

# Retailers hit hard in Cuomo's tax idea

**SPECIAL REPORT: TAX LAW**



## High revenue

*Legalized cannabis is projected to boost New York's economy, but how would - and should - it be taxed?*

Hodgson Russ LLP partner Christopher Doyle is a member of the cannabis practice and leads the state and local tax practice.

BY PATRICK CONNELLY  
Buffalo Law Journal

Sooner or later, it was sure to be part of the conversation.

As Gov. Andrew Cuomo continued his push in January to legalize cannabis for recreational adult use, he outlined a three-tier structure on how the drug would be taxed.

"We have to do it in a way that creates an economic opportunity for poor communities," Cuomo said.

Cannabis is typically taxed based on weight, price or potency. States where legalized programs have been introduced have used the influx of money from taxes to pay for a variety of things.

The Marijuana Regulation and Taxation Act would amend existing laws to create a regulatory structure to oversee the licensure, cultivation, production, distribution, sale and taxation. It includes provisions on hemp products and expands the already-in-place structure for medical marijuana.

Under Cuomo's plan:

- The first tax is imposed on the cultivation of cannabis at the rate of \$1 per dry weight gram of cannabis flower and 25 cents per dry weight gram of cannabis trim.

- The second tax is imposed on the sale by a wholesaler to a retail dispensary at the rate of 20 percent of the invoice price.

- The third tax is imposed on the same sale by a wholesaler to a retail dispensary at the rate of 2 percent of the invoice price but collected in trust for and on account of the county in which the retail dispensary is located.

- All wholesalers would be required to register for renewal every two years for a fee of \$600.

"I think it's overly complicated, frankly, but I get what they're trying to do. They're trying to get the middleman to do all the collecting here," said Christopher Doyle, partner at Hodgson Russ LLP.

He is a member of the cannabis practice and the state and local tax practice leader for the firm.

"One area that they made more simple which I commend the state for is they've pretty much said no sales tax on adult-use

marijuana," Doyle said.

Attorneys at Harter Secrest & Emery LLP also assist clients in the realm, said Michael Roche. He compared Cuomo's cannabis tax plan to what's already in place in the food and beverage industry.

"I think the most important thing to take away from all of this is there is going to be a strict licensing regimen here," Roche said.

If the tax structure winds up as proposed, attorneys with experience in those other industries may be particularly helpful to clients regarding compliance, he said.

"We represent several breweries and other retail locations that have gone through that licensure process," Roche said. "We see ourselves filling a similar role."

Recreational cannabis for adults would represent a new marketplace in the state, Doyle said.

"I think there's going to be a whole new industry created in New York," he said. "We're a little late to the industry compared to folks in (some states). We're trying to get up to speed on what other issues are out there."

He and the practice team will jump in with both feet, Doyle said.

"We need to be able to advise our bank clients on their potential liability under federal banking laws that severely limit federal banks from allowing businesses selling marijuana to borrow," he added.

Cuomo's proposal, however, favors big businesses because entities that grow, process and distribute cannabis could not own retail stores, said Marc Gromis, a Williamsville attorney who specializes in cannabis law.

"The adult-use law should ensure that small-business owners and women- and minority-owned businesses be afforded a level playing field," Gromis said.

Meanwhile, he said medical marijuana dispensaries already established in the state would be exempt from that provision and be able to sell to consumers.

"(It gives) these multimillion-dollar companies a huge and unfair advantage over other retail store owners because they will be able to sell their retail products at a much lower price," Gromis said.

## How high?

Legalized cannabis would net approximately \$300 million in revenue for the state, Cuomo said.

Mitchell Moss, a professor of urban policy and planning at New York University, put the estimated figure at \$750 million and up in a report he compiled with researchers Kelsey McGuinness and Rachel Wise. The report's impetus was to show that legalized cannabis could fund improvements to infrastructure such as the New York City Subway.

"The great advantage of the legalization of cannabis is that it's a new revenue stream. It is not going to take money from other services," Moss said in an interview with WLNy-TV in New York.

The report said: "New York can learn from the experiences of Washington, Colorado, Oregon and California in determining how to raise revenues through retail and wholesale marijuana taxation. New York State is not a leader, but it need not be a laggard."

Using data from the 2016 National Survey of Drug Use and Health, researchers determined that the black market for marijuana in New York pulls in \$1.7 billion to \$3.5 billion a year. The first full year of a legal cannabis market would see 1.29 million consumers shift to be legal purchasers, the study found.

## Learning from other states

"There is immense opportunity for U.S. states to reap benefits from sales and excise taxes placed on legalized marijuana, as well as from licensing fees issued to retailers and producers," the NYU report said.

Higher-than-expected tax revenues were reported in Colorado, Washington and Oregon since legalization.

In 2018, in public hearings statewide on implementation, representatives of the state Department of Health outlined the findings of a study commissioned by Cuomo. That study, with help from the state Department of Taxation and Finance and other experts, found that cannabis should be taxed between 7 percent and 15 percent. That would net the state an estimated \$248.1 million to \$677.7 million in retail tax revenue, depending on price per ounce.

Colorado used the revenue to create the Marijuana Tax Cash Fund that supports school construction, expanded education, drug-prevention programs and law enforcement, the DOH report said. Munic-

ipalities there can opt not to participate in marijuana sales but then do not receive any of the funds.

Under Cuomo's proposed plan, counties and large cities could opt out.

"We're not telling them what to do but they have to affirmatively opt out of the program," Cuomo said.

The plan doesn't then exclude non-participating cities and towns from receiving funding as it did in Colorado.

"If this provision remains ... a separate provision should be added denying revenues derived from the state's cannabis program to any such county or city that bans cannabis businesses," Gromis said. "If they do not wish to allow cannabis businesses in their jurisdictions, they should not reap any of the revenue from the program."

To get started in New Jersey, a plan that hasn't become law called for a graduated rise in tax rate over time, starting low to entice black-market purchasers to become legal consumers. Cuomo said he would look at the tax rate in neighboring states of Massachusetts and New Jersey. Massachusetts has a 17 percent state excise and sales tax and local governments can add up to 3 percent to that.

## Next steps

What needs to happen next for cannabis to become legal?

A plan must be approved by the state Assembly and Senate and then signed by Cuomo. That could happen by mid-March when the governor must have his final budget wrapped up prior to the April 1 start of the state's new fiscal year.

With Democrats in control of both houses, many anticipate the law to pass with ease but it's unclear if legislators with different ideas may revise the Cuomo plan.

Cuomo wants the bill to take effect immediately, with sales beginning April 1, 2020.

From a tax perspective, participating businesses must be cognizant of liability and other legal implications, Doyle said.

"It's not like a regular business, from a federal income tax standpoint," he said. "You're going to have to be really careful that you build enough margin into your product to cover it."



GROMIS

## PROPOSED PLAN FOR TAXING ADULT-USE CANNABIS

**As part of Gov. Andrew Cuomo's proposed plan to legalize cannabis for adult use in New York, he outlined a three-tier tax structure in his budget proposal.**



Growers of cannabis would be taxed at a rate of **\$1 per dry weight gram** of cannabis flower and **25 cents per dry weight gram** of cannabis trim.



Retail dispensaries buying from wholesalers would be taxed at **20 percent of the invoice price**, with the money collected paid to the state.



On that same purchase, retail dispensaries would owe another **2 percent to the county** in which they operate.