



Robert W. Wood

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Toking And Taxes Don't Mix, Says IRS

It's not every day members of Congress get to write the IRS asking for help with a little drug problem. Marijuana—for medical use—to be exact. Not getting some, mind you, but taxing it more fairly.

The IRS has [released a passel of letters](#) it sent to members of Congress replying to the [their letters](#) about taxing medical marijuana. The pot-tax-worried members included Representatives Sam Farr (D-CA), Linda Sanchez (D-CA), Jared Polis (D-CO), Raul Grijalva (D-AZ), Pete Stark (D-CA) and Barney Frank (D-MA). The members of Congress have a point—if their states **allow** pot dispensaries for medicinal use, how is it remotely fair for dispensaries to be taxed in an arguably confiscatory way?

As I noted [here](#), the IRS and Tax Court deny tax deductions for dealing in controlled substances even though the expenses—like rent—are legitimate and would qualify for regular “business expense” tax deductions. The culprit is Internal Revenue Code [Section 280E](#). It precludes deductions for **any** business trafficking in controlled substances. Even though some state laws allow marijuana for medical



use—like California—federal law still classifies it as a controlled substance.

Whether or not the feds choose to enforce the criminal law, the IRS says the tax law is clear that [Section 280E](#) kicks in. The IRS didn't make the Internal Revenue Code, Congress did! If the tax code says there's no deduction, that's that.

Besides, even the U.S. Supreme Court has said there is no exception in the Controlled Substances Act for medically necessary marijuana. See [U.S. v. Oakland Cannabis Buyers' Co-Op](#). Of course, denying a deduction to medical marijuana businesses effectively means they are paying tax on their gross, not their net income. Fortunately, some medical marijuana dispensaries squeak by the tax issues by having two lines of business and segregating their activities.

In fact, one U.S. Tax Court ruling says marijuana dispensaries can legally deduct expenses associated with **all** activities **except** dispensing marijuana. See [Californians Helping to Alleviate Medical Problems Inc. v. Commissioner](#). Although this case disallowed the expenses of selling marijuana, it ruled that the dispensary was **also** engaged in the business of care-giving. All **those** expenses were OK. It turned out only about 10% of the premises were used to dispense marijuana, and that made most of the rent deductible.

For more, see:

[Medical Marijuan Tax Woes](#)

[IRS Commissioner's letter to Congress regarding medical marijuana dispensaries business deductions](#)

[Don't Toke At Tax Time](#)

[Comment: The Implications of IRC § 280E in Denying Ordinary and Necessary Business Expense Deductions to Drug Traffickers](#)

[U.S. v. Kevin Petri](#)

*Robert W. Wood practices law with [Wood & Porter](#), in San Francisco. The author of more than 30 books, including *Taxation of Damage Awards & Settlement Payments* (4th Ed. 2009, [Tax Institute](#)), he can be reached at wood@woodporter.com. This discussion is not intended as legal advice, and cannot be relied upon for any purpose without the services of a qualified professional.*