

# The Best Practice Drawn From the Cannabis Taxation Lessons in California, USA

<sup>1</sup>Dorkrak Daoruang, <sup>2</sup>Gridsada Jamjuntr, <sup>3</sup>Yannakorn Toprayoon

<sup>12</sup>Academicien, Long Beach, CA, USA

<sup>3</sup>The Association of Researchers of Thailand, Thailand

<sup>1</sup>Email: d\_daoraung@yahoo.com

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## Abstract

In 2018, the state of California and Massachusetts, and Maine USA announced the legalized use of marijuana for "entertainment". It is the seventh state in the United States to allow the recreational use of marijuana, while 29 other states allow the use of marijuana for medical purposes. The latest research from Gallup reveals that in 2017, over 64% of the US adult population advocated the legalization of Cannabis. By seeing that there is more benefit than harm, over 57% of the voters in California support the legalization of recreational cannabis. The objective of this study is to identify the lessons drawn of the taxation on marijuana in the United States.

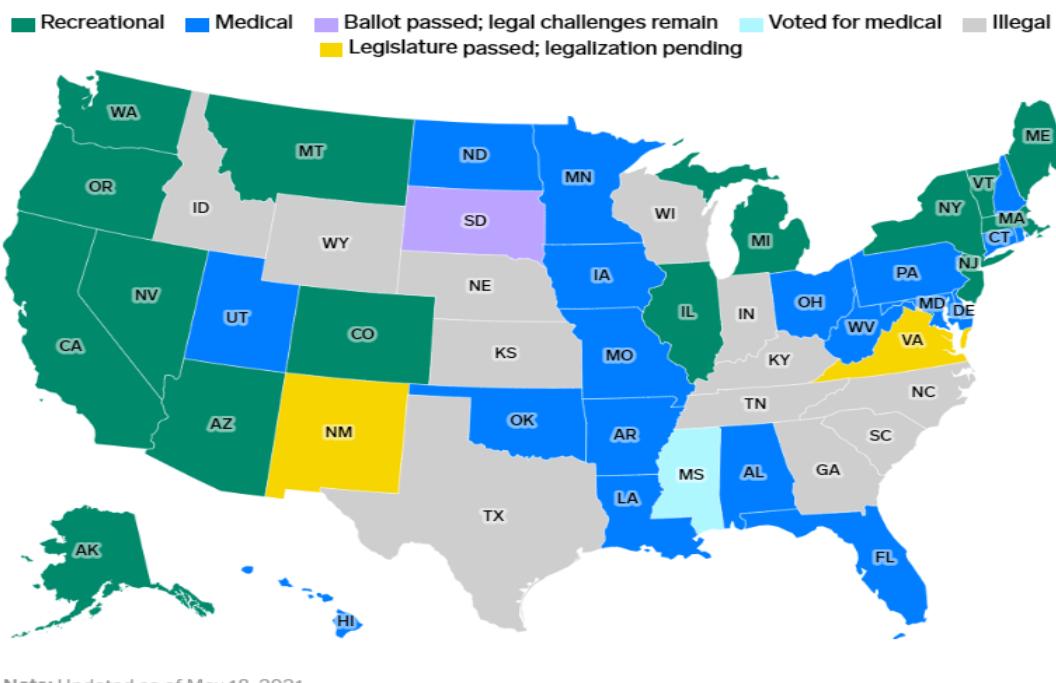
The results of the research are as follows: The legal cannabis industry will generate more than \$ 40 billion in revenues and create more than 400,000 jobs in the United States by 2021. The government will tax \$ 4 billion in three years. Worth not less than 15 billion US dollars (approximately 480,000 billion baht), however. Although local law recognizes the status of the sales and use of cannabis in state-run areas, national laws still classify Cannabis as a Schedule 1 Narcotic, which prohibits the planting, possession, and trading. Therefore, the California cannabis business faces two major problems in the cannabis industry: Some banks have not yet endorsed marijuana-related transactions, because they want to avoid money laundering charges. This has caused a large number of unverified money migration problems. Besides, local authorities under the State have different policies.

