How to Save the Subway Fare with Cannabis

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Executive Summary

The proposed legalization of recreational cannabis in the State of New York provides an opportunity to maintain current subway, bus and commuter rail fares—on a temporary basis—for a one year time period. This report analyzes how potential cannabis revenues can be used to maintain current fares, thus relieving the burden on families and workers who depend on public transit for access to work, school, and health care.

Projected annual state tax revenues from the legalization of cannabis exceed the revenue target of $100 million from a proposed fare increase in 2021. Issuing revenue anticipation bonds and allocating cannabis revenues in 2021 to stabilize subway and bus fares would maintain and expand ridership during the COVID 19 pandemic, providing a temporary source of funds to support bus and subway fares. This proposed policy would not address the longterm financial challenges facing the MTA but assure the continued growth in MTA ridership during the coming year.

Introduction

The Metropolitan Transportation Authority (MTA) faces serious fiscal challenges stemming from the economic shutdown brought on by the COVID-19 pandemic. The decline in ridership on subways, buses and commuter rail lines since March 2020 has generated multi-billion deficits that have been addressed, for the short term, by $3.2 billion in federal assistance from the CARES Act and $4 billion from the Coronavirus Response and Relief Supplemental Appropriations Act. An October 2020 report by the NYU Rudin Center for Transportation and Appleseed, Inc. estimated that potential service cutbacks could snowball into a loss of up to 450,000 jobs and $50 billion in earnings.[1]

In January 2021, New York Governor Andrew Cuomo announced his support of cannabis legalization in his Annual State of the State Message. This report analyses the use of tax revenues from cananbis sales to ensure bus and subway fares remain at their current levels during the economic crisis brought on by COVID-19 pandemic. Proposed legislation, such as the Secure and Fair Enforcement Banking Act and the Marijuana Opportunity Reinvestment and Expungement Act of 2019, reflect growing support for national legalization or decriminalization of cannabis.

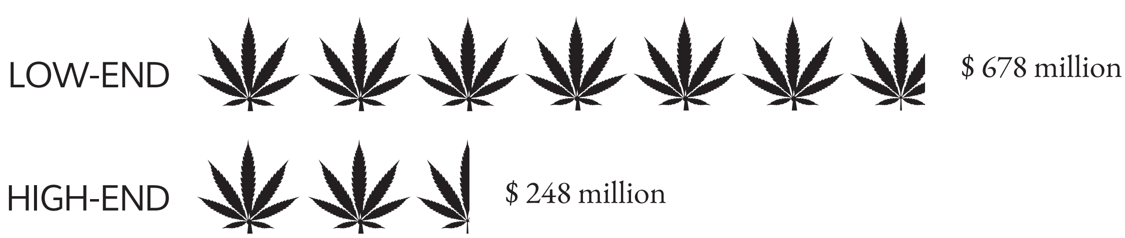
The MTA is required to balance its budget; by having access to projected revenue from cannabis legalization, the MTA would be able to limit fare increases —thereby ensuring that riders can reach their jobs and meet family responsibilities as the city recovers from the pandemic.

Evolving State and Federal Policies

In the November 2020 elections, five states legalized marijuana, including New Jersey.[2] This brings the total number of states that have legalized marijuana for recreational use to 15. In New Jersey, the state exclusively limited cannabis transactions to the regular sales tax of 6.625% and permitted municipalities to place an additional tax up to 2%.[3] This is in contrast to states like Illinois that heavily tax marijuana at up to 34.75% depending on the concentration of tetrahydrocannabinol (THC).[4]

At the federal level, the 2018 Farm Bill legalized hemp cultivation under several conditions. The bill allowed hemp products to be produced and sold across state lines, but required these products be made from cannabis plants with less than 0.3% THC.[5] Moreover, the bill legalized hemp-derived cannabidiol (CBD) and removed CBD products from the Schedule I list.[6] The schedules or categories identify a drug for addictive behaviors with Schedule I drugs having the highest potential for abuse.[7] CBD is used for its therapeutic properties and doesn't contain any psychoactive compounds.

