



E-ALERT

Related Lawyers

John W. Schmehl
Stephanie Searles Vogel

Media Contact

Peter Dunn
Director of Client
Relations and
Communications
Philadelphia, PA
pdunn@dilworthlaw.com

HELD: DISALLOWANCE OF ALL BUSINESS EXPENSES OF A MARIJUANA BUSINESS IS CONSTITUTIONAL; INDUSTRY FACES ONEROUS TAX BURDEN

November 04, 2019

While marijuana businesses become more prevalent, and investors are being solicited for funding, the United States Tax Court has reaffirmed the applicability and constitutionality of IRC section 280E, which disallows all deductions and credits for a business involving a Schedule 1 controlled substance within the meaning of the Controlled Substances Act. Despite efforts in several states to legalize marijuana use and sale, it remains a Schedule 1 controlled substance under Federal law. In *Northern California Small Business Assistants Inc. v. Commissioner*, Docket No. 26889-16 (Oct. 23, 2019), the Tax Court concluded that:

- Section 280E is not a penalty or an excessive fine, so it does not violate the Eighth Amendment’s prohibition against excessive fines.
- Congress has authority to tax gross income under the Sixteenth Amendment (“power to tax and collect taxes on income”), and Congress has not carved out any exception for marijuana businesses that operate lawfully under state law.
- The disallowance applies to all business expenses (including rent), state and local taxes, and depreciation.
- The legality under state law of a marijuana business has no impact on Section 280E.
- The opinion was joined in by ten judges, with one judge concurring, but concluding that Section 280E was a penalty. One judge dissented in part, finding that Section 280E imposed an unconstitutional penalty, with the Sixteenth Amendment not permitting such a provision.

This means that marijuana sellers can reduce their taxable income only by their cost of goods sold. No other business expenses or credits will be permitted unless Section 280E is amended by Congress to provide a carve out for permissible marijuana sales under state law (or a similar exception). A marijuana business that claimed deductions under Section 280E on constitutional grounds on a tax return may need to amend such return and pay additional tax in order to reduce or eliminate penalties and interest. This decision could be appealed by the taxpayer to the Ninth Circuit.

For additional information contact [John Schmehl](mailto:jschmehl@dilworthlaw.com) at 215-575-7201, jschmehl@dilworthlaw.com and [Stephanie Vogel](mailto:svogel@dilworthlaw.com) at 215-575-7087, svogel@dilworthlaw.com.