

Marijuana taxes: Options, opportunities, and challenges

Revenue Stabilization and Tax Policy Committee
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1. If you decide to legalize and tax marijuana for recreational use, what are your policy goals?
2. How do other states tax marijuana? What are the pros and cons of each approach?
3. How much revenue do other states raise from marijuana taxes? How is the revenue spent?

What are your goals?



- New Mexico taxes income to raise money for government services
- New Mexico taxes motor fuel purchases to raise money specifically for transportation spending
- New Mexico taxes cigarettes to dissuade residents from smoking

- Why does New Mexico want to tax marijuana?

Possible goals



- Raise revenue for government services
- Eliminate the illegal marijuana market
- Reform criminal justice system
- Economic development

- Goals may conflict: Tax rate that maximizes state revenue might maintain large illegal market

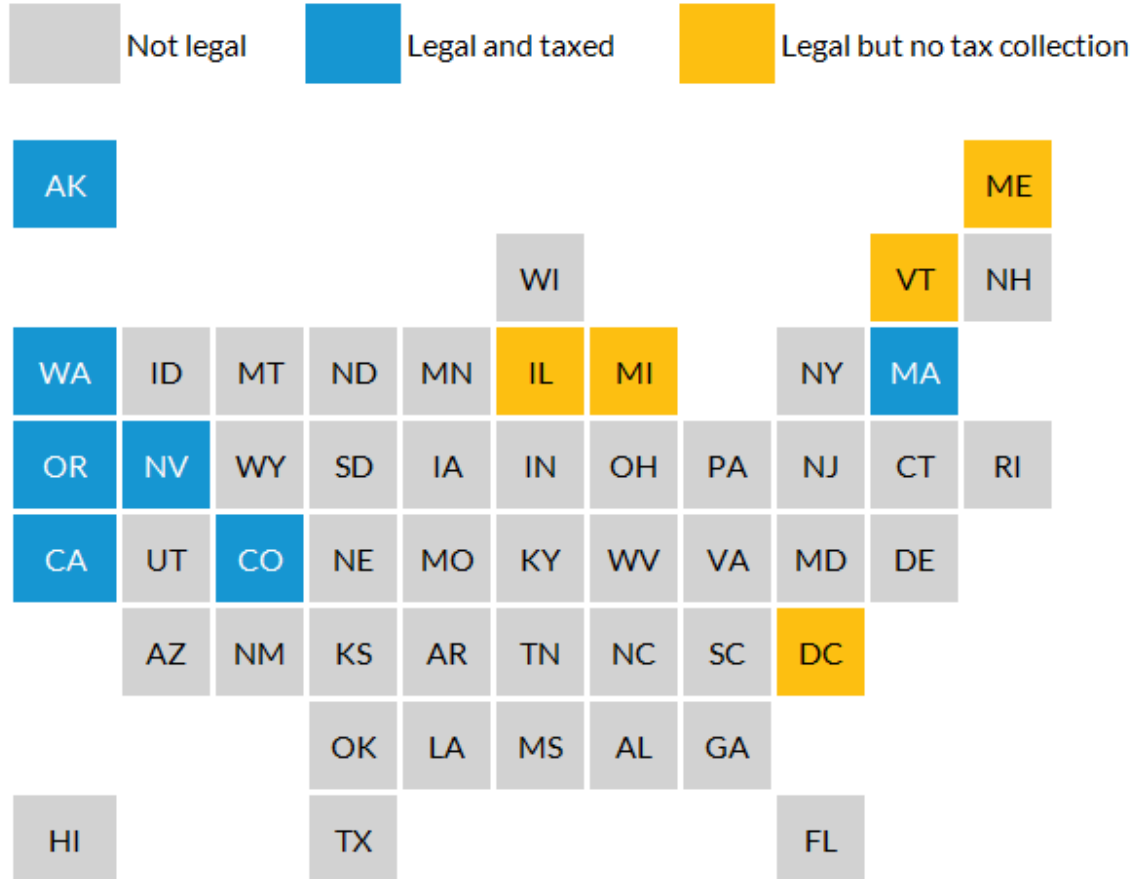
- Taxes are not the only policy: Licensing, regulation, criminal justice, and many other issues are critical

What states currently tax recreational marijuana?



Where is Marijuana Legal and Taxable?

2019



Source: State government websites.

Note: Medical marijuana is legal in 32 states.