CANNABIS REVENUE PROJECTIONS



Congress has addressed the financial complexities of the cannabis industry. In September 2019, the House of Representatives passed the Secure and Fair Enforcement (SAFE) Banking Act of 2019, which opens the door for federally-insured banks to provide services for legal medical and recreational businesses.[8] Access to financial services is a recurring issue for cannabis business entrepreneurs. In Oregon, only two credit unions provide banking services for the entire state. Meanwhile, small dispensaries in California often can't access capital to overcome the upfront licensing and regulation fees.[9]

The US Congress is also considering legalizing marijuana and removing the product from the Schedule I list. In December 2020, the House of Representatives approved the Marijuana Opportunity Reinvestment and Expungement (MORE) Act of 2019, which would legalize cannabis as a recreational substance and impose a 5% federal tax on any cannabis-derived product. The tax would be exclusively used to implement the Community Reinvestment Grant Program to provide job training, legal aid, and youth programs to individuals most impacted by the War on Drugs—those below 250% of the Federal Poverty Level or those convicted for cannabis offenses.[10]

Nationwide, marijuana tax revenues have reached $5.5 billion since 2014 in states where recreational use is legal. Tax revenue forecasting continues to be a challenge for each state government. In California, legalization had a difficult start when 2018 tax revenue failed to meet expectations.[11] However, in just the third and fourth quarters of 2019, the state obtained approximately 75% of revenues of the previous four quarters.[12] Between 2015 and 2016, Oregon saw a 240% increase in its tax revenue, but between 2018 and 2019, the state experienced only a 24% increase (Figure 1).[13] In addition to retail excise and general sales taxes, most states also levy a tax on legal cultivators of recreational marijuana. By contrast, Alaska charges its growers a fixed dollar amount, with no tax on retail sales.[14] As marijuana prices have fallen dramatically in the years since its legalization, the Alaska's flat $50-per-ounce tax is an increasingly heavy financial burden on growers, many of whom have become delinquent.[15]

Recognizing this unpredictability, no state relies so heavily on cannabis revenue as to be significantly impacted by sudden changes in the market. For example, marijuana tax revenues accounted for less than 1% of Colorado's fiscal year 2019-2020 state budget.[16] Market volatility would be especially threatening if a state were to directly allocate the revenues toward a specific target (e.g., social service benefits or education line items). To account for these risks, Colorado and California place annual revenue into a lockbox, only making it available in the following year. Doing so ensures the states don't have to rescind funds and can allocate precise figures based on actual revenues rather than projections.[17]

This volatility became especially salient when the coronavirus pandemic diminished economic activity in the spring of 2020 and affected revenue collections, albeit unevenly, across the country. Compared to the fourth quarter (April–June) of fiscal year 2019, four states saw increases in their marijuana tax revenue collections while two saw decreases (see Table A2 in Appendix).[18] Alaska, California, Colorado, and Oregon saw double digit increases ranging from 18.0% to 47.1%. In contrast, Massachusetts and Nevada saw decreases of 23.4% and 6.7%, respectively.[19, 20, 21] Fueling these different realities is the composition of the consumer base for cannabis in each state. For example, California saw more people pivoting from the illegal market to the more safe and regulated retail market while Nevada lost its tourists, a major consumer group.[22] The coronavirus has shown, that to a remarkable degree, there is relative resiliency in cannabis demand during a major crisis.

