F I S C A L   I M P A C T   R E P O R T

SPONSOR Ortiz y Pino **ORIGINAL DATE** 1/31/19 **LAST UPDATED** 2/04/19 **HB**

SHORT TITLE Medical Cannabis Gross Receipts & Deductions **SB** 242

ANALYST Iglesias

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY19	**FY20**	**FY21**	**FY22**	**FY23**		
$0.0	($6,400.0)	($7,700.0)	($9,200.0)	($11,000.0)	Recurring	General Fund
$0.0	($4,400.0)	($5,300.0)	($6,400.0)	($7,700.0)	Recurring	Local Governments

Parenthesis ( ) indicate revenue decreases

Relates to SB71

SOURCES OF INFORMATION
LFC Files

Responses Received From
Taxation and Revenue Department (TRD)
Department of Finance and Administration (DFA)
Human Services Department (HSD)
Corrections Department (NMCD)
Department of Health (DOH)

SUMMARY

Synopsis of Bill

Senate Bill 242 adds medical cannabis to the gross receipts tax (GRT) deduction under Section 7-9-73.2 NMSA 1978. This bill excludes medical cannabis from the definition of a prescription drugs and specifies that only receipts from the sale of medical cannabis by a licensed producer and qualified patient pursuant to the Lynn and Erin Compassionate Use Act would qualify. The effective date of this bill is July 1, 2019.

FISCAL IMPLICATIONS

This bill narrows the gross receipts tax (GRT) base. See *Significant Issues* for more information.

Combined patient sales from the 35 licensed producers in New Mexico's Medical Cannabis Program totaled $105.8 million in 2018, representing a 23 percent increase over 2017 sales.[1] Patient enrollment grew by 45 percent over the same time period, with the New Mexico Department of Health reported about 67.5 thousand current patients as of December 2018.

Using the 2018 sales data, the fiscal impact estimate assumes 20 percent growth in sales (on par with industry estimates) each year to derive an estimated impact of about $6.4 million to the state general fund and about $4.4 million to local governments in FY20.

Additionally, the Human Services Department (HSD) would have an impact on the County Supported Medicaid Fund (CSMF) and the Safety Net Care Pool (SNCP) Fund. These funds are calculated off the matched taxable gross receipts collected in a county, and any gross receipts tax deduction will thereby reduce the amount of revenues that are distributed to these two funds. HSD estimates the impact to be negative $125 thousand and negative $165 thousand to the SNCP and CSMF, respectively, in FY20.

Estimating the cost of tax expenditures is difficult. Confidentiality requirements surrounding certain taxpayer information create uncertainty, and analysts must frequently interpret third-party data sources. The statutory criteria for a tax expenditure may be ambiguous, further complicating the initial cost estimate of the expenditure's fiscal impact. Once a tax expenditure has been approved, information constraints continue to create challenges in tracking the real costs (and benefits) of tax expenditures. Due to the increasing cost of tax expenditures, revenues may be insufficient to cover growing recurring appropriations.

SIGNIFICANT ISSUES

This bill narrows the gross receipts tax (GRT) base. Many of the efforts over the last few years to reform New Mexico's taxes focused on broadening the GRT base and lowering the rates. Narrowing the base leads to continually rising GRT rates, increasing volatility in the state's largest general fund revenue source. Higher rates compound tax pyramiding issues and force consumers and businesses to pay higher taxes on all other purchases without an exemption, deduction, or credit.

According to Taxation and Revenue Department (TRD) analysis of this bill, "the deduction for receipts from medical marijuana sales would put it in-line with other approved medications, from a taxation perspective. It would also reduce the financial burden on patients, however, deductions reduce the tax base which may result in higher taxes in other areas."

According to the New Mexico Department of Health (DOH), most states with both recreational adult use and medical cannabis programs have implemented an excise tax on sales of cannabis for both recreational and medical use.

The following chart demonstrates how some other states tax medical cannabis.

Alaska	$50 per ounce for medical cannabis.
Arizona	6.6% medical cannabis sales tax.

