

## SALT INSIGHTS

Jurisdiction: Multistate  
Tax Type: Individual/Corporate/Partnership  
Issue: State Tax Implications of Cannabis  
Date: January 10, 2019

### SYNOPSIS:

Currently, 46 states have laws permitting or decriminalizing cannabis or cannabis-based products for medical use. And 9 states: Alaska, California, Colorado, Maine, Massachusetts, Nevada, Oregon, Vermont, Washington and the District of Columbia, have legalized recreational cannabis. As states continue to legalize cannabis and the growing, production and use of cannabis increases, taxation of cannabis is ever more murky, particularly as it relates to the interplay between federal and state taxation.

The state and local tax implications of selling cannabis can be significant. Currently 45 states impose a specific sales tax on cannabis ranging between 10% and 37%, which in most states exceeds the general sales tax rate levied on other products. Further, Alaska, because they do not have a state sales tax, subjects cannabis growers to a tax of \$500 per ounce sold to dispensaries or retailers.

Also complicating the landscape is the extent that expenses and or “costs” are deductible for entities involved in the manufacture and sale of cannabis products for federal purposes. The most recent guidance can be found in two federal court cases; *Alterman v Commissioner of Internal Revenue* (“Alterman”) T.C. Memo. 2018-83, and *Loughman vs. Commissioner of Internal Revenue* (“Loughman”), T.C. Memo. 2018-85. The seminal issue in both cases is the application of IRC §280E. In *Alterman*, the Court held, that IRC §280E operates to disallow a cannabis businesses’ tax deductions and credits to a business **trafficking in a controlled substance**. And, the Court in *Loughman* found that IRC §280E disallows the deduction of wages paid to S Corporation shareholders. However, these cases only address the issue from a federal perspective.

### INSIGHT:

Investors and businesses that are deemed to be in cannabis need to consider the classification of cannabis as medical or recreational use; the numerous cannabis sales tax implications; and the repercussions of the disallowance of deductions and credits related to the trafficking of a controlled substance. These complex state and local tax issues should be discussed with state and local tax professionals. Contact SimekScott.

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