

The National Cannabis Economy

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JOINT ECONOMIC COMMITTEE
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Cannabis, or marijuana, is the most commonly used illicit drug in the United States. Though illegal at the federal level, states are taking action to legalize cannabis—from recreational use in states like Colorado and Maine to medical use in New Mexico and Florida. A record 66 percent of Americans now support legalizing cannabis, a dramatic increase from just 12 percent in 1969.¹

The legalization of cannabis has significant implications for state economies, as well as the national economy. The industry totaled more than \$8 billion in sales in 2017, with sales estimated to reach \$11 billion this year and \$23 billion by 2022.² There were more than 9,000 active licenses for cannabis businesses in the U.S. in 2017, with the industry employing more than 120,000 people.³

As more states move to legalize cannabis, these numbers will only continue to rise, potentially providing a new stream of revenue and jobs to local economies. But to realize these benefits, policymakers must address conflicts between state and federal regulations that impede the growth of the cannabis economy.

Federal Cannabis Regulation

Derived from the cannabis sativa plant, cannabis is a psychoactive drug used for both recreational and medical purposes. It has been federally classified as a Schedule I substance under the Controlled Substance Act (CSA) since 1970, making it a federal crime to grow, sell, or possess the drug. Schedule I substances are also defined as having no currently accepted medical use and a high potential for abuse.

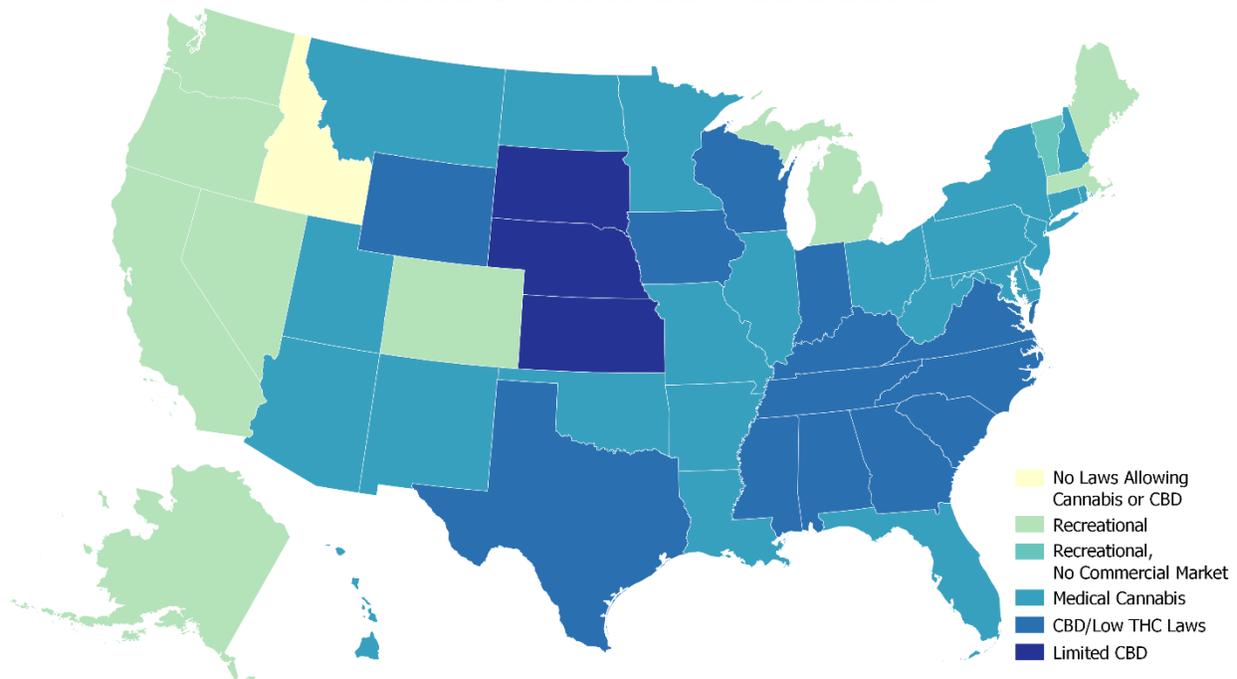
The CSA equates cannabis to be as dangerous as heroin and lysergic acid diethylamide (LSD), and more dangerous than cocaine and methamphetamine. There have been zero recorded lethal overdoses from cannabis, however, while cocaine and methamphetamine took more than 25,000 lives combined in the U.S. in 2017.⁴

