

# Intelligence MEMOS



From: Rosalie Wyonch  
To: Provincial Ministers of Finance  
Date: November 21, 2017  
Re: **THE FEDERAL GOVERNMENT GOT MARIJUANA TAXES (ALMOST) RIGHT**

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Ottawa has announced its plan to tax recreational cannabis once it becomes legal in July of next year. The proposed approach is to tax dried cannabis flowers at a rate of \$0.50 per gram or 5 percent of the sale price, whichever is higher. Additionally, provinces that agree to the proposed framework could set their own excise tax rates, and would receive a proportional share of the tax revenue. In addition, retail sales of cannabis will be subject to GST/HST (calculated inclusive of the excise tax). The federal government suggests that the combined tax revenue and Crown monopoly markups (if applicable), should be set at a minimum of \$1.00 per gram or 10 percent of the sale price.

Overall, this proposal might work. If governments were to tax marijuana heavily, it would ensure the continuation of the black market and [undermine its efforts to control the substance](#). At the federally suggested minimum rate, Canadian taxes on recreational marijuana would be lower than in any of the US states with legalized recreational cannabis, and would likely make the [budding legal market competitive](#) with the established black market. Over time, as black market activity becomes less profitable, taxes may increase. For example, Colorado [increased its retail sales tax](#) on marijuana from 10 percent to 15 percent this year, after having legal recreational sales for three years.

There are, however, some drawbacks to the proposed excise tax framework. The first is that producers are being persuaded to price marijuana at \$10 per gram or more because they will pay at least \$1 per gram in tax, no matter the price. To illustrate, if a producer charges \$5 per gram + \$1 excise tax, the tax rate is 20 percent. If the same producer charged \$10 per gram, the producer only pays a 10 percent tax. In addition, since marijuana will be subject to GST/HST inclusive of the excise tax, consumers will also face a higher effective tax rate when prices are below \$10 per gram. More importantly, \$10 a gram may mean the black market remains price competitive.

Another drawback is the federal decision to [apply excise taxes to sales of marijuana for medicinal purposes](#). This is inconsistent with Canada's policies for prescription medications, which are generally zero-rated. The reasoning is that government does not want to give people an incentive to evade taxes by accessing recreational cannabis through the medical system. This happened in Colorado, [which generated lower than expected revenues](#) because of the tax differential between medical and recreational sales. California, on the other hand, proposes to impose a 15 percent excise tax on both medical and recreational marijuana. Washington did not initially exempt medicinal retail sales from tax, but created a retail tax exemption for medicinal consumers two years after recreational consumption became legal in the state.

These points of contention are relatively minor in the overall context of legalization and the goal of minimizing the black market. Further, if all provinces tax at a similar rate then there is a lower likelihood that illegal profits could be made by simply moving marijuana from a low-tax province to a high-tax one. With the potential benefits, I urge provinces to join the proposed coordinated tax framework and impose low and similar tax rates across the country.

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