**Keywords:** Best practice, cannabis taxation, California.

## Introduction

The estimated origin of early cannabis derives from the ancient Central Asia, where the temperature and environment were temperate and moist. Indigenous people began utilizing oil from the cannabis plant for cooking, fuel, medicine, and soap. The stalks provided long, strong, and durable fibers used to weave twine ropes and baskets, useful for many purposes. Psychoactive effects are thought to have been encountered shortly after the discovery of the multipurpose plant, leading to its use in ritual ceremonies and traditions.

Main article: Cannabis in California July 1975: Senate Bill 95 reduced the penalty for possession of 1 oz (28 g) or less of cannabis to a citable misdemeanor. Budman (1977) November 1996: first state to legalize medical marijuana when Proposition 215 passed by 56%. Kaye, Jeffrey (1996). November 2016: Proposition 64 passed by 57% to 43%, legalizing sale and distribution, effective January 1, 2018.



**Fig. 1.** All the states where cannabis is legal (Source: <https://www.businessinsider.com/legal-marijuana-states-2018-1#alaska-1>)

The cannabis-related business (cannabis) is growing and gaining a lot of attention in the United States, while many companies are listed on the stock exchange, making it an attractive stock for investors, with excellent performance. This makes it likely that many cannabis-related businesses will grow more this year. The Motley Full reports that three companies involved in the US cannabis industry have benefited from the booming cannabis trend. Starting with Cresco Labs, the largest cannabis-related product wholesaler in the US takes a 60% market share in the United States. It distributes cannabis-derived products from brands such as Remedi, hemp extract, tinctures, capsules, and RSO (Rick Simpson oil) to "min Mindy's, a cannabis-containing snack and food brand. This includes products for smoking cannabis such as "Vape Pens" to cannabis strains selected by the country's top growers.

Business Wire reported that Cresco Labs' Q3/2020 revenue was \$153.3 million (\$4.6 billion), an increase of \$59 million, or 63% from the previous quarter, the third consecutive quarter of revenue growth. grow more than 40% (<https://www.businesswire.com/news/home/20201013005414/en/Cresco-Labs-to-Report-Third-Quarter-2020-Financial-Results-on-November-18th-2020>).

The California Department of Tax and Fee Administration (CDTFA) is a government agency in the United States responsible for taxing marijuana and issuing licenses for distributors. In California, cannabis businesses must be registered with CDTFA for a seller's

license, and file sales and use tax returns regularly. The interest page has all the steps listed in Adjusting California's Cannabis taxes.

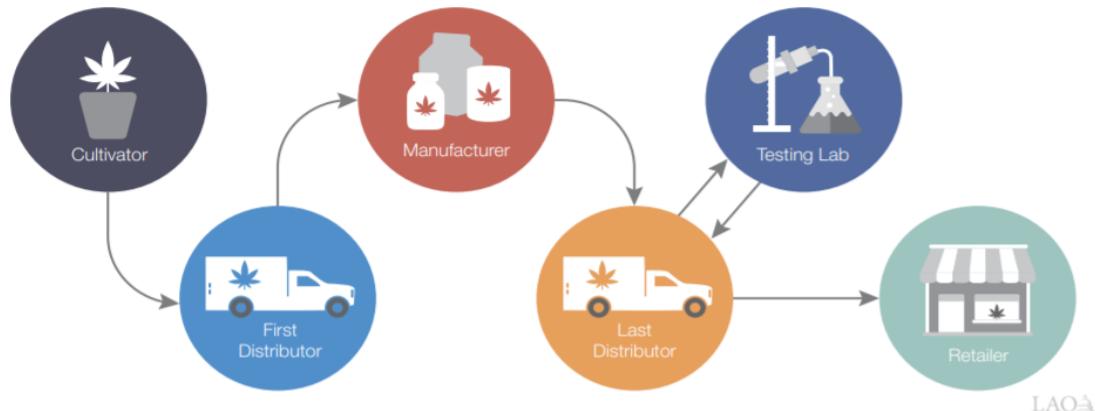
Report Required by Proposition 64. Proposition 64 established two state excise taxes on cannabis. The first is a 15 percent retail excise tax, effectively a wholesale tax under current law. The second is a tax based on the weight of harvested plants, often called a cultivation tax. The measure authorizes the Legislature to amend its tax provisions without voter approval, but the scope of this authorization is unclear.