Cannabis Laws by State

A majority of states have taken action to legalize cannabis in some form, despite its federal classification. Today, recreational cannabis is legal in ten states and D.C. (with Vermont and D.C. prohibiting commercial sales), while 33 states have legalized medical cannabis for patients with a valid medical prescription.⁵ Additionally, 13 states have decriminalized cannabis, imposing civil fines for small amounts of cannabis possession rather than jail time.⁶ Michigan, Missouri and Utah approved cannabis measures in the 2018 midterms, with Michigan legalizing

recreational use and Missouri and Utah legalizing medical cannabis. States that have taken action on cannabis are still in direct conflict with existing federal laws, however.

Status of State Cannabis Laws



Federal Prohibition Creates Barriers to Banking

Conflict between state and federal cannabis laws has led to a variety of constraints on the industry's growth. The Obama administration attempted to clarify these conflicts, issuing financial guidance from the Department of the Treasury and legal guidance from the Department of Justice. Former Attorney General Jeff Sessions rescinded these directives, however, creating greater uncertainty for the industry.⁷ Although DOJ has not recently disrupted any cannabis businesses operating legally under state laws, it could choose to enforce federal restrictions at any time. To date, the Trump administration has yet to clarify its stance on the issue.

Even where legal under state law, banks and other financial institutions can face penalties for working with cannabis businesses. Banks that knowingly work with cannabis businesses are in violation of federal anti-money laundering laws, subjecting these banks to potential asset seizure by the Department of Justice (DOJ).⁸ These anti-money laundering laws require banks to regularly file Suspicious Activity Reports when working with cannabis businesses, which can be

burdensome and costly to comply with.⁹ They are also required to conduct thorough inspections of cannabis businesses, adding yet another complex layer of regulation.¹⁰

These regulations have prevented the majority of cannabis businesses from accessing capital and traditional banking services. Today, 411 banks were actively providing depository services to cannabis businesses, but just 30 percent of cannabis businesses have access to traditional banking services.¹¹

Banks that do work with cannabis businesses also pass on the costs of regulation to businesses.¹² The lack of permanent banking solutions has forced the remainder of these businesses to operate with cash only, creating security problems and complications for paying employees. States have tried to work around these banking restrictions by authorizing cannabis credit co-operatives (state-chartered banks to work with cannabis businesses), but the Federal Reserve has refused to authorize any of these institutions thus far.¹³

Conflict Between Federal and State Laws Harms Small Businesses

Conflicts between state and federal cannabis laws have also created barriers for small businesses. At the federal level, Section 280E of the tax code prohibits businesses from deducting ordinary business expenses associated with the “trafficking” of Schedule I substances. Originally intended to penalize black market operators, this provision denies cannabis vendors operating legally under state law the same tax deductions available to other small businesses. This leaves many cannabis businesses with an effective tax rate between 40 and 70 percent, more than twice as high as other businesses.¹⁴ This crushing tax burden incentivizes legal cannabis businesses to remain on the black market and engage in tax evasion, while punishing businesses that stay within the law.¹⁵

Effect of Section 280e on Cannabis Businesses

| Typical Deductions | Cannabis Businesses | Non-Cannabis Businesses |
|---------------------------|---------------------|-------------------------|
| Cost of Goods Sold | Deductible | Deductible |
| Employee Salaries | Non-Deductible | Deductible |
| Utility Costs | Non-Deductible | Deductible |
| Health Insurance Premiums | Non-Deductible | Deductible |
| Marketing Costs | Non-Deductible | Deductible |
| Repairs and Maintenance | Non-Deductible | Deductible |
| Rental Fees | Non-Deductible | Deductible |
| Payments to Contractors | Non-Deductible | Deductible |

Source: IRS.gov, National Cannabis Industry Association

Cannabis businesses also face unique challenges accessing capital to launch or grow their operations. Financial institutions are prohibited from granting loans to cannabis businesses, making it difficult for vendors to raise capital. Start-up costs for opening and operating a small dispensary typically range between \$250,000 and \$750,000. While most small businesses owners can obtain a business loan from a bank, cannabis business owners are forced to rely on individual investors or their own money.¹⁶ These obstacles have created both racial and wealth inequalities in the cannabis industry, disproportionately benefiting individually wealthy business owners.¹⁷

