

Taxation of Drugs – The Dutch Experience

Tributación de las drogas – La experiencia Holandesa

Tributação das drogas – A experiência Holandesa

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Abstract

This paper gives a short overview of the Dutch soft drugs policy and the current discussion with regard to soft drugs in the Netherlands. Secondly, some figures and estimates about the use of soft drugs and the amounts involved are presented. In the third place, the legalisation discussion is addressed. Finally, the income tax and the indirect tax aspects are discussed. At the moment no value added tax or excise is levied on drugs. The possibility to levy an excise on soft drugs in the Netherlands is investigated in the final part of the paper. It is demonstrated that the potential revenue of an excise on soft drugs is substantially higher than the revenue mentioned in the programs of those political parties who are in favour of legalisation of soft drugs and introduction of an excise.

Keywords

Soft drugs, Legalisation, Regulation, Coffee shops, Taxation, Excise, Revenue, The Netherlands.

Resumen

En este trabajo se ofrece una breve visión general de la política de drogas blandas holandesa y la discusión actual en relación con las drogas blandas en los Países

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Bajos. En segundo lugar, se presentan algunas cifras y estimaciones sobre el consumo de drogas blandas y los importes correspondientes. En tercer lugar, se aborda la discusión de la legalización. Finalmente, se discuten aspectos del impuesto sobre la renta e impuestos indirectos. Por el momento no hay un impuesto al valor agregado o impuestos especiales aplicados a los medicamentos. La posibilidad de imponer un impuesto al consumo de drogas blandas en los Países Bajos se investiga en la parte final del documento. Se demuestra que los ingresos potenciales por drogas blandas son sustancialmente mayores que los ingresos mencionados en los programas de los partidos políticos que están a favor de la legalización de drogas blandas y la introducción de un impuesto al consumo.

Palabras clave

Drogas blandas, Legislación, Regulación, Cafeterías, Impuestos, Impuesto al consumo, Ingresos, Países Bajos.

Resumo

Neste trabalho oferece-se uma breve visão geral da política de drogas leves holandesas e a discussão atual em relação às drogas leves nos Países Baixos. Em segundo lugar, apresentam-se algumas cifras e estimações sobre o consumo de drogas leves e os importes correspondentes. Em terceiro lugar, se aborda a discussão da legalização. Finalmente, discutem-se aspetos do imposto sobre a renda e impostos indiretos. Para já, não há nenhum imposto ao valor acrescentado ou impostos especiais aplicados aos medicamentos. A possibilidade de impor um imposto ao consumo de drogas leves nos Países Baixos investiga-se na parte final do documento. Demonstra-se que os ingressos potenciais por drogas leves são substancialmente maiores que os ingressos mencionados nos programas dos partidos políticos que estão a favor da legalização de drogas leves e a introdução de um imposto ao consumo.

Palavras-chave

Drogas leves, Legislação, Regulação, Cafés, Impostos, Imposto ao consumo, Ingressos, Países Baixos.

Sumario

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Policy Analysis; 10. Drugs related public expenditures; 11. Soft drugs and income tax; 12. Soft drugs and Value Added Tax; 13. Soft drugs and excise duties; 14. Potential budgetary effects

1. Dutch soft drugs policy

The Dutch soft drugs policy is based on four pillars:

- 1) Prevent usage and provide treatment.
- 2) Reduce harm to users.
- 3) Minimize public nuisance.
- 4) Combat production and trafficking.

The Dutch law makes a distinction between drugs with a high risk (hard drugs) such as heroin, cocaine and also XTC, and drugs with an acceptable risk (soft drugs) such as the cannabis products, marijuana and hashish. The law also makes a distinction between production and possession of cannabis for a person's own use and production and possession for commercial purposes. With regard to commercial production and trade there is an active detection and prosecution policy. Production with a maximum of 5 plants and possession of a maximum of 5 grams has in general no consequences, but confiscation and fines remain possible.

Most soft drugs are sold in so-called *coffeeshops*. Coffeeshops are establishments where the sale of cannabis for personal consumption is tolerated by the local authorities. They have long been a unique Dutch phenomenon. The last five years, however, in Spain the number of cannabis clubs has proliferated from less than 50 in 2010 to more than 700 in 2014. These clubs are, unlike in the Netherlands, for members only. According to Spanish media the booming cannabis clubs have turned Spain, and especially Barcelona, into a 'Holland of the South'.²

In the Netherlands the sale of cannabis to individual users is tolerated by the mayor of a municipality and not prosecuted by the Public Prosecutor if the sale takes place in a coffeeshop which has a formal permit of the mayor and which adheres to the criteria for non-prosecution. These criteria are defined in the Opium Act Directive.