In November 2016, California voters approved Proposition 64, which legalized the nonmedical use of cannabis (typically called recreational or adult-use) and created a structure for regulating and taxing it. Proposition 64 also directed to submit a report to the Legislature by January 1, 2020, with recommendations for adjustments to the state's tax rate on cannabis to achieve three goals: undercutting illicit market prices, ensuring sufficient revenues are generated to fund the types of programs designated in the measure, and discouraging use by persons younger than 21 years of age. This report responds to that requirement, which includes:

- (1) background information on cannabis and its legalization in California,
- (2) a discussion of the effects of adjusting the tax rate,
- (3) an assessment of other potential changes to California's cannabis tax structure, and
- (4) recommendations for the Legislature.

Cannabis Legalization in California Under the Federal Law: The U.S. Department of Justice (US DOJ) does not prosecute most cannabis users and businesses that follow state and local cannabis laws if those laws are consistent with US DOJ priorities, such as preventing cannabis from being exported to other states. Despite federal law, California and many other states have taken steps to legalize and regulate cannabis in the past few decades. However, these states have not been able to include exported cannabis in these efforts due to federal prohibitions. In California, exports likely account for a large share of California-grown cannabis—roughly 80 percent by some recent estimates.

#### The Cannabis Supply Chain in California



**Fig. 2.** The cannabis supply chain in California  
 (Source: <https://lao.ca.gov/reports/2019/4125/cannabis-taxes-121719.pdf>)

## **Sales Taxes on Cannabis**

Sales Taxes Apply to Tangible Goods, Including Cannabis: California's state and local governments levy a sales and use tax (commonly known as a sales tax) on retail sales of tangible goods. The rate varies across the state, ranging from 7.25 percent to 10.5 percent, with a statewide average of 8.6 percent. Cannabis products are tangible goods, so their retail sales generally is subject to this tax.

Legislative Analyst's Office Definition of Cannabis Taxes does not include sales tax. Two reasons for not including the sales tax, as follows: First, as discussed in the 2018 report, Taxation of Sugary Drinks, changes in excise tax rates, such as cannabis tax rates, primarily affect the price of one specific type of good relative to the prices of other items that consumers buy. The sales tax applies to a wide range of goods, so it does not have this property. Second, as described above, Proposition 64 (2016) requires that state cannabis tax revenues be allocated to purpose specified by the measure. In contrast, sales tax revenue goes to the state's General Fund and local programs, regardless of whether that revenue comes from cannabis sales or sales of other goods.

The United States is an interesting model for teaching cannabis taxation lessons: To study how the management of the public sector should be carried out appropriately and will generate large sums of money returned to the local and government for use in the administration of the country.

## **Research Objective**

To study by taking lessons from taxation in the cannabis business in California. United States.

## **Research Methodology**

This study used a research model to obtain information from papers, works published in the form of articles, research report Tax Guide California as well as websites that include information related to the cannabis business. Analyze and present the results by summarizing the content and in descriptive presentation.

### ***The Best Result of the Transcript***

Economic Impact of Cannabis in San Diego County indicates that the cannabis industry has gone through many series of events that have brought it to the billion-dollar industry it is today. Since its move from the illicit market, to the legalization of medicinal cannabis in 1996, and continued positive shifts of perceptions of cannabis, there has been exponential growth in the industry. The Office of Business Research and Analysis (OBRA) has analyzed the general impact of the cannabis industry in San Diego County. Throughout this research, OBRA sought to find how adult-use and medicinal cannabis sales increases in

revenue and influence the community regarding finances, police enforcement, cannabis license types, public health, and social equity.