The Medical Benefits of Cannabis

Federal regulations are also restricting researchers' ability to conduct large-scale, well-controlled clinical trials on the medical effects of cannabis. Researchers who want to study cannabis are forced to obtain approvals from several different agencies and engage in a complex application process. These also face difficulties in accessing the types and quantities of research-grade cannabis needed for comprehensive studies.¹⁸ To date, the Food and Drug Administration (FDA) has not approved any drug containing cannabis, though it has approved the use of cannabidiol (CBD), a naturally occurring constituent of cannabis, for two rare epileptic conditions.¹⁹

Despite the research challenges, there is a large body of evidence that cannabis is effective for treating chronic pain. There is also suggestive evidence that cannabis is effective for decreasing weight loss associated with HIV/AIDS.²⁰ Additionally, several studies have shown medical cannabis is associated with lower prescription opioid use.²¹ There were over 2 million registered medical cannabis patients in the U.S. as of May 2018.²²

Social Impacts of Cannabis Legalization

States that have legalized recreational cannabis have drastically reduced their arrests. The number of arrests for cannabis possession and sales/manufacturing in Alaska declined by 93 percent from 2013 to 2015, while possession charges in Colorado dropped by almost 90 percent from 2012 to 2015. Washington, California and Oregon have also substantially decreased their cannabis arrests.²³ With the cost of housing an inmate averaging over \$30,000 annually per prisoner, these social justice improvements are saving states millions of dollars.²⁴

Legalizing cannabis has also improved the efficiency of police departments. Washington and Colorado, for example, saw an increase in their overall crime clearance rates after legalization in 2012. Clearance rates for crimes such as burglary and motor vehicle theft in particular saw dramatic increases, while the national trends remained flat. Furthermore, the researchers found that legalization did not negatively impact clearance rates for any specific crime type.²⁵

With increased revenue from cannabis taxes, states are spending more on important social programs, including schools and drug treatment programs.²⁶ At the local level, cannabis tax revenue has had a transformative effect for small towns. Towns are using this revenue to fix city streets, fund college scholarships, and hire more police officers.²⁷ Small businesses are also seeing gains from the cannabis boom, including improved economic conditions and support from local governments.²⁸

Going Forward

There are a variety of proposals to fix the conflicts between state and federal cannabis laws. Of these proposals, the bipartisan STATES Act has drawn support from President Trump and the cannabis industry.²⁹ The STATES Act would amend the Controlled Substances Act so that its provisions no longer apply to individuals acting in accordance with state laws. Importantly, the bill would also clarify that financial transactions with state-legal cannabis businesses are not drug-trafficking, creating a solution for financial institutions and the cannabis industry.³⁰

Several states could be next to legalize cannabis. A bill to legalize cannabis is progressing through the New Jersey legislature, while New York lawmakers are preparing to consider similar legislation this year.³¹ Similarly, newly elected governors in New Mexico, Minnesota, Illinois, and Connecticut have all voiced support for legal cannabis, positioning their states to consider the issue.³²

Conclusion

The growth of the cannabis economy presents opportunities for greater job creation, more tax revenue, and better patient care. But current conflicts between state and federal law threaten to impede social and economic growth. Going forward, lawmakers and regulators should prioritize solutions that promote greater research into the health effects of cannabis and reduce regulations that restrict the industry's ability to conduct business.

Click [here](#) for snapshots of each state that has legalized recreational cannabis, excluding Maine and Vermont, as neither state has set up a recreational marketplace.

Click [here](#) for a table with data for all states that have legalized cannabis in some form.

