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Classification

The reclassification of cannabis will allow cannabis businesses to benefit from these tax credits and initiatives for programs or systems that many are already implementing.

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The Department of Health and Human Services recently made an official

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cannabis has a “moderate to low potential for physical and psychological dependence,” marking a milestone on the road to full legalization. So, what do cannabusiness leaders need to know about the implications of this potential reclassification?

Increased Federal Oversight

Rescheduling cannabis as a Schedule III drug will open cannabusinesses up to increased oversight by federal administrations including the Food and Drug Administration (FDA). Currently, the FDA oversees regulatory compliance for the CBD and hemp industries and maintains supervision over medical research and clinical trials. The cannabis industry will likely experience the same kind of intervention if they are reclassified. Federal organizations will also have a hand decision-making over cannabis-related research project funding.

The End of Section 280E Compliance

If you are a cannabusiness owner, you know Internal Revenue Code Section 280E very well. It's the federal tax law that states, in short, that no deductions or credits will be allowed for businesses that traffic in Schedule I or Schedule II controlled substances.

To date, cannabis' classification as a Schedule I drug has subjected cannabis businesses to this law, resulting in high effective tax rates and exorbitant tax bills that significantly impact businesses' annual profits. Many leaders must settle for paying high interest and penalties later in the year in order to ensure that they have enough positive cash flow to run their businesses. Some have even tried to argue in court that their plant-touching activities and non-plant-touching activities should

be considered separate businesses in a desperate attempt to limit the overall revenue

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With 2002 no longer applicable, cannabis reclassification would warrant eligibility for a few attractive tax deductions.

For example, cannabis businesses would be able to file for deductions for all of their business expenses as any regular business would, including utilities, payroll, marketing and more. Additionally, accounting can be done on a cash-basis reporting structure, and businesses will have access to accelerated depreciation, bonus depreciation, and full expensing under Sec. 179. Investors in cannabis pass-through entities will also be able to claim the 20% Qualified Business Income deduction under Sec. 199A.

However, it's important to note that state adoption and conformity may take longer than the federal status, so it's important to monitor and continue to plan accordingly.

Access to Federal Business Credits

The federal government offers several financial incentives for companies to adhere to business practices that aid the improvement of their communities, the environment, and the economy. The reclassification of cannabis will allow cannabis businesses to benefit from these tax credits and initiatives for programs or systems that many are already implementing.

These include hiring individuals from specified groups, including ex-felons, unemployed veterans, and recipients of federal assistance programs, as well as leveraging energy efficient and green energy tactics for their growing or processing operations. Credits will also be made available for research related to technology, agriculture, and medical advancements.

While there has been no date set to release a final decision, if the reclassification is approved, cannabis businesses stand to experience significant fiscal relief, and there

is no question that they need it. Recent reports state that only 25% of

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Kristin Kowalski is a partner in The Bonadio Group's tax practice. She has over a decade of experience providing tax compliance, consulting, and advisory services to multi-state corporations and flow-through clients in the manufacturing, technology, and real estate industries. Additional areas of interest include inbound international organizations, tax credits, accounting for income taxes, and transaction planning. Kowalski is also a member of Bonadio's cannabis and industrial hemp team.

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