The cannabis industry yields a considerable amount of revenue to municipalities from cannabis city taxes. Data from the public records requests from the cities of San Diego, La Mesa, and Vista illustrate the amount of money by quarter that each city has brought in since they legalized medicinal cannabis and or adult-use cannabis. In 2019, medicinal cannabis taxation brought in over \$1M to the city of Vista. In 2019, adult-use cannabis taxation yielded over \$12M to the city of San Diego and \$183K to the city of La Mesa. As additional dispensaries are added, revenue numbers are expected to grow exponentially.

Cannabis business license holders in San Diego County completed a survey arranged by OBRA, that was used to analyze the industry's demographics of those who hold cannabis licenses in the San Diego County region. The survey indicated that 68% of cannabis business license holders were White, 14% Hispanic, 7% African-American, 3% Middle Eastern, 4% American-Indian, and 4% Asian. Additionally, 87% of cannabis business license holder participants were male and 13% were female. Their surveys indicates that racial diversity within the cannabis industry remains an issue. It is advisable for jurisdictions in the County to look into other cities that have successfully implemented social equity programs to increase the diversity in potential cannabis license holders. Establishing a social equity program in San Diego County could result in more racial diversity and equity among cannabis license holders.

As more new entrants emerge, the cannabis industry will continue to increase in size as long as regulations allow for it. This will result in more revenue brought in by cannabis taxation.

Ten U.S. states, Canada, and Uruguay have passed laws to legalize the production and sale of cannabis for non-medical purposes. Available research has documented rapidly falling prices and changing product mixes, but many details are not well understood: particularly, the popularity, prices, and product characteristics of different cannabis edibles and extract-based products – each offering different ways to consume cannabis, with unclear health consequences (Steven, 2019).

A LAO estimate of the average cumulative tax rate, including taxes on cultivation, manufacturing, distribution, testing, and retail: California's Cannabis Taxes Tax State retail excise tax Ad valorem tax primarily on wholesale sales Nominally 15 percent of the retail price.

In practice:

- For most sales, administratively determined percentage of the wholesale price (currently 27 percent)
- For some sales, 15 percent of retail price State cultivation tax Weight-based tax on harvested cannabis • \$9.65 per ounce of dried cannabis flowers
- \$2.87 per ounce of dried cannabis leaves
- \$1.35 per ounce of the fresh cannabis plant

- Local taxes Varies; most commonly ad valorem or based on square footage Varies—on average, roughly equivalent to 14 percent tax on retail sales

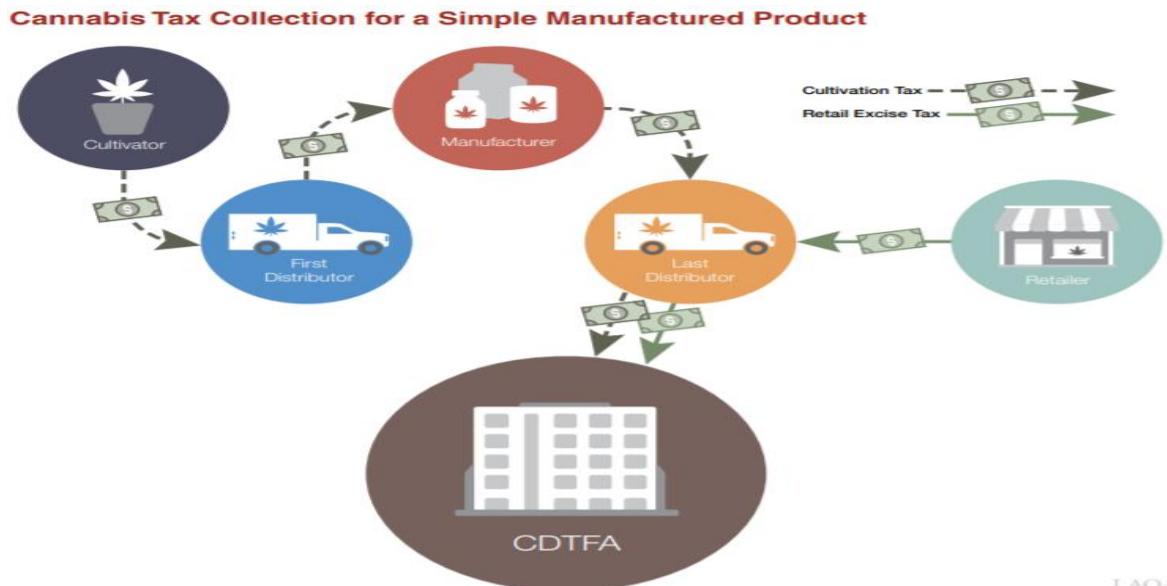
**Table 1.** California's cannabis taxes**California's Cannabis Taxes**

