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Marijuana Dispensary faces Tax Audit

Medical marijuana dispensing has long been a dicey issue skirting between a legitimate health practice and illegal drug pushing. Medical marijuana dispensaries portray themselves as nonprofit health centers and they offer value-added services like yoga and health-related literature. But the fact is there are truckloads of cash going into these dispensaries raising suspicion that certain quarters are surreptitiously selling drugs.

The Harborside Health Center in Oakland has come under scrutiny from the IRS. Harborside has long been regarded as a role model for the medical marijuana industry on the West Coast as it is one of the largest dispensaries there but this month has been called for audit by the IRS, according to its Chief Executive Stephen DeAngelo.

The IRS would not comment on this matter, saying the agency neither confirms nor denies audits. Last month, Oakland city official agreed to postpone large-scale plans to license marijuana farms after the Justice Department and the city's own attorney warned that the marijuana dispensing business could violate state and federal laws.

In California, the medical marijuana industry began to grow especially after a state-proposed law to legalize cannabis was not passed in November last year. For example, the three dispensaries in Oakland alone

generated between \$35 million to \$38 million in 2010 which represents a rise from \$29 million the year before. Larger cities naturally would have even more dispensaries. San Jose, for example has 98 marijuana dispensaries, outnumbering the number of 7-Eleven convenience stores in the city by 4 to 1.

California has laws that stipulate how the cultivation of marijuana ought to be done but the laws are unclear when it comes to the selling of it. Under guidelines issued by the state attorney general, dispensaries are advised not to profit from dispensing marijuana. But the guidelines are not clear and there is no case law on the issue.

Because laws are fuzzy, dispensaries increasingly operate in the gray zone between profit-making businesses and nonprofit health centers. But although a lot of money comes into the centers it does not mean that they are making a profit because of the high cost of their product. This results in razor-thin profit margins for the most part.

According to Harborside officials, the IRS has been harping on one part of the tax code, Section 280E. This section prohibits any deduction of expenses if the centers are 'trafficking in controlled substances' and is primarily aimed at drug kingpins. Harborside has been trying to get the government to exempt medical marijuana dispensaries from this law, saying they would go out of business if not allowed to deduct their expenses.

Harborside currently has about 70,000 members.