URBAN INSTITUTE

There is no single “marijuana tax”

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Types of taxes

- Percentage of price
- Weight-based (i.e., per ounce)
- THC-based (similar to alcohol taxes)
- Government-controlled stores

Percentage of price tax

- Works like a general sales tax:
\$20 of marijuana x 15% tax = \$3 tax
- Can levy tax on wholesale/cultivator transaction or retail sale or both

States with this type of marijuana tax

- **California:** 15% on retail sale
- **Colorado:** 15% on cultivator and 15% on retail sale
- **Maine:** 10% (*pending*)
- **Massachusetts:** 10.75% on retail sale
- **Michigan:** 10% on retail sale (*ballot initiative*)
- **Nevada:** 15% on wholesale and 10% on retail sale
- **Oregon:** 17% on retail sale
- **Washington:** 37% on retail sale

Percentage of price: pros and cons



Pros

- Simple: easy for sellers and consumers to understand
- Relatively easy to administer
- Price is *somewhat* correlated with potency (not always), but “premium” products are more expensive

Cons

- Tax revenue falls with marijuana price (if rates not adjusted)
 - Colorado: From 2014 to 2017, the cost for one gram (flower) fell from \$14.05 to \$5.35
- Can possibly be gamed with “free pot with pipe” deals

Weight-based taxes

- Similar to a per pack cigarette tax
- Cultivators pay tax
- Marijuana Policy Project recommends taxing different parts of the plant—flowers, leaves, immature plant—at different rates

States with this type of marijuana tax

- **Alaska:** \$50 per ounce for bud and flowers; \$15 per ounce for remainder of plant
- **California:** \$9.25 per ounce for flowers; \$2.75 per ounce for leaves
- **Colorado:** Many of the state’s marijuana businesses are vertically integrated so there is often no sale before retail. Thus, the state’s 15% tax on cultivators is based on “average market rate,” and that rate is based in part on weight.
- **Maine:** Considering weight-based tax in addition to percentage of price

Weight-based: pros and cons



Pros

- Tax revenue should stay relatively stable even if price drops
- Collected early in the production process
 - Prevents gaming of tax
 - Might discourage illegal sales of legally grown products

Cons

- Weight does not correlate with potency
 - It under taxes potent products
 - Could encourage retailers to sell more potent products (at lower cost)

- Tax the THC the way we tax different alcohol (liquor > wine > beer)
- **Illinois** is the first state to try this approach:
 - THC level at or below 35%: 10% of purchase price
 - THC level above 35%: 25% of purchase price
 - All cannabis infused products (e.g., edibles): 20% of purchase price
- Illinois passed its legislation (HB 1438) in June; sales set to begin in January 2020

Potency-based: pros and cons



Pros

- Tax revenue should stay stable even as price drops
- May prevents retailers from selling more potent products

Cons

- THC is not a perfect measure of intoxication
- **RAND report:** “THC content does not correlate as well with intoxication as one might think. A sample’s potency, even measured accurately, could change over time ... An overwhelmingly large share of the variability in psychoactive effect arises from the method of use and drug metabolism, rather than the chemical contents of the product.”

- Similar to government-run liquor stores (17 states)
- No state has attempted this, yet
- But there are government-run stores in Uruguay, some Canadian provinces, and North Bonneville, Washington
 - There are government-run stores for medicinal marijuana in Louisiana and Utah

Government-run: pros and cons



Pros

- Government completely controls sales and can quickly change prices in response to market changes
- Possibly raises more revenue (true of government-run liquor stores)

Cons

- Government is now in the marijuana business
 - Do you advertise?
- Less responsive to customers, which could feed illicit market or cross-border sales

- **General sales taxes** at both the state (CA, ME, MI, NV, and WA) and local level (AK, CA, CO, NV, WA)
- **Local excise taxes** on marijuana are allowed in Alaska, California, Massachusetts, and Oregon
- **Section 280E:** The federal government denies marijuana business the deduction for business expense (because it's still illegal).
 - Some states (such as Colorado and Oregon) allow some business deduction; others apply federal restrictions

How much revenue do states collect from marijuana taxes?

BUSINESS NEWS MAY 8, 2018 / 5:11 AM / A YEAR AGO

Legal marijuana offers small state tax revenue boost: Moody's

Robin Respaut

3 MIN READ



SAN FRANCISCO (Reuters) - Tax revenue from recreational marijuana makes up a small percentage of annual general fund revenues in states with the most established retail markets, such as Colorado, Washington and Oregon, Moody's Investors Service said on Tuesday.

1% of general fund revenue is a lot of revenue!