Tax	Type	Rate on January 1, 2020
State retail excise tax	Ad valorem tax primarily on wholesale sales	Nominally 15 percent of retail price. In practice: <ul style="list-style-type: none"> <li>• For most sales, administratively determined percentage of wholesale price (currently 27 percent)</li> <li>• For some sales, 15 percent of retail price</li> </ul>
State cultivation tax	Weight-based tax on harvested cannabis	<ul style="list-style-type: none"> <li>• \$9.65 per ounce of dried cannabis flowers</li> <li>• \$2.87 per ounce of dried cannabis leaves</li> <li>• \$1.35 per ounce of fresh cannabis plant</li> </ul>
Local taxes	Varies; most commonly ad valorem or based on square footage	Varies—on average, roughly equivalent to a 14 percent tax on retail sales <sup>a</sup>

<sup>a</sup> LAO estimate of the average cumulative tax rate, including taxes on cultivation, manufacturing, distribution, testing, and retail.

Source: Gabriel Petek Legislative Analyst (2019)

Retail Excise Tax. Retailers generally must pay the retail excise tax to final distributors when they make wholesale purchases. These distributors then remit the retail excise taxes to CDTFA. Retailers must make these payments before they sell the products to consumers, so the tax is based directly on the wholesale price (the price that retailers pay to distributors) rather than the retail price (the price that consumers pay to retailers). Pursuant to Chapter 27, CDTFA sets the tax based on its estimate of the average ratio of retail prices to wholesale prices—commonly known as a “markup.” CDTFA’s current markup estimate (as of January 1, 2020) is 80 percent. Due to the 15 percent statutory tax rate and the 80 percent markup estimate, the current effective tax rate on wholesale gross receipts is 27 percent (15 percent x [100 percent + 80 percent]).



**Fig. 3** All processes in the cannabis business are taxable (Source: Gabriel Petek Legislative Analyst, 2019)

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Table 3 outlines the number of businesses, city tax revenue, estimated gross taxable sales, and the general economic impact of individual cannabis businesses for each quarter, since the second quarter of 2018, for the City of La Mesa.

**Table 3.** La Mesa estimated local cannabis market value by quarter

Adult - Use Cannabis Estimated Market Value by Quarter in La Mesa				
Tax Period (Quarter)	Number of Businesses	Tax Revenue	Gross Sales	Impact per Business
2nd Q 2018 (Apr-Jun)	0	-	-	-
3rd Q 2018 (July-Sep)	0	-	-	-
4th Q 2018 (Oct-Dec)	1	-	-	-
1st Q 2019 (Jan-Mar)	1	\$49,415	\$1,235,367	\$1,235,367
2nd Q 2019 (Apr-Jun)	1	-	-	-
3rd Q 2019 (July-Sep)	1	\$29,815	\$745,384	\$745,384
4th Q 2019 (Oct-Dec)	3	\$104,438	\$2,610,959	\$870,320
1st Q 2020 (Jan-Mar)	3	\$142,663	\$3,566,576	\$1,188,859
2nd Q 2020 (Apr-Jun)	3	\$263,860	\$6,596,505	\$2,198,835

Source: Information retrieved via City of La Mesa public records request on August 12, 2020.