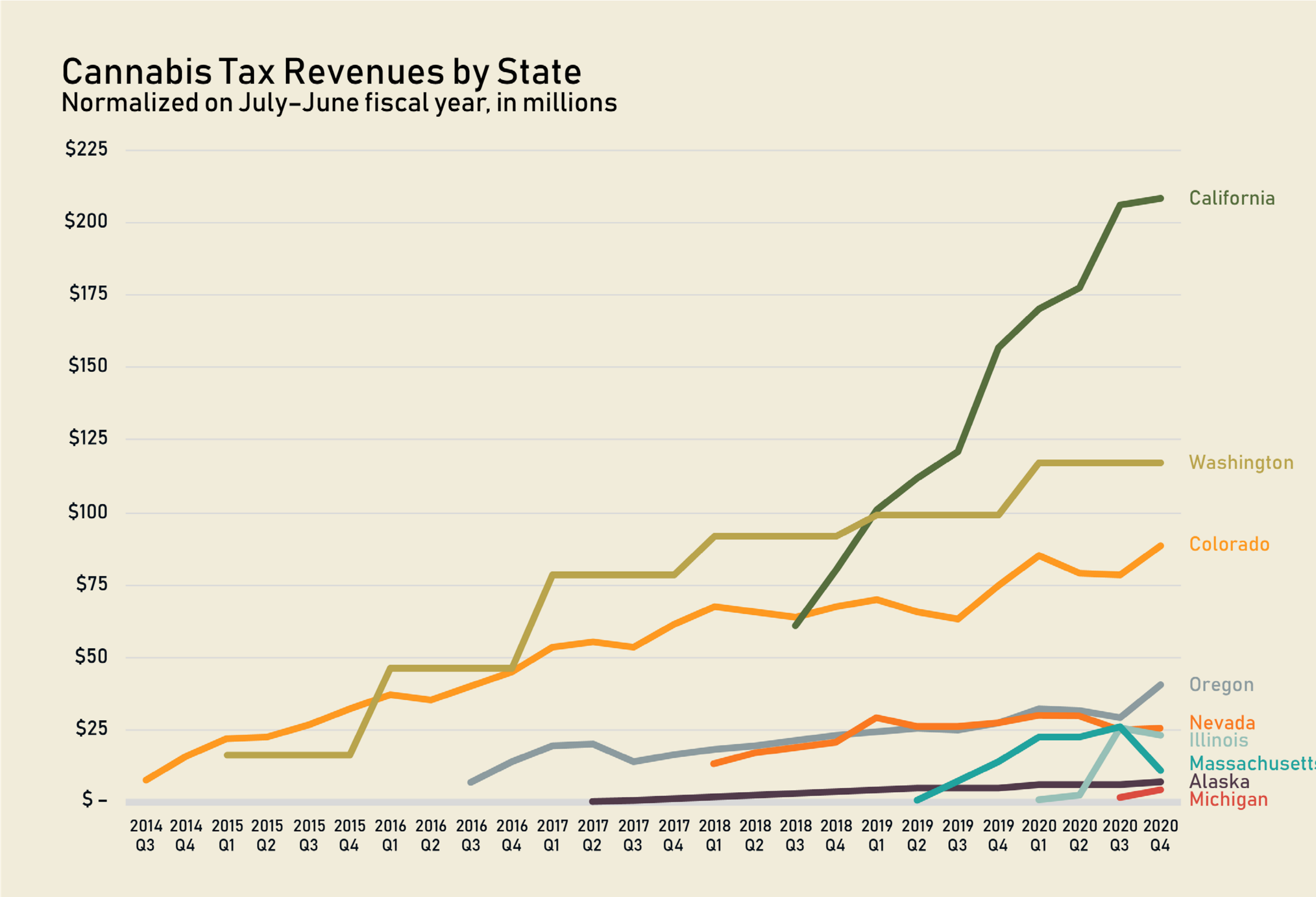


Figure 1. Cannabis Tax Revenues by State.[12, 13, 14, 19, 20, 21, 33, 34, 35]
Note. See Table A1 in Appendix A for tabular data.

Creating Equity in Cannabis

As noted in the proposed plans for spending cannabis revenue from the MORE Act, there is a strong effort to return these dollars to the communities devastated by excessive and harsh drug policies. States such as Illinois and Massachusetts both included equity initiatives in their legalization bills. Beyond expunging nearly 740,000 cannabis-related charges, Illinois requires 25% of cannabis tax revenues be allocated to its R3 Program, which gives funds to organizations that sponsor re-entry programs, job training, and violence reduction in neighborhoods.[23] Further, the state obligated existing medical dispensaries applying to enter the recreational market to contribute to a fund that will help train new business owners who otherwise have not had resources to learn how to maintain a business. This policy prevents established dispensaries from dominating the market, often favoring white business owners at the detriment of minority entrepreneurs.