[1] https://ultrahealth.com/2019/01/25/new-mexico-medical-cannabis-program-finishes-2018-with-106-million-in-sales/

California	15% medical cannabis excise tax.
Colorado	2.9% generic sales tax.
Hawaii	4.5% generic excise tax on Oahu. 4% generic excise tax everywhere else.
Illinois	1% sales tax under the state's pharmaceutical rate. 7% privilege tax paid by sellers and growers.
Louisiana	5% generic sales tax.
Maine	5.5% medical cannabis sales tax.
Maryland	Exempt.
Massachusetts	Exempt.
Nevada	15% wholesale tax (medical and recreational).
New Jersey	7% generic sales tax.
New York	7% medical marijuana excise tax.
Oregon	Exempt.
Pennsylvania	5% medical cannabis excise tax.
Rhode Island	4% medical cannabis surcharge paid by the seller. 7% generic sales tax.
Vermont	Exempt.
Washington, D.C.	5.75% generic sales tax.

DOH provides the following discussion:

> "It has been argued that medical cannabis should not be subject to taxation under federal tax laws because it is considered a pharmaceutical. On page 2, line 11 of [this bill], the drafters excluded medical cannabis from the definition of "prescription drugs" and added sales of medical cannabis by a licensed provider to a qualified patient as a new category of exception to the gross receipts tax. In 2018, a licensed LNPP, Sacred Garden, filed a request for refund of taxes on the basis that all cannabis sold by that producer was being used for medical purposes because it only sells to active participants in the [medical cannabis program (MCP)], all of whom have a qualifying medical condition. The hearing officer denied Sacred Garden a refund because marijuana is not a "prescription drug" and the taxpayer failed to establish entitlement to a refund (Sacred Garden Admin Hearing findings, available at https://www.foxrothschild.com/content/uploads/2018/05/Sacred-Garden.pdf).
>
> [This bill] could have the inadvertent effect of encouraging enrollment in the MCP, particularly if the recreational use of cannabis is legalized in New Mexico. It appears that, in states that have legalized both medical cannabis and recreational cannabis, tax benefits for the sale of medical cannabis may tend to drive persons to enroll in medical cannabis programs, to save on taxes. This in turn may reduce the amount of tax revenue that a state receives from a recreational cannabis program."

PERFORMANCE IMPLICATIONS

The LFC tax policy of accountability is <u>not</u> met since TRD is <u>not</u> required in the bill to report annually to an interim legislative committee regarding the data compiled from the reports from taxpayers taking the deduction and other information to determine whether the deduction is meeting its purpose.

Does the bill meet the Legislative Finance Committee tax policy principles?

1. **Adequacy**: Revenue should be adequate to fund needed government services.
2. **Efficiency**: Tax base should be as broad as possible and avoid excess reliance on one tax.
3. **Equity**: Different taxpayers should be treated fairly.
4. **Simplicity**: Collection should be simple and easily understood.
5. **Accountability**: Preferences should be easy to monitor and evaluate

Does the bill meet the Legislative Finance Committee tax expenditure policy principles?

1. **Vetted**: The proposed new or expanded tax expenditure was vetted through interim legislative committees, such as LFC and the Revenue Stabilization and Tax Policy Committee, to review fiscal, legal, and general policy parameters.
2. **Targeted**: The tax expenditure has a clearly stated purpose, long-term goals, and measurable annual targets designed to mark progress toward the goals.
3. **Transparent**: The tax expenditure requires at least annual reporting by the recipients, the Taxation and Revenue Department, and other relevant agencies.
4. **Accountable**: The required reporting allows for analysis by members of the public to determine progress toward annual targets and determination of effectiveness and efficiency. The tax expenditure is set to expire unless legislative action is taken to review the tax expenditure and extend the expiration date.
5. **Effective**: The tax expenditure fulfills the stated purpose. If the tax expenditure is designed to alter behavior – for example, economic development incentives intended to increase economic growth – there are indicators the recipients would not have performed the desired actions "but for" the existence of the tax expenditure.
6. **Efficient:** The tax expenditure is the most cost-effective way to achieve the desired results.

LFC Tax Expenditure Policy Principle	**Met?**	**Comments**
Vetted	✘	
Targeted		
Clearly stated purpose	✘	
Long-term goals	✘	
Measurable targets	✘	
Transparent	✘	
Accountable		
Public analysis	✘	
Expiration date	✘	
Effective		
Fulfills stated purpose	?	
Passes "but for" test	?	
Efficient	?	
Key: ✓ Met ✘ Not Met ? Unclear		

DI/gb