Fredrick J. Nicely
Senior Tax Counsel
(202) 484-5213
fnicely@cost.org

April 16, 2024

VIA EMAIL
Senator John Arch, Speaker
Nebraska Legislature

Re: COST Opposes the Proposed Advertising Services Tax Act in L.B. 388 (Final Reading)

Dear Speaker Arch:

On behalf of the Council On State Taxation (COST), I am writing in opposition to the proposed Advertising Services Tax in L.B. 388 that would be imposed on businesses in Nebraska whose combined gross advertising revenue exceeds $1 billion at a rate of 7.5 percent. This proposed Advertising Services Tax is a new, controversial, and untested tax and will likely face protracted litigation similar to Maryland's Digital Advertising Tax.[1] It would put Nebraska at a competitive disadvantage with respect to businesses seeking to maintain or expand their operations in the State because the tax is ultimately a gross receipts tax on business inputs,[2] and the activities are already sufficiently taxed under the State's corporate income tax regime.

About COST

COST is a nonprofit trade association based in Washington, DC. COST was formed in 1969 as an advisory committee to the Council of State Chambers of Commerce and today has an independent membership of approximately 500 major corporations engaged in interstate and international business. COST's objective is to preserve and promote the equitable and nondiscriminatory state and local taxation of multijurisdictional business entities. Many COST members have operations in Nebraska that would be negatively impacted by this legislation.

[1] *See* Bloomberg Daily Tax Report: State (2/13/24) by Michael Bologna, "Apple, Peacock Battle for Top Position in Maryland Ad Tax Fight," available at: https://news.bloombergtax.com/daily-tax-report-state/apple-peacock-battle-for-top-position-in-maryland-ad-tax-fight. Litigation is also pending at the federal court level, Civil No. 21-cv-410 (D. Md., filed February 18, 2021). Unlike Maryland, Nebraska allows declaratory relief (Neb. Rev. Stat. §§ 25-21,149 and 25-21,159) and injunctive relief (Neb. Rev. Stat. §§ 25-1062-1080) to be immediately available to contest the Advertising Services Tax.
[2] Business inputs constitute intermediate transactions of goods and services that businesses either resell or use to produce other goods or services that are subsequently sold for final consumption by consumers.

COST Opposes Excise Taxes on Business Inputs

The COST Board of Directors has adopted formal policy statements opposing both gross receipts taxes and sales taxes on business inputs. While the position on business inputs primarily concerns the states' sales taxes, its logic also applies to the proposed Advertising Services Tax, which is a gross receipts tax on business inputs. COST's policy positions are as follows:

> *Gross receipts taxes are widely acknowledged to violate the tax policy principles of transparency, fairness, economic neutrality and competitiveness; generally, such taxes should not be imposed on business.*[3]
>
> *Imposing sales taxes on business inputs violates several tax policy principles and causes significant economic distortions. Taxing business inputs raises production costs and places businesses within a State at a competitive disadvantage to businesses not burdened by such taxes. Taxes on business inputs, including taxes on services purchased by businesses, must be avoided.*[4]

The imposition of the Advertising Services Tax is primarily focused on taxing business inputs, not consumer purchases. This disproportionate taxation of business inputs violates several core tenets of sound tax policy—transparency, economic neutrality, effective tax administration, and fairness.

- *Transparency.* A transparent tax, like the sales tax on consumer purchases, is obvious to the taxpayer, and its economic effects are easily understood. The Advertising Services Tax, on the other hand, is a stealth tax that will affect Nebraska businesses and residents in several unseen ways. The tax will impact residents as purchasers, by imposing hidden taxes and thus making the products they purchase more expensive, and as workers, by depressing investment and thus reducing wages and employment opportunities.
- *Economic Neutrality.* An economically neutral tax does not influence business choices (of location, of operational entity, of suppliers, *etc.*). This tax will force companies to either pass their increased costs on to consumers or reduce their economic activity in the State in order to remain competitive with other companies in other states that do not bear the burden of such taxes.
- *Effective Tax Administration*. Effective tax administration is enabled by taxes that can be easily administered by a state and can facilitate voluntary compliance by all businesses. This entails tax base and sourcing rules that are comprehensible to both tax administrators and taxpayers. The Advertising Services Tax is anything but easy to administer. As an untested and novel tax, companies will be forced to adopt sophisticated accounting and recordkeeping systems to evaluate transactions on a continuous basis. For example, verifying what portion of the national advertising audience was within the State will be extremely difficult using IP addresses. The increased use of virtual private networks (VPNs) and allowing the use of "another reasonable method" to source the revenue is very

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[3] https://www.cost.org/globalassets/cost/state-tax-resources-pdf-pages/cost-policy-positions/grossreceiptstaxes.pdf.
[4] https://www.cost.org/globalassets/cost/state-tax-resources-pdf-pages/cost-policy-positions/sales-taxation-of-business-inputs.pdf.

open ended and unclear. This tax does not conform to or harmonize with any prior national or uniform state model, leading to additional complexity for taxpayers and the Department of Revenue.

- *Fairness.* A fair tax treats similarly situated taxpayers equally. Instead of having a broad base and low tax rate, the Adverting Services Tax is selectively imposed in a punitive manner based on those providers exceeding a $1 billion threshold.[5]

Businesses Subject to the Advertising Services Tax Are Already Subject to the State's Corporate Income Tax

Businesses subject to the Advertising Services Tax are already subject to the State's corporate income tax on their net income. The corporate income tax requires mandatory unitary combined reporting and is imposed on the privilege of corporations earning or receiving income in Nebraska. This imposition threshold gives the State expansive jurisdiction to impose the corporate income tax without requiring a physical presence in the State. As a result, the same businesses that would be subject to the Advertising Services Tax are also subject to the State's corporate income tax. Nebraska also imposes a market-based sourcing regime for receipts from services and apportions such receipts using a single-sales factor formula. Market-based sourcing seeks to tax a receipt based on where the customer receives the benefits from the service rather than the location of the taxpayer. To the extent a business collects advertising revenue from Nebraska customers, that income is already sourced to Nebraska for corporate income tax purposes under the State's market-based sourcing rules. Under the single-sales factor apportionment formula, the physical location of a corporation's business now has minimal effect on how receipts are apportioned to the State. As a result, Nebraska's corporate income tax regime sufficiently taxes the same activities that would be subject to the Advertising Services Tax.

Conclusion

COST remains aligned with the Association of National Advertisers (ANA) and others in our request that the Advertising Services Tax should be rejected. We respectfully oppose the Advertising Services Tax included in L.B. 388 because it is a direct tax on business inputs that violates several key tax policy principles, and would immediately lead to protracted litigation similar to that facing the Maryland tax. Advertising activities are already subject to Nebraska's corporate income tax, which would result in the proposed Advertising Services Tax serving as a second or "double" tax.

Respectfully,

Fred Nicely

cc: COST Board of Directors
Patrick J. Reynolds, COST President & Executive Director

[5] This raises issues under the Commerce Clause (*e.g.*, extraterritorial taxation), First Amendment (exemptions for news media providers), and the Internet Tax Freedom Act.