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- ¹ https://news.gallup.com/poll/243908/two-three-americans-support-legalizing-marijuana.aspx?g_source=link_NEWSV9&g_medium=TOPIC&g_campaign=item &g_content=Two%2520in%2520T hree%2520Americans%2520Now%2520Support%2520Legalizing%2520Marijuana
 - ² <https://bdsanalytics.com/new-report-legal-marijuana-markets-projected-to-reach-23-4-billion-employ-nearly-a-half-million-americans-by-2022-effective-end-of-federal-prohibition-is-in-sight/>
 - ³ <https://money.cnn.com/2018/01/31/news/marijuana-state-of-the-union/>
 - ⁴ <https://www.drugabuse.gov/related-topics/trends-statistics/overdose-death-rates>
 - ⁵ <http://www.ncsl.org/research/health/state-medical-marijuana-laws.aspx>
 - ⁶ <https://www.mpp.org/issues/decriminalization>
 - ⁷ <https://www.justice.gov/iso/opa/resources/3052013829132756857467.pdf>
<https://www.cnn.com/2018/01/04/politics/jeff-sessions-cole-memo/index.html> and
<https://www.njlawblog.com/2018/09/articles/cannabis-lawyer/banking-cannabis-industry/>
 - ⁸ <https://crsreports.congress.gov/product/pdf/R/R44782>
 - ⁹ <https://www.nbcnews.com/think/opinion/legal-marijuana-businesses-deserve-better-be-treated-potentially-criminal-enterprises-ncna867816>
 - ¹⁰ https://www.nytimes.com/2018/01/04/magazine/where-pot-entrepreneurs-go-when-the-banks-just-say-no.html?_r=0
 - ¹¹ https://www.fincen.gov/sites/default/files/shared/277157%20EA%20nd%20Q%20MJ%20Stats_Public.pdf
and <https://www.forbes.com/sites/kevinmurphy/2018/09/06/legal-marijuana-the-9-billion-industry-that-most-banks-wont-touch/#308713943c68>
 - ¹² <https://www.nytimes.com/2018/01/04/magazine/where-pot-entrepreneurs-go-when-the-banks-just-say-no.html>
 - ¹³ <https://www.pewtrusts.org/en/research-and-analysis/blogs/stateline/2016/03/22/why-marijuana-businesses-still-cant-get-bank-accounts>
 - ¹⁴ <http://fortune.com/2015/04/15/marijuana-industry-tax-problem/>
 - ¹⁵ <http://reason.com/assets/db/14615903738888.pdf>
 - ¹⁶ <https://thecannabisindustry.org/member-blog-how-much-does-it-actually-cost-to-open-a-dispensary/>
 - ¹⁷ <https://www.forbes.com/sites/kriskrane/2018/06/13/marijuana-banking-constraints-disproportionately-harm-small-businesses/#1bd8435254ed>
 - ¹⁸ <https://www.ncbi.nlm.nih.gov/books/NBK425757/>
 - ¹⁹ <https://www.fda.gov/newsevents/newsroom/pressannouncements/ucm611046.htm>
 - ²⁰ https://www.nap.edu/resource/24625/Cannabis_committee_conclusions.pdf
 - ²¹ <https://jamanetwork.com/journals/jamainternalmedicine/article-abstract/2676999>
and <https://www.ncbi.nlm.nih.gov/pubmed/27001005>
 - ²² <https://medicalmarijuana.procon.org/view.resource.php?resourceID=005889>
 - ²³ <http://www.drugpolicy.org/legalization-status-report> and
<https://www.civilized.life/articles/california-marijuana-legalization-arrest-drops/>
 - ²⁴ <https://www.politifact.com/california/statements/2017/aug/09/kamala-harris/does-it-cost-75k-year-lock-inmate-california/>
 - ²⁵ http://www.drugpolicy.org/sites/default/files/dpa_marijuana_legalization_report_feb14_2018_0.pdf
 - ²⁶ <http://cde.state.co.us/communications/2018marijuanarevenue>
 - ²⁷ <https://www.latimes.com/nation/la-na-cannabis-city-colorado-20160404-story.html> and
<https://www.pewtrusts.org/en/research-and-analysis/blogs/stateline/2018/12/04/the-little-town-that-pot-built>
 - ²⁸ <https://www.pewtrusts.org/en/research-and-analysis/blogs/stateline/2018/12/04/the-little-town-that-pot-built>
 - ²⁹ https://www.americanbanker.com/opinion/the-one-banking-bill-congress-might-actually-pass-next-term?brief=00000158-07c7-d3f4-a9f9-37df9bc10000&wpisrc=nl_finance202&wppmm=1
 - ³⁰ <https://www.congress.gov/bill/115th-congress/senate-bill/3032/all-info>
 - ³¹ <https://www.nbcnewyork.com/news/local/NY-Lawmakers-to-Hold-Hearing-on-Legalizing-Marijuana-501732611.html> and
<https://chicago.suntimes.com/cannabis/legal-weed-is-one-step-closer-in-new-jersey-heres-whats-next/>
 - ³² <https://www.civilized.life/articles/new-governors-feel-about-marijuana/>