In the NYU Rudin Center for Transportation's *Coronavirus in New York City* report found that 75% of the essential workers who used MTA services were people of color. When the MTA announced it would shut down subways between 1 and 5 am for sanitation, the agency implemented an Essential Connector service to provide for-hire vehicles for eligible essential workers. The NYU Rudin Center for Transportation found that more than 18,000 trips were provided in May 2020 through this service, showing the importance the MTA has for essential workers.[24]

In New York State, MTA jobs and membership in the Transport Workers Union has long has been a powerful and important path for upward economic mobility. As of December 2020, the MTA's workforce was almost 40% Black and 16% Latino.[25] On an agency basis, Black and Latino workers concentrate within the subway and bus divisions, contributing to their higher exposure to COVID during the initial months of the pandemic.[26] More than 130 MTA workers have died from COVID, more than 90 of whom were part of TWU-100.[27] Preserving the MTA's budget keeps these jobs in place and provides economic security to individuals and families of all ethnic and racial groups.

State of the MTA

The MTA's current fiscal challenges have intensified with the COVID 19 pandemic. In its November 2019 Financial Plan, the MTA reported that the agency would see surpluses in fiscal years 2020 and 2021 but transition to up to $638 million deficits in 2022 and 2023.[28] At that point, debt service payments were expected to consume more than 30% of farebox revenues. Although the agency proposed policies such as an organizational restructuring and fare increases, none of the remedies could have anticipated the impact of the coronavirus.

MTA fare revenues declined as ridership plummeted in March and April 2020, and while bridge and tunnel tolls partially recovered in the fall of 2020, ridership will require two years, at least, to recover. In its December 2020 update, the MTA stated that without federal intervention, the agency would require massive cuts in service and operations. Fortunately, the federal government provided a second round of funds of $4 billion to the MTA, averting many of the predicted service cuts but still not removing the threat of an increase in fares.[29] Because the MTA expected $4.5 billion, thus there is still a $468 million deficit for 2021.

The suspension of major capital program projects has amplified the budget impacts of the operating deficit and jeopardized necessary improvements to the 116-year-old system. These projects include Phase 2 of the Second Avenue Subway, Metro-North's Penn Station Access, ADA station upgrades, and CBTC signal modernization. To salvage the operating budget, the MTA has proposed moving more than $1.5 billion from the 2021–2024 capital budget. While solving an immediate liquidity issue, the delay in these projects and procurements creates the potential for financing issues in the future.

Critically, New York City reduced support to the MTA when it slashed the Fair Fares budget for fiscal year 2021. Fair Fares was designed to provide a 50% discount on MetroCards to city residents living under the federal poverty level. Recognizing the $7.1-billion drop in tax revenues due to the coronavirus, the City Council adopted a $9.6-billion cut in the FY21 budget over FY20. This included reducing the Fair Fare budget by 61%, or $65 million. Further emphasizing the threat to Fair Fares is the City Comptroller's recent report labelling the program a financial risk in future fiscal years.[30]

Beyond cannabis revenues, advocates and policymakers have identified other sources for funds. There has been discussion of a $3 fee on package deliveries in New York City. State Assembly member Robert Carroll estimates that the fee would generate more than $1 billion in revenue for the MTA.[31] This particular fee is a regressive attempt to solve the fiscal problems for the subway. A $3 fee on every box is more burdensome for a family in Queens earning $50,000 than for a family on the Upper West Side earning more than $200,000. Further, the fee would not likely help the department stores as advertised, since these stores continue to rely more on online sales to keep up with consumer preferences and have actively reduced their storefront presence.[32] While cannabis may not be the only way to help the MTA, it has the potential to stabilize fares without producing detrimental externalities.

Policy Recommendations

Should New York State legalize cannabis for recreational use, those tax revenues should be used to stabilize the MTA's subway and bus fares during the coming year. In 2018, the New York State Department of Health (DOH) projected recreational marijuana tax revenues to be between $248.1 million and $677.7 million.[36] Various factors, such as price per ounce, tax rate, price elasticity, and other non-price effects, explain this range. DOH also assumed a two-part tax: a retail excise tax plus state and local general sales taxes. Because the legalization of marijuana in New Jersey did not come with an excise tax, there is some potential for leakage in the New York market, should consumers cross the Hudson to purchase cannabis products at cheaper prices. Should this happen as it does with cigarette smuggling (55.8%), then the projections would require revision.[37] It is important to note that cannabis revenues do not fill the MTA's budget gap but can be targeted toward specific time-limited policies. We propose targeting the cannabis revenues to limit the expected fare increases in 2021.