Coffeeshops are not allowed to:

- 1) Advertise.
- 2) Sell hard drugs.

² <http://www.theguardian.com>.

- 3) Give access to youth under 18.
- 4) Cause public nuisance.
- 5) sell more than 5 gram to a customer per day.
- 6) Have a stock of 500 grams or more.

Most municipalities apply additional local criteria for instance with regard to opening hours or location³. In general, coffeeshops are not allowed within a certain distance from the nearest secondary school.

2. Stricter rules for coffeeshops

Since 2007, no alcohol is allowed in coffeeshops and since 2008, like in other public spaces, smoking of tabac is forbidden. The consequence is that only pure weed and hashish may be smoked inside a coffeeshop.

In 2011 a drugs policy letter was sent to Parliament. The government announced in this letter a shift towards stricter legal measures against cannabis-related criminality and a stricter policy against public nuisance associated with coffeeshops. Not all announced measures were adopted in the Coalition Agreement of the current coalition government which is in office since November 2012. For instance, the planned national distance criterion of 350 meters from the nearest secondary school has not been introduced.

In 2012 two new criteria to which coffeeshops must adhere were introduced: the private club criterion and the residence criterion. On the basis of the first criterion, coffeeshops can only sell to registered members. The second criterion stipulated that only residents of the Netherlands could become a member and enter a coffeeshop. As a consequence the number of drug tourists in the border region, especially in the southern provinces, decreased substantially. Another consequence was that many residents turned away from the coffeeshops because of the required membership registration. As a result, the importance of the illegal cannabis consumer market increased. For the government this was a reason to cancel the private club criterion⁴. The residence criterion is enforced at the moment in parts of the Netherlands (e.g. the southern provinces) but not yet everywhere (e.g. Amsterdam).⁵

The government sees high potency cannabis as an unacceptable health risk. This is one of the arguments underlying the plan to place cannabis with a

3 *The Netherlands Drugs Situation in 2013. Report to the European Monitoring Centre for Drugs and Drug Addiction (EMCDDA)*. Page 121-123. Netherlands Institute of Mental Health and Addiction.

4 *The Netherlands Drugs Situation in 2013*. Pages 17, 22-23.

5 <http://www.jellinek.nl>.

THC-percentage of more than 15% on the hard drugs list of the Opium Act. THC is the active ingredient in cannabis. Several cannabis varieties have a THC-content higher than 15%. Consequently coffeeshops will no longer be allowed to offer this high potency cannabis and higher penalties will be imposed on trafficking, importing and exporting this category of cannabis⁶. This plan is, however, controversial and for this reasons has not yet been introduced. One element in the discussion is that it is forbidden for coffeeshops to have equipment available in their shop to measure the THC-content of cannabis. The minister wrote to Parliament that no prosecution will take place for measuring equipment in coffeeshops. So this would mean a second tolerance element within the existing policy of tolerance of coffeeshops. According to the coffeshops sector the proposal is impracticable.⁷

3. Coffeeshops, some figures

In 1972 the first coffeeshop in the Netherlands (*Mellow Yellow*) opened in Amsterdam. In 1999 there were 846 coffeeshops where the sale of cannabis was tolerated under strict conditions, of which 288 in Amsterdam. As a consequence of the strengthening of the rules, the number of coffeeshops shows a decreasing trend. In 2010 the number of coffeeshops had decreased to 650. At the end of 2012 there were 617 coffeeshops left. They were located in 103 of the 415 municipalities. Almost half of all coffeeshops are located in the three big cities: Amsterdam, Rotterdam, and The Hague.

Most municipalities have a zero-policy with regard to coffeeshops, they do not permit any coffeeshop within their borders. A quarter of all municipalities does limit the number of coffeeshops. Almost two-thirds of the municipalities with coffeeshops do not experience problems with the rules. In 2012, 56 violations of the rules were recorded (maximum stock criterion, youth criterion, residence criterion).

In 2010, 9% of all coffeeshops were within a distance of 350 meters from a secondary school. The province of North Holland, with Amsterdam within its borders, has about 10 coffeeshops per 100,000 inhabitants. In other provinces the numbers are much smaller, in absolute terms as well as per 100,000 inhabitants.⁸

4. Other outlets

Beside the regular coffeeshops, there are several thousands of non-tolerated outlets of cannabis. For instance, dealers with a fixed address, dealers in pubs,

6 *The Netherlands Drugs Situation in 2013*. Page 46.

