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SUPPLEMENTAL REPLY BRIEF

The State's supplemental brief does not defend the pass-through prohibition as a speech ban. It thus makes no effort to show that it satisfies strict or intermediate scrutiny, as is its burden. As we demonstrated in our own supplemental brief, the ban does not satisfy either of those exacting standards and therefore must be invalidated.

The State's principal position, instead, is to say that the pass-through prohibition regulates conduct rather than speech. But the parties have jointly stipulated the opposite. *See* Dkt. 68. The Act does *not* forbid "passing on the cost of the tax . . . by factoring such cost into its customer pricing" and instead applies "only when [the tax] is imposed on the consumer by means of a 'separate fee, surcharge, or line item.'" Neglecting the import of that binding stipulation, the State nonetheless insists (Supp. Br. 2) that the pass-through prohibition does not limit "what the taxpayer may say to the customer" and "merely prohibits a particular business practice." But the only "business practice" to which the pass-through prohibition can be understood to apply is the practice of expressly breaking out and identifying for consumers the fact and size of the tax as a "a separate fee, surcharge, or line-item" on invoices and the like. Tax-Gen. § 7.5-102(c). That's speech, plain and simple, as the Sixth Circuit correctly held in *BellSouth*. The pass-through prohibition is therefore a presumptively unconstitutional content-based speech restriction.

1. The State asserts (Supp. Br. 1) that our facial challenge to the pass-through prohibition fails because our prior filings "acknowledge[d] that the direct pass-through prohibition is susceptible to a plausible interpretation that it regulates not speech but *conduct*." On this basis, it says (*id.*) we have failed to show "that no set of circumstances exists under which the Act would be valid." But, again, that ignores the binding stipulation that the

State has entered into. Even accepting that the pass-through prohibition were originally susceptible to an interpretation that it regulates conduct rather than speech, it is no longer. The State has expressly interpreted the provision to regulate speech, and our former pleading in the alternative does not relieve the State of the effect of that binding position. *See Radiological Ventures, LLC v. Marine Electrical Systems*, 2008 WL 11509472, at *2 (D. Md. 2008) ("The federal rules govern the pleadings in this case, and they expressly allow pleading in the alternative.").

The State is thus wrong to say (Supp. Br. 2-3) that if a "taxpayer wishes to inform the customer that the invoiced charge is higher than it might otherwise be due to the imposition of the digital ad tax, the taxpayer is free to communicate that or any other message." That is simply untrue. If the taxpayer "wishes to inform the customer that the invoiced charge is higher" *and to state by how much*, it would be forbidden as "a separate fee, surcharge, or line-item" within the meaning of Tax-Gen. § 7.5-102(c). Consider just three among countless possible examples:

ACME DIGITAL ADVERTISING
INVOICE – February 1, 2022

January 2022 advertising services: $900
Maryland Digital Advertising Tax recoupment fee: $100
Total due: $1000

SMITH & SONS DIGITAL ADVERTISING CO.
INVOICE – February 1, 2022

Total due for January 2022 advertising services: $1000*
** Includes a 10% Maryland Digital Advertising Tax surcharge, which will be remitted to Comptroller of Maryland pursuant to Md. Tax-Gen. § 7.5-102.*

DIGITAL MARKETING OF AMERICA
INVOICE – February 1, 2022

Advertising services, 1/1/22 thru 1/31/22: $1000
Please note: Your total includes $100 to pay the Maryland Digital Advertising Tax.

Any of these invoices would plainly violate the pass-through prohibition inasmuch as they identify the fact and size of the tax as a "a separate fee, surcharge, or line-item." And what sets them apart from permissible invoices is the content of their messages.

The pass-through prohibition is thus facially invalid. In a First Amendment facial challenge, "a plaintiff may sustain its burden" by demonstrating either overbreadth or "that no set of circumstances exists under which the law would be valid, or that the law lacks any plainly legitimate sweep." *Education Media Co. at Virginia Tech v. Insley*, 731 F.3d 291, 298 n.5 (4th Cir. 2013) (quoting *Greater Baltimore Center for Pregnancy Concerns v. Mayor & City Council of Baltimore*, 721 F.3d 264, 282 (4th Cir. 2013) (en banc) (cleaned up)). The question whether the challenged law "lacks any plainly legitimate sweep" asks whether there are any cases in which the challenged law, *properly construed*, could be constitutionally applied. It thus requires the Court to "consider hypothetical situations" in which the law might be invoked. *White Coat Waste Project v. Greater Richmond Transit Co.*, 463 F. Supp. 3d 661, 694 (E.D. Va. 2020). If the Court determines that the law "can *never* be validly enforced and would be unconstitutional in all, or virtually all, of its applications," it is facially invalid. *Id.* Here, the State has interpreted its law to prohibit speech based on content, and it is therefore unlawful in all its applications.