Here are some other taxes that only account for 1% or 2% of state and local general fund revenue

- Alcohol taxes
- Cigarette taxes
- Corporate income taxes
- Estate taxes
- Motor fuel taxes

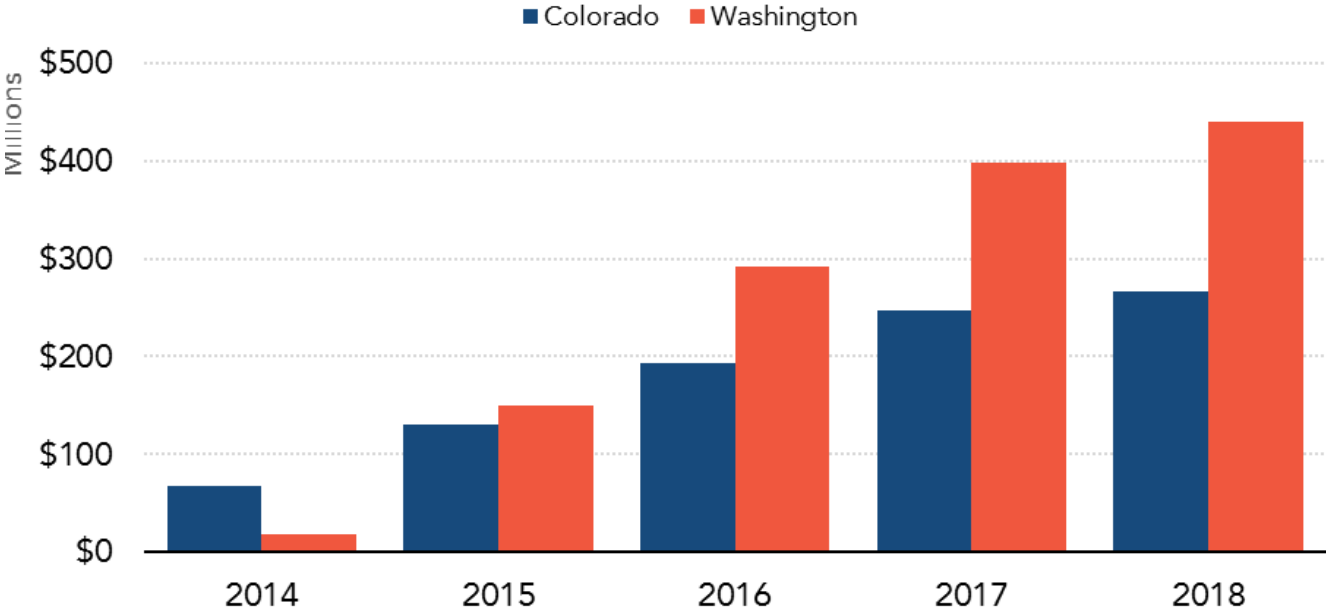
Census data; national averages

Marijuana excise tax revenue in 2018 (calendar)



- **Alaska: \$14.6 million**
- **California: \$353.8 million**
- **Colorado: \$266.5 million**
- **Nevada: \$86.9 million**
- **Oregon: \$94.2 million**
- **Washington: \$439.4 million**

Marijuana Tax Revenue in Colorado and Washington



Source: State tax reports.

Note: Does not include general sales tax revenue.

WARNINGS!



- Marijuana tax revenue is hard to predict
 - Every state has a different market and different economic, demographic, social, and cultural factors that will affect sales
- Marijuana tax revenue is volatile
 - Prices fall
 - Markets changes
 - Increased competition as new states enter the market
 - Federal action?

How do states spend their marijuana revenue



- **Alaska:** General fund and programs aimed at reducing repeat criminal offences
- **California:** Administrative costs associated with marijuana legalization, programs related to drug use
- **Colorado:** Education programs
- **Massachusetts:** Public safety programs
- **Nevada:** Education programs and rainy day fund
- **Oregon:** Education programs and drug prevention
- **Washington:** Health care programs

Should states dedicate marijuana revenue?



- To drug-prevention, criminal justice, and other programs related to marijuana use? Sure.
- To anything else? Probably not.
- Remember: The revenue is volatile and relatively small. That is, it will not fund your education budget. (So don't tell voters it will.)
- However, millions of dollars can help the state pay for numerous programs

Conclusions: This tax require work



- Numerous states have already reformed their marijuana taxes, both changing type of tax and tax rates
- We're still learning which taxes work best
- If you approve a marijuana tax, important to monitor the tax (its revenue, the market, etc.) and be prepared to make changes so that the tax achieves your policy goals

For more on this topic ...



Tax Policy Center reports on state marijuana taxes and sin taxes more broadly (Lucy Dadayan)

Released soon—if you're interested in either report, please email me at rauxier@ubran.org or check <https://www.taxpolicycenter.org/>

Tax Policy Center Briefing Book: How do marijuana taxes work?

<https://www.taxpolicycenter.org/briefing-book/how-do-marijuana-taxes-work>

Blog: A Trump Crack Down on Legal Marijuana Would Hurt State Budgets

<https://www.taxpolicycenter.org/taxvox/trump-crack-down-legal-marijuana-would-hurt-state-budgets>

Report: How Should Governments Use Revenue from Corrective Taxes?

<https://www.taxpolicycenter.org/publications/how-should-governments-use-revenue-corrective-taxes>

Report: Should We Tax Internalities Like Externalities?

<https://www.taxpolicycenter.org/publications/should-we-tax-internalities-externalities>

THANK YOU

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