Following a implementation schedule similar to the State of Illinois, tax revenues could roll into coffers within six months of legalization. Assuming the New York State legislature will legalize recreational cannabis during the

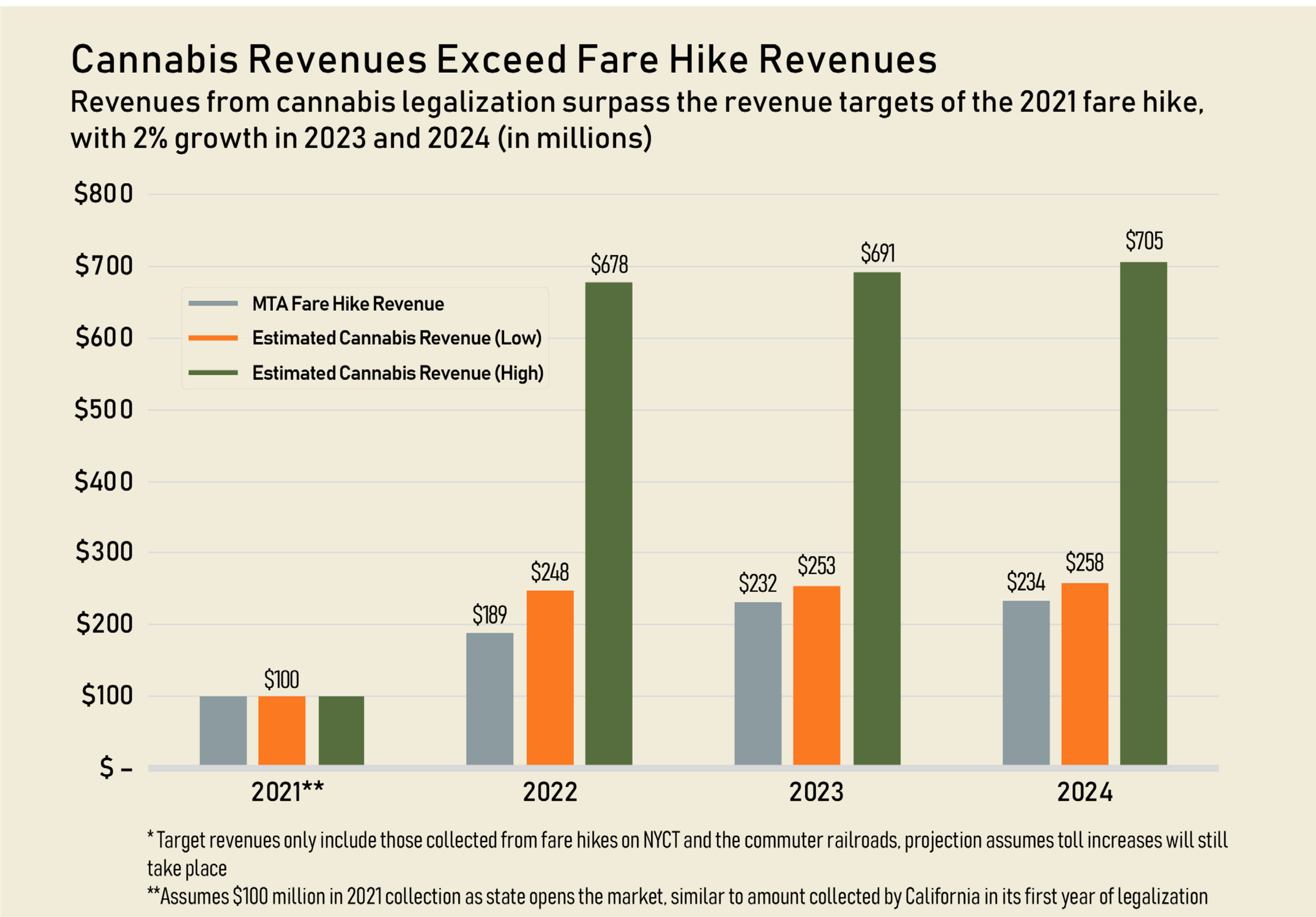


Figure 2. Cannabis Revenues Exceed to Fare Hike Revenues. [36, 38]

2021 legislative session, taxes could be generated by the fall of 2021. While Illinois had a larger medical cannabis industry on which to build their recreational retail market, New York could collect taxes during fiscal year 2022 (April 2021–March 2022), albeit less than the figures represented in the DOH report.

