

Department of Legislative Services
Maryland General Assembly
2017 Session

FISCAL AND POLICY NOTE
First Reader

House Bill 1186 (Delegate M. Washington, *et al.*)
Ways and Means and Judiciary

Excise Tax and Sales Tax - Cannabis

This bill establishes excise and sales taxes on the licensed sale of recreational cannabis. The bill requires the Comptroller to distribute the revenue generated by the taxes to the Cannabis Tax Distribution Fund established by the bill. After deducting certain administrative expenses, the net proceeds of the fund may only be used to provide supplemental funding, as provided in the State budget, to (1) the Public School Opportunities Enhancement Program; (2) the Maryland Substance Abuse Fund; (3) specified workforce development programs; and (4) State programs for impaired driving public education and law enforcement training.

The bill is contingent on the enactment of Senate Bill 928/House Bill 1185 of 2017.

Fiscal Summary

State Effect: Special fund revenues may increase significantly from taxes imposed on licensed cannabis sales. Special fund expenditures for certain Comptroller administrative expenses and purposes specified by the bill increase by a corresponding amount.

Local Effect: Local finances are not directly impacted.

Small Business Effect: Minimal.

Analysis

Bill Summary: The bill is contingent on the enactment of Senate Bill 928/House Bill 1185 of 2017. As described in the fiscal and policy notes, Senate Bill 928/House Bill 1185 removes criminal penalties for the use and possession of cannabis and cannabis

paraphernalia by individuals age 21 and older and legalizes the use, possession, sale, transportation, and cultivation of cannabis under specified circumstances. Senate Bill 928/House Bill 1185 also establishes a regulatory framework for cannabis establishments and requires the Comptroller to establish regulations to register cannabis establishments, which includes retailers, cannabis cultivation facilities, and cannabis product manufacturers.

The bill imposes taxes on cannabis produced and sold by these licensed establishments and requires the Comptroller to administer the taxes and special fund as described below.

Taxes Imposed

The bill imposes on sales of licensed cannabis a 9% State sales tax and an excise tax of \$30 per ounce. The taxes imposed do not apply to cannabis sold under the State medical marijuana program pursuant to the Natalie M. LaPrade Medical Cannabis Commission. The Comptroller must administer and implement the taxes established by the bill and adopt implementing regulations. Beginning in fiscal 2020, the Comptroller may adjust the excise tax annually based on inflation.

The 9% sales tax is imposed on all cannabis sold by a cannabis retailer. A retailer must remit to the Comptroller the sales tax on all cannabis sold by the establishment. The \$30 per ounce excise tax applies to all cannabis sold by a (1) cannabis cultivation facility to a cannabis product manufacturer or retailer and (2) craft cannabis cultivator to a cannabis cultivation facility or cannabis product manufacturer. The excise tax must be remitted to the Comptroller by (1) a cannabis cultivation facility on all cannabis it sells and all cannabis purchased from a craft cannabis cultivator and (2) a manufacturer for all purchases made directly from a craft cannabis cultivator. Each entity must file a tax return in accordance with dates established by regulations adopted by the Comptroller.

Distribution Fund

From the cannabis tax revenues collected, the Comptroller distributes an amount necessary to administer cannabis tax laws to an administrative cost account and distributes the remainder to the Cannabis Tax Distribution Fund established by the bill. The fund is a special, nonlapsing fund that is administered by the Comptroller and held separately by the State Treasurer. The fund consists of (1) the net tax revenue distributed to the fund; (2) money appropriated in the State budget; and (3) any other money from any other source accepted for the benefit of the fund.

The fund may only be used to provide supplemental funding for:

- *Public School Opportunities Enhancement Program (50%):* Funds provided to the program are for use by community schools in which 50% or more of the students qualify for a free or reduced price lunch program under the National School Lunch Program.
- *Maryland Substance Abuse Fund (25%):* Funds are to be used for the prevention, evaluation, and treatment of problematic use and addiction, including addiction to over-the-counter drugs, prescription drugs, and opioids.
- *Workforce Development Programs (15%):* Funds are distributed to the workforce development programs established under Title 11, Subtitle 5 of the Labor and Employment Article.
- *Impaired Driving Public Education and Law Enforcement Training (10%):* Funds are provided to State programs that provide public education and additional law enforcement training to address the dangers of driving under the influence.

