

Tax Benefits to Arise from Department of Justice's Move to Reclassify Marijuana

On April 30, 2024, the Department of Justice submitted a formal proposal to the White House to loosen the restrictions placed on marijuana and formally recognize its medical use. Specifically, the proposal would reclassify marijuana from a Schedule I controlled substance to a Schedule III controlled substance. Since 1971, marijuana has been classified as a Schedule I controlled substance along with other drugs that have a high potential for abuse, such as heroin and LSD.

The reclassification of marijuana to a Schedule III controlled substance would provide significant tax benefits for companies in the cannabis industry. Cannabis companies have generally been prohibited from deducting certain business-related expenses under Section 280E of the Internal Revenue Code of 1986, as amended, due to marijuana's Schedule I classification. Under Section 280E, taxpayers are generally prohibited from claiming any deduction or credit for amounts paid or incurred in carrying on a trade or business that consists of trafficking controlled substances (within the meaning of Schedule I and II of the Controlled Substances Act) which are prohibited by Federal law or the law of any state in which such trade or business is conducted. Because marijuana is a Schedule I controlled substance, cannabis companies have been prohibited from deducting certain business expenses such as rent, payroll, advertising, and various other expenses. As a result, except for reducing gross income for certain costs, including the cost of goods sold, cannabis companies have generally been subject to federal income tax on their gross income. If marijuana is reclassified as a Schedule III controlled substance, cannabis companies would be able to claim significant tax savings by being able to deduct these expenses, which has historically been prohibited.

While the Department of Justice has made its recommendation to reclassify marijuana, the proposal must still be reviewed by the White House's Office of Management and Budget. If accepted by the White House's Office of Management and Budget, the proposal would be formally published and subject to a period of public comment. Accordingly, while it may be months before the reclassification of marijuana would possibly occur, cannabis companies should begin considering potential tax planning strategies to maximize their deductions in the event marijuana is reclassified.



Richard J. Silpe

Chair, Tax

rsilpe@cozen.com
Phone: (215) 665-2704
Fax: (215) 665-2013



Nathan L. Rudy

Associate

nrudy@cozen.com
Phone: (215) 366-4450
Fax: (215) 665-2013

Related Practice Areas

- Business
- Tax

Industry Sectors

- Cannabis