The revenue goals from the projected fare increases for 2021 would be congruent with funds from a cannabis tax. Assuming the toll increases remain on bridges, the MTA would need to find approximately $100 million in 2021 and $189 million in 2022 to replace the revenue targets of the proposed fare increase.[38] Cannabis would fill this need, limiting fare increases on the subway, buses, and commuter rail systems. With projected revenues ranging from $248.1 million and $677.7 million, cannabis would allow fares to remain at their current levels, adding riders while the city and regional economy recover (See Figure 2).

The use of cannabis funds to maintain the $2.75 fare does more than benefit riders. By stabilizing the current fares, the MTA's ridership would recover faster than under increased fares since more citizens would have accessible transit within their reach. With sustained ridership and a new revenue source, credit rating agencies may signal that the MTA's recovery is brighter. The MTA's commitment to maintaining service and increasing ridership is vital to the economic health of the entire New York region.

Conclusion

While cannabis revenue is not the primary path to resolving the long-term fiscal challenges facing the MTA, legalizing cannabis and targeting the revenues to limit fare increases will create a lifeline for low income households in the city and region.

Public transit is the most productive investment to allow individuals to get access to jobs, health care, and education. Should the MTA be compelled to raise fares, the impact will fall unevenly on those who have the fewest available options. Cannabis revenues can avoid painful fare increases while assuring the superior mobility options of mass transit that the MTA provides.

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Appendix A

Table A1. State Cannabis Tax Revenue Collection through FY20

Normalized on a July–June fiscal year

	2014	2015	2016	2017	2018	2019	2020
Alaska				1,748,299	11,084,808	19,204,109	24,447,587
California[a]					141,100,000	490,400,000	761,700,000
Colorado	23,582,385	102,395,177	156,701,019	223,465,056	263,766,809	274,050,767	331,183,825
Illinois							52,024,876
Massachusetts						22,058,543	81,734,083
Michigan							5,877,000
Nevada					69,759,784	109,042,018	110,393,505
Oregon			20,652,983	70,263,897	82,203,730	102,094,948	133,150,350
Washington[b]		64,880,580	185,678,648	314,839,660	367,382,493	397,523,568	468,502,946
Fiscal Year Total	$ 23,582,385	$ 167,275,757	$ 363,032,650	$ 610,316,912	$ 935,297,624	$ 1,412,373,952	$ 1,969,014,172

[a] California revenues are reported in quarterly press releases. Each press release reports a specific figure for the quarter as well as an update to the previous quarter's revenues in the format of $X.X million, and do not sum to the $1,450,000,000 total reported in the most recent press release dated August 19, 2020.

[b] Washington reports revenues on an annual basis. The figures have been divided by four to estimate quarterly results and do not represent Washington's actual quarterly revenues.

Table A2. Fourth Quarter State Cannabis Tax Revenue Collection between 2019 and 2020

Normalized on July–June fiscal year, Q4 defined as April–June[a]

	2019 Q4	2020 Q4	Percent Change
Alaska	5,147,060	7,000,136	*36.0%*
California	156,900,000	208,400,000	*32.8%*
Colorado	74,962,675	88,474,627	*19.0%*
Massachusetts	14,180,310	10,860,013	*−23.4%*
Nevada	27,502,495	25,658,869	*−6.7%*
Oregon	27,519,717	40,489,987	*47.1%*

[a] While Washington's FY20 collections were greater than FY19, the state does not provide data on a quarterly basis and thus fails to capture the timing of the COVID-19 pandemic. Illinois and Michigan did not have tax collections in FY19 Q4. All three states are omitted in this comparison.