Additional Tax Regulations and Implementation

As also generally required in Senate Bill 928/House Bill 1185 and detailed in the fiscal and policy notes, the Comptroller must adopt specified regulations governing cannabis establishments. The Comptroller must also adopt regulations (1) establishing the procedures for the collection of taxes; (2) specifying the content, form, and timing of required reports; and (3) requiring that reports must be made available for inspection and retained for at least one year.

The bill also establishes that, notwithstanding any federal tax law to the contrary, a cannabis establishment may deduct from State taxes all ordinary and necessary expenses paid or incurred during the taxable year in carrying on a trade or business as a cannabis establishment. These ordinary and necessary expenses include a reasonable allowance for salaries or other compensation for personal services rendered.

Current Law:

Marijuana Taxation and Current Law

No State or local tax is currently imposed on the sale of cannabis. For the criminal law provisions related to marijuana, please refer to the fiscal and policy note for Senate Bill 928/House Bill 1185.

Public School Opportunities Enhancement Program

Chapter 32 of 2016 established the Public School Opportunities Enhancement Program and Grant to assist local school systems, public community schools, and nonprofit organizations in the State in expanding or creating extended day and summer enhancement programs and to assist nonprofit organizations in the State and community schools in expanding or supporting existing educational programming during the school day. For fiscal 2018 through 2021, the Governor must include \$7.5 million annually in the State budget for the program. Specified counties in which at least 50% of public school students as a percentage of full-time equivalent students qualify for free lunch under the National School Lunch Program are eligible to participate in the program. If the grantee is a local school system, the local school system must provide at least an equal match to State grant funding.

Workforce Development Programs

The workforce development programs provide employment, training, supportive, and related services to eligible job seekers, as defined in the federal Workforce Innovation and Opportunity Act, including individuals with barriers to employment, such as those who are low income or low skilled, to allow individuals to succeed in the labor market and to match employers with the skilled workers needed to compete in the global economy.

Maryland Substance Abuse Fund

The Maryland Substance Abuse Fund is used to assist local governments with expenditures related to substance abuse evaluation and treatment services, among other things. The Governor's proposed fiscal 2018 budget includes \$5,000 in program funding.

Background: According to the National Conference of State Legislatures (NCSL), 28 states, the District of Columbia, Guam, and Puerto Rico have comprehensive public medical cannabis programs. Additionally, another 17 states allow for the use of low THC (delta-9-tetrahydrocannabinol), high CBD (cannabidiol) products for medical reasons in limited situations or as a legal defense. NCSL also reports that 21 states (including Maryland) and the District of Columbia have decriminalized small amounts of marijuana. Prior to the November 2016 election, recreational use was legal in four states (Alaska, Colorado, Oregon, and Washington) and the District of Columbia. Of these states, marijuana licensing and taxes have been established for some time in Colorado, Washington, and Oregon, as discussed below.

Colorado

Voters approved Amendment 64 in November 2012, thereby generally legalizing marijuana. Proposition AA, approved in November 2013, established taxes on the recreational sale of marijuana. The Colorado Department of Revenue licenses establishments and administers state marijuana taxes. As of March 1, 2017, there are a total of 1,374 licensed marijuana establishments – 641 of which are cultivators followed by retailers (473), manufacturers (247), and testing facilities (13). Retail marijuana sales began on January 1, 2014.

Retail marijuana sales are subject to (1) a 10% marijuana state sales tax; (2) the state sales tax of 2.9%; and (3) local sales taxes, if imposed. A 15% excise tax based on the average market price of marijuana is also generally imposed on cultivators at time of the first sale or transfer of marijuana products. **Exhibit 1** shows the total State taxes remitted during calendar 2016, as reported by the Colorado Department of Revenue.

