



# TaxNewsFlash

## United States

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### **U.S. Tax Court: Medical-marijuana dispensary operator deficiency challenge denied**

The U.S. Tax Court today issued an opinion in a case involving a taxpayer that operated a medical-marijuana dispensary in California.

The case is: *Patients Mutual Assistance Collective Corp. v. Commissioner*, 151 T.C. No. 11 (November 29, 2018). Read the Tax Court's 61-page [opinion](#) [PDF 231 KB]

#### **Summary**

The taxpayer operated a medical-marijuana dispensary and deducted business expenses under section 162 and adjusted for indirect cost of goods sold (COGS) under the section 263A UNICAP rules for producers.

The IRS determined that the taxpayer's sole trade or business was trafficking in a controlled substance and that section 280E prevented the taxpayer from deducting business expenses. The IRS also determined that the taxpayer had to calculate COGS using the section 471 regulations for resellers and was liable for accuracy-related penalties.

The taxpayer countered that section 280E did not apply; that it was a producer; and that a dismissed civil-forfeiture action precluded a deficiency action.

The Tax Court today held that the government's dismissal with prejudice of a civil-forfeiture action did not bar the deficiency determinations; that section 280E prevented the taxpayer from deducting ordinary and necessary business expenses; that during the years at issue, the taxpayer was engaged in only one trade or business—trafficking in a controlled substance; and that the taxpayer must adjust for COGS according to the section 471 regulations for resellers.

#### **Tax Court case in December 2018**

The U.S. Tax Court in December 2018 addressed similar issues in *Alternative Health Care Advocates v. Commissioner*, 151 T.C. No. 13 (December 20, 2018).

In this case, a corporation operated a medical marijuana dispensary in California, and the other taxpayers were individual shareholders of an S corporation that was organized to handle daily operations for the corporation including paying employee wages and salaries. The corporation deducted section 162 business expenses and later adjusted COGS to include indirect expenses pursuant to section 263A.

The IRS determined that the corporation and S corporation's sole trade or business was trafficking in a controlled substance and that section 280E precluded the deductions for business expenses. The IRS further determined that the taxpayers had underreported their flowthrough income from the S corporation, and that the corporation was not entitled to COGS in an amount greater than what had already been allowed and that the corporation was liable for accuracy-related penalties.

The Tax Court held: (1) section 280E precluded the corporation and S corporation from deducting business expenses; (2) that the taxpayers had underreported their flowthrough income from the S corporation; (3) that the corporation was not entitled to a COGS greater than what the IRS had already allowed; and (4) that the corporation was liable for the accuracy-related penalties.

Read the Tax Court [opinion](#) [PDF 137 KB]

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