Source: Information retrieved via City of San Diego public records requests on August 12, 2020 and November 2, 2020.

The estimated gross taxable sales were derived by applying a 4% tax rate to city revenue. The revenue figures for La Mesa in the second quarter of 2019 are not available; the City of La Mesa finance department maintains that there are “no responsive records for this period (Piper, personal communication, November 2, 2020).” The City of La Mesa further

explained that “an omission in the La Mesa Municipal code from the original tax measure was discovered and corrected at the end of quarter 2. No taxes were collected during that quarter until the correction was made (R.C., Piper, personal communication, November 16, 2020).” It can be seen that the trend of tax collection is increasing every year. This could mean that the business is growing.

#### TYPES OF CANNABIS TAXES TO CONSIDER

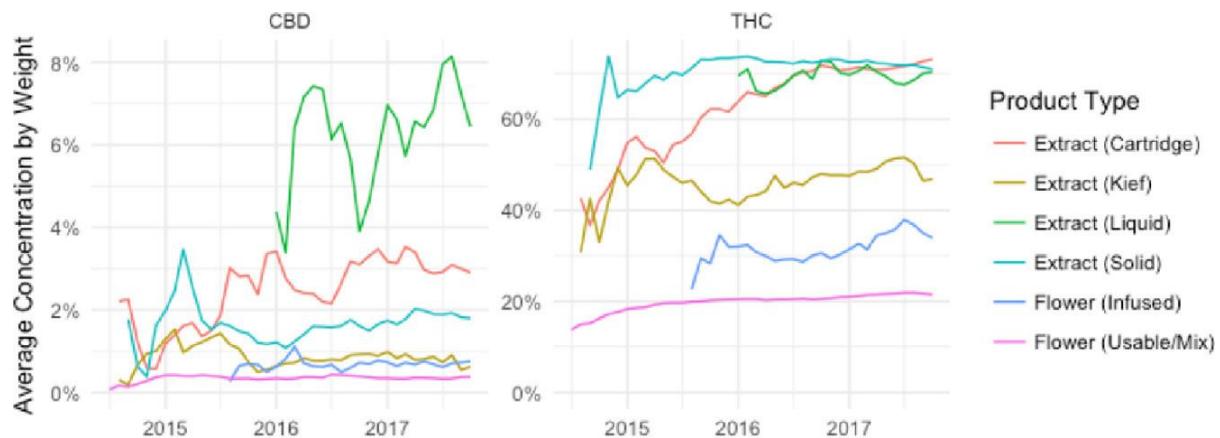
- Basic Ad Valorem Tax. Under a basic ad valorem tax, the amount of tax due is a percentage of the price. The sales tax and California’s current retail excise tax on cannabis are examples of ad valorem taxes.
- Weight-Based Tax. Under a weight-based tax, the amount of tax due is based directly
  - on the weight of the product. The rates can vary depending on the part of the plant (for example, flower or leaves) or its condition (for example, dried or fresh). California’s current cultivation tax is an example of a weight-based tax.
- Potency-Based Tax. Under a potency-based tax, the amount of tax due depends only on the potency of the cannabis product. For example, Canada’s cannabis tax system includes a rate of \$0.01 Canadian (roughly three-quarters of a cent of the U.S.) per milligram of tetrahydrocannabinol (THC) in certain types of cannabis products. Hereafter, we use “potency-based” primarily to refer to this simple THC-based structure. However, potency-based taxes could take a variety of forms—for example, incorporating other cannabinoids in addition to THC.
- Tiered Ad Valorem Tax. A tiered ad valorem tax is similar to the basic ad valorem tax, but with multiple rates. These rates could depend on potency and/or the type of product. For example, Illinois has set three different ad valorem tax rates on cannabis-based on potency and product type: 10 percent on cannabis flower and other products with THC concentrations below 35 percent; 20 percent on cannabis infusions, such as edibles; and 25 percent on products with THC potency above 35 percent, such as concentrates. Accordingly, a potency-based tax is a direct, consistent way to use taxes to discourage harmful use, so it scores well on this criterion.