Against this backdrop, the State's protracted discussion in a footnote of the subsequent history in *Expression Hair Design* is irrelevant. *See* State Supp. Br. 3 n.1. There, the New York court held that the law at issue "permits differential pricing [and] requires [only] that a higher price charged to credit card users be posted in total dollars-and-cents form." *Expression Hair Design v. Schneiderman*, 117 N.E. 3d 730, 736 (N.Y. 2018). That is not the case here—the Act does not *compel* speech, but rather *prohibits* it.

2. The State's analogies to federal antitrust and procurement laws do not improve its position. It is true, of course, that certain areas of the law speak of costs being passed on directly and indirectly. For example, in the antitrust context, the *Hanover Shoe* and *Illinois Brick* doctrine restricts who may sue for certain antitrust violations based on whether the customer paid an overcharge directly (meaning she purchased goods directly from an alleged monopolist) or instead whether she incurred a supra-competitive overcharge only indirectly (meaning the surcharge was imposed by the manufacturer of an upstream input, resulting in diffusely higher end-product prices after having been passed on through multiple stages of the production and distribution chains). *See Illinois Brick Co. v. Illinois*, 431 U.S. 720, 723-726 (1977). The cited procurement regulations reflect a similar notion, concerning recoupment of fixed costs incurred indirectly. *See* 48 C.F.R. § 31.203.

This case is not about the antitrust or procurement laws, nor does it involve multiple steps in a production and distribution chain. Rather, the case is about a State-imposed fee applicable to the sale of digital advertising services to customers in Maryland. The parties' stipulation makes clear that the pass-through prohibition does not prohibit a person from factoring the cost of the tax "into its customer pricing" and prohibits only "impos[ing] it by means of a 'separate fee, surcharge, or line-item.'" (Dkt. 68) That is a regulation of speech, not conduct, and it is therefore unconstitutional. *See* Pl. Supp. Br. 1-6.

3. The State also defends the pass-through prohibition on the ground that, even if it forbids the identification of the fact and magnitude of the Act's charge on invoices and bills, it does not "prevent[], or even discourage[], a taxpayer from including on an invoice any [other] 'political speech' the taxpayer wishes to convey." Supp. Br. 2. But the fact that the State could have attempted to prohibit *additional* protected speech does not mean that

prohibiting line-items identifying the tax on billing statements is somehow lawful. On the contrary, failure to forbid "all communications between the providers and consumers about the relationship between the tax and price increases[,]whether on the invoice, in advertisements or on billing inserts," means only that the pass-through prohibition is ineffectual and thus unsustainable under either strict or intermediate scrutiny. *BellSouth Telecommunications, Inc. v. Farris*, 542 F.3d 499, 507 (6th Cir. 2008).

4. Finally, according to the State, the pass-through prohibition is valid because it ensures that the amounts collected by digital advertising companies and remitted to the State under the Act are included in "gross revenue." Supp. Br. 4. In other words, the State wants to ensure that it can tax revenues recouping the tax.

The pass-through prohibition is not necessary for that purpose. As the State notes (Supp. Br. 4), the law defines "gross revenues" to be "income or revenue from all sources, *before any expenses or taxes*, computed according to generally accepted accounting principles." Tax-Gen. § 7.5-101(b) (emphasis added). Because the Act makes digital advertising companies liable for the digital advertising tax—not their customers—recoupments of the tax from customers count as "revenue" before payment of "any expenses or taxes," no matter whether or not they are expressly identified on invoices. Even if there were doubt about that, it would not be necessary to ban express line-items to ensure that revenues recouping the tax are counted as taxable gross revenue—that could be accomplished simply though Comptroller guidance or an interpretative regulation. Thus, even crediting the State's dubious explanation, this less restrictive means of achieving the State's objective would doom the pass-through prohibition.

CONCLUSION

The Court should deny the State's motion to dismiss and grant plaintiffs' cross-motion for summary judgment with respect to Count IV of the amended complaint.

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Respectfully submitted,

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