



For Immediate Release
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The Grass May Not be Greener in DC
Taxes Present a Challenge to Medical Marijuana Producers

Washington, DC (June 24, 2010)—Reps. Jason Chaffetz (R-UT) and Jim Jordan (R-OH) introduced a resolution in Congress this week to strike down a Washington, DC, bill legalizing medical marijuana. Currently, 14 out of 50 US states have approved the medical use of marijuana for qualified patients and legislation is pending in 11 states and DC. Thus far, the debate over legalization has been centered on whether marijuana's apparent effectiveness in the treatment of pain, nausea, loss of appetite and other symptoms outweighs the negative effects of chronic marijuana use. As more states legalize production and distribution of medical marijuana, however, the tax ramifications promise to present a new platform for debate.

"The legal status of medical marijuana may be changing on the state level, but it remains illegal on the federal level, making it impossible for those who run medical marijuana businesses to take advantage of any of the tax deductions IRS permits other businesses," said Trudy Moore, EA, an enrolled agent in Stevensville, MT. "Medical marijuana producers may not deduct expenses such as the cost of goods sold and salaries. Generally, businesses that make or buy goods to sell may deduct the cost of goods sold from their gross receipts in computing business income and most businesses rely on this to reduce their taxes and keep them profitable."

The issue revolves around what is called "illegal source income" and the upshot may well be that the sellers of medical marijuana can't come out ahead financially because they are being taxed on their gross income. It may seem odd that IRS taxes money from federally illegal enterprises, but the practice was in place back in the days of Al Capone. Section 61 of the Internal Revenue Code states that all income is taxable, from whatever source derived.

Sen. John Sapien (D-NM) in January introduced a bill to the New Mexico state legislature that would apply a 25 percent excise tax on the value of medical marijuana sold by producers, as well as a gross receipts tax on its purchase by patients. If this kind of additional taxation from states looking to dig out of their financial holes becomes a trend, it will make survival extremely difficult for medical marijuana sellers who are already looking at an unfavorable federal tax situation. Ultimately, the fate of these businesses may be decided by taxation, rather than ethical or medical hurdles.

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The National Association of Enrolled Agents (NAEA) is the professional society representing tax preparers who have earned the distinction of "enrolled agent" (EA) from the IRS by passing a stringent three-part test on taxation, completing annual continuing education and abiding by a Code of Ethics. EAs are federally licensed to represent taxpayers before the IRS for audits, collections and appeals.

NAEA takes no position on whether medical marijuana should be available. Its intention is only to report on an interesting tax situation that has resulted from state legalization without federal legalization.