#### Comparing Different Types of Cannabis Taxes

Scale From  (Worst) to  (Best)

	Basic Ad Valorem Tax	Weight-Based Tax	Potency-Based Tax	Tiered Ad Valorem Tax
Reducing Harmful Use				
Raising Stable Revenue				
Administration and Compliance				

**Fig. 4.** Comparing different types of cannabis taxes (Source: Gabriel Petek Legislative Analyst, 2019)



**Fig. 5.** Average concentration by weight (Source: Steven, 2019)

From the information, it was found that the extracts were accounted for 28.5% of sales and were labeled “dabs” and half as “cartridges.” The price per 10 mg THC was about \$3 for the consumable item, 70 cents for the extract, and 30–. 40 cents for cannabis flowers. Solid concentrates offer the lowest cost THC among extract products. Prices have continued to decline but have slowed down. High-CBD chemotherapy is becoming more common. But it is still almost nonexistent in floral cannabis and is rare (1% of sales) in extract products.

## Discussion

The cannabis-related business (cannabis) is growing and gaining a lot of attention in the United States, with many companies being listed on the stock exchange, making it an attractive stock for investors. with excellent performance. This makes it likely that many cannabis-related businesses will grow more this year. The Motley Full reports that three companies involving in the US cannabis industry have benefited from the booming cannabis trend. Starting with Cresco Labs, the largest cannabis-related product wholesaler in the US has a 60% market share in the United States following Research of Steven (2019). As Washington's recreational cannabis market has developed over three and a half years, trends identified in that market may serve as an early indication of potential issues in other states.

Legislators and regulators in other jurisdictions with commercial non-medical cannabis markets may wish to establish policies that are responsive to these trends in product popularity, price, and potency. There is a comparative study on the management of the cannabis business but from the point of view of the policy. Taupachit1 and Kessomboon (2021) state that cannabis prescribing system for medical use involves prescribing by

physicians, having the registration system for patients being approved by the government agencies, and often a central unit called the "Cannabis Agency" under the Ministry of Health is installed for control. Israel, Canada, Germany, and more than 50 percent of the states in the United States currently allow cannabis use in form of the herbs. While cannabinoids are widely allowed, some countries limit further.

The results of the study and the opinions of the experts were consistent, i.e., agreeing with the medical use of cannabis and policy formulation appropriate to the context, allowing cannabis use in Thailand by service providers or for self-treatment, setting up comprehensive systems from production, planting, distribution, use, including advertisement control, preventing monopoly from patents and cannabis abuse.

## Conclusion

In this report, we analyze several decisions regarding potential changes to California's cannabis taxes. The first and most basic decision is the type of tax to levy. We recommend that the Legislature replace the state's existing cannabis taxes with a tax designed to reduce harmful cannabis use more effectively—namely, a potency-based tax or tiered ad valorem tax. That said, if the Legislature prioritizes administration and compliance more highly, a basic ad valorem tax is worth considering. We further recommend changes to the way the state collects cannabis taxes (the taxed event and point of collection) and to the tax rate itself. Our recommended range of tax rates reflects the three goals outlined in the statute: undercutting illicit market prices, generating sufficient revenues, and discouraging youth use. In pursuit of these goals, we also encourage the Legislature to consider complementing tax changes with nontax policies.

## Suggestions

Government policy proposals should establish a federal cannabis agency to cover the entire system throughout the supply chain from planting, processing, transportation distribution and use by the Ministry of Health should have a robust system. Medical marijuana treatment to suit the context of Thailand has been allowed the use of cannabis in medicinal and medicinal forms. There is a prescription system for both modern medicine and Thai traditional medicine. The government should control the misuse of anti-monopoly and establish an appropriate patent system. The government should give the patients the right to

access this drug, which is a fundamental right of the patient and to help reduce drug imports. All processes that are traded or sold are subject to different taxes. For example, buying to extract medicines to keep at a low rate to promote production. Recreational sales may be charged at a high rate, in order to use the tax revenues to develop the country.

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