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Fitch: Budget Impact of Marijuana Legalization Modest for NYC.

Fitch Ratings-New York-24 May 2018: The potential budgetary impact of legalizing marijuana for recreational use in New York State would be modest for New York City with no impact on credit quality, according to Fitch Ratings. Fitch expects the decision to legalize in New York State, which as a whole would also see modest revenue gains, will be based on political and public policy considerations rather than budgetary ones.

A recent report by New York City's Comptroller estimates the legal adult-use marijuana market at \$3.1 billion in New York State, including \$1.1 billion in New York City. The \$336 million in annual tax revenue to New York City estimated by the comptroller represents 0.3% of fiscal 2019 budgeted revenues of \$89 billion. The budget, which does not assume legalization for recreational use, includes \$100 million in excise taxes from medical marijuana, which has been legal since 2014. Fitch expects any increased receipts would take time to become fully realized. If legalization is approved by the state, many details would remain to be worked out, including which elements to tax and at what rate.

The comptroller also estimates a \$36 million savings from reduced misdemeanor arrests if legalization is approved, although the mayor has already announced an order for the New York Police Department to stop making marijuana-related arrests and the Manhattan district attorney announced that his office would no longer prosecute most marijuana-related cases.

As Fitch noted in "U.S. States Experiment with Cannabis Legalization," (August 2017) states have taken a variety of approaches to cannabis legalization (Fitch uses the broader term cannabis to refer to both marijuana, which typically connotes the dried form of the plant used for smoking, as well as oils and other formulations derived from the same plant). Eight states and the District of Columbia have legalized cannabis use for adults for nonmedical purposes, and another 22 have legalized it for medical purposes only. Taxes on nonmedical cannabis vary greatly, reflecting a range of both tax rates and the elements that are taxed. Some states tax based on price, with others based on weight, and taxes can be levied on producers, retailers and/or customers.

The New York City comptroller report's estimate of \$336 million in annual taxes, which is based on surveys of marijuana use and sales per user in states that have already legalized recreational marijuana, equates to a tax rate of 30%, which is sizable but in line with the effective tax rates estimated by Fitch in its review of states that already have legalization for recreational use. States with high effective tax rates may see legal sales shift back to black markets over time, especially if neighboring states legalize with lower effective rates. Price declines over time could also result in reduced tax revenues if the tax is tied to price.

Neighboring states New Jersey and Connecticut are also considering legalization for recreational purposes. Legislators in all three states have proposed bills, and the new governor of NJ made legalization a campaign promise.

In our earlier report, Fitch noted the need for flexibility in implementing new laws, as they may not achieve the expected goals within the anticipated timeframe. Obstacles to successful legalization include state restrictions on cultivation, distribution and sales, which may conflict with other policy goals.

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