

Forbes®

Dude, Would Legalizing And Taxing Weed Solve Our Budget Woes?

By: Howard Gleckman – December 6th, 2012

Starting today, it is legal to smoke marijuana in Washington State. That got me thinking: Could taxing stoners help balance state budgets?

The answer is yes, but it wouldn't help much. One 2010 study, done for the libertarian CATO Institute, figures legalizing and taxing weed would increase state tax revenues by about \$9 billion a year and reduce spending on enforcement by about the same amount. Overall, legalizing pot would both reduce spending and raise tax revenue by about 0.5 percent, according to the authors, Jeffrey Miron and Katherine Waldock.

The RAND Corporation, in its own 2010 report, concludes the revenue estimates from an excise tax on dope are much less certain. However, RAND's best estimate is California alone would generate about \$1.4 billion from a pot tax of \$50 an ounce.

Btw, the \$50 tax is not pulled out of a hat—or, um, a bong. It is roughly equal to the tax on cigarettes.

As with any excise tax, the amount of revenue a weed tax could generate is a function of four big things: The tax rate, supply, demand, and price. Each, of course, affects the other three.

And, with marijuana, this gets pretty interesting—at least for a tax wonk. Besides, it gives a whole new meaning to the phrase Tea Party.

How much would legalization boost demand? Well, economists can only guess. RAND reports there is good research on the response of cocaine use to changes in price, but not much when it comes to pot. Don't ask.

Stoners probably wouldn't change behavior much. They seem to be getting as high as they want, even with illegal weed. Some current users might even stop or curtail their usage once dope becomes mainstream, and thus boring. Economists call this the "forbidden fruit" effect.

Still, it is reasonable to expect legalization would increase demand overall—in part because casual users who won't buy illicit marijuana might purchase once it is legal.

On net, people would smoke more pot. But some users might also reduce their intake of booze. If so, that substitution of one drug for another might also reduce the net increase in tax revenue.

And how about supply? Well, the two-handed economists strike again. On one hand, suppliers would no longer incur the costs of prohibition (such as, say, arrest). On the other, they would face new regulatory costs—and those pesky taxes. C'mon dude. Why can't I get a straight answer?

By comparing prices in the Netherlands, where grass was de facto legal, with prices in the U.S., Miron and Waldock figure the price of dope would fall by as much as half if the drug were legalized in the U.S. The RAND authors conclude it would decline even more, so legal weed (including tax) would cost only one-quarter to one-third as much as illicit marijuana.

A brief word on spending. Both studies suggest that net costs to state and local governments would fall if pot is legalized. However lower enforcement costs might be offset a bit by higher medical and regulatory costs.

All this seems to suggest two results. First, given an excuse (and some funding), economists will research almost anything. Second, legalizing dope will trim spending and generate some new taxes.

Nationally, Miron and Waldock estimate that taxing dope would increase revenues by about \$9 billion which, in the scheme of things, isn't very much money. Legalizing dope and making it widely available certainly won't prevent us from going over the fiscal cliff. On the other hand, maybe we won't care as much.