Exhibit 1
State Recreational Marijuana Taxes – Colorado
Calendar 2016
(\$ in Millions)

<u>Tax</u>	<u>Rate</u>	<u>Revenue</u>
State Sales Tax	2.9%	\$24.0
State Marijuana Sales Tax	10.0%	83.8
Cultivator Tax	15.0%	59.4
Total		\$167.2

Source: Colorado Department of Revenue

According to published reports, Colorado dispensaries reported a total of \$1.3 billion in recreational and medical cannabis sales in calendar 2016. Recreational sales comprised \$875 million of this amount.

Washington

Retail marijuana sales in Washington began on July 2014, after voters approved Initiative 502 in November 2012. Producers, processors, and retailers must be licensed by the Washington State Liquor and Cannabis Board. There are currently a total of 1,454 licensed establishments, of which 1,080 are licensed producers and processors and 374 are licensed retailers. As of July 2015, Washington imposes a 37% excise tax on retail

marijuana sales. Retail sales are also subject to a state sales tax of 6.5%. In addition, the gross income generated by producers, processors, and retailers is generally subject to the state business and occupation gross receipts tax. Marijuana excise taxes totaled \$16.4 million in calendar 2014, \$128.9 million in calendar 2015, and \$255.8 million in calendar 2016. Licensed recreational retailers sold an estimated \$696.4 million in marijuana products during calendar 2016.

Oregon

In 2014, Oregon voters approved Ballot Measure 91 which generally legalized recreational marijuana. In early 2015, the Oregon legislature enacted legislation implementing and regulating the recreational marijuana market. Also in early 2015, the Oregon Liquor Control Commission began the process of developing administrative rules and licensing procedures for producers, wholesalers, processors, testing laboratories, and retailers. In January 2016, the commission began accepting applications and issued the first producer licenses in April 2016 and issued the first retail establishment licenses in October 2016. According to the commission, it has issued more than 700 licenses, about one-half of which are retailers.

A state sales tax of 17% is imposed on the recreational marijuana sold by a licensed retailer. In addition, with voter approval, municipalities may also impose an additional 3% sales tax. Retail sales to medical marijuana cardholders or designated caregivers are exempt.

A limited amount of retail sales have occurred to date due to the time necessary to implement regulations, issue licenses, and deliver marijuana products to the retail market. During calendar 2016, the commission reported that producers harvested approximately 655 metric tons of usable marijuana (wet weight), most of which was harvested in October and November. Harvested marijuana is dried or cured for several weeks, thereby decreasing the product's weight by as much as 90%. However, the commission noted that many producers transfer harvested plants that have not been dried or cured. As of late January 2017, about 115 metric tons had been packaged, the vast majority of which had not yet been transferred to retailers. Of the marijuana items sold by retailers between October 1 and December 31, 2016, most (71%) was usable marijuana, followed by concentrate/extract (18%) and edibles/tincture (8%). In calendar 2016, published reports indicate that the Department of Revenue collected a total of \$60.2 million in marijuana taxes.

State Fiscal Effect: The bill imposes on sales of licensed cannabis a 9% State sales tax and an excise tax of \$30 per ounce. From the taxes collected, after the Comptroller deducts certain administrative costs, the net proceeds are distributed to the Cannabis Tax Distribution Fund. Accordingly, special fund revenues may increase significantly due to the imposition of the taxes.

Revenues in the fund may only be used to provide supplemental funding, as provided in the State budget, for the (1) Public School Opportunities Enhancement Program; (2) Maryland Substance Abuse Fund; (3) workforce development programs; and (4) impaired driving public education and law enforcement training. Accordingly, special fund expenditures for these purposes and Comptroller expenses will increase by a corresponding amount.

Additional Information

Prior Introductions: None.

Cross File: SB 927 (Senator Madaleno, *et al.*) - Budget and Taxation and Judicial Proceedings.

Information Source(s): Colorado Department of Revenue; Comptroller's Office; Oregon Liquor Control Commission; Washington State Department of Revenue; Washington State Liquor and Cannabis Board; Department of Legislative Services

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