7 <http://www.voc-nederland.org>

8 Statistics Netherlands (CBS). Webmagazine. 6 September 2011.

streetdealers and delivery at home. It is estimated that 70% of the cannabis is sold in coffeeshops and 30% is sold through non-tolerated outlets.⁹

A fast-growing category is the online shop. Their turnover is estimated at € 30 million in 2014. Some of these shops only sell to foreign clients. They sometimes do not only offer softdrugs but also hard drugs, and no questions are asked about age. The quality of their cannabis is high because clients can place reviews on the internet. Cannabis is packed vacuum in order to prevent discovery by detection dogs. The so called TOR network is used to stay anonymous: the server is in country x, the buyer in country y and the seller in country z. Detection is difficult, international cooperation is necessary to combat this form of drug trafficking. A number of European countries, the USA, European Commission, Europol, etc. work together in Project ITOM: illegal trade on online marketplaces.¹⁰

5. Disadvantages of the present situation

The current policy with regard to soft drugs has advantages, but also a number of disadvantages. An often mentioned advantage is that tolerating the sale of soft drugs through coffeeshops and applying strict rules to it keeps soft drugs users away from harddrugs. The fact however that the commercial production and trade of softdrugs is forbidden has a number of disadvantages.

- 1) The production and supply of soft drugs takes place through and is organised by the criminal circuit. They take advantage of the situation and as a consequence make high profits, partly also to compensate for the risk of detection and prosecution.
- 2) There is no control on the quality of the drugs. The lack of control leads to health risks.
- 3) The drugs are often produced under unsafe circumstances and in places that are not suitable. This may lead to outbreaks of fire and to high maintenance and repair costs for the owners of the premises where the drugs are produced after detection of the production site.
- 4) Enforcement of the law and prosecution of the illegal production and trade leads to an extra burden on the police organisation and the courts.
- 5) And last but not least, tolerating the sale through coffeeshops, but not tolerating the production and supply gives frictions. This situation is referred to as the front door back door problem. The sale of soft drugs at the front door is

9 <http://www.jellinek.nl>.

10 Response of the Ministry of Security and Justice to an article in newspaper Volkskrant. 26 September 2014.

tolerated, but the supply at the back door is not. As a result, no invoices for the supply can be shown by coffeeshop owners and the tax administration often cannot check the turnover and profit figures of the coffeeshop. It is a source of tax evasion by coffeeshop owners in addition to the tax evasion by the producers who only pay income tax and fines in the case of detection.

6. Legalisation and regulation discussion

In reply to questions from Parliament, the Minister of Security and Justice of the Netherlands has time and again explained that in his opinion the full legalisation of the production and sale of soft drugs is not in line with international treaties. This point of view is sometimes disputed by legal scientists. Opponents of legalisation often refer to article 168 of the Lisboa Treaty of the EU which states that the policy of the EU member states should be directed at the improvement of public health and the prevention of diseases of the population. This is, however, a very general statement. The efforts (through publicity etc) of individual EU member states to prevent health damage as a consequence of drugs use will according to this Treaty be complimented by the EU. The EU policy is laid down in the European drugs strategy 2005-2012 and in the EU drugs action plan 2009-2012.

In 1961 the UN Single Convention on Narcotic Drugs was signed. This convention aims to combat drug abuse by coordinated international action.

The position of the major political parties in the Netherlands as to the legalisation or regulation of soft drugs is as follows.¹¹

1) Liberals (D66)

- legalisation of soft drugs and aiming at changes in international treaties.
- regulation of the production of soft drugs through a system of licenses.
- no small scale production at home.
- prosecution of growers and traders who infringe the rules.

2) Social Democrats (PvdA)

- legalisation of the whole soft drugs chain of production, trade and sale.
- introduction of value added tax on cannabis.
- prosecution of illegal production at home.
- regulation of grow shops (sale of grow lamps, etc.).

¹¹ <http://www.jellinek.nl>.

- 3) Green Party (GL)
 - legalisation of production and trade.
 - introduction of a system of licenses.
 - introduction of an excise on cannabis.
- 4) Socialist Party (SP)
 - legalisation of soft drugs.
 - regulation of coffeeshops.
- 5) Christian Democrats (CDA)
 - reduction of the number of coffeeshops.
 - in the long term: close all coffeeshops.
 - stricter enforcement of the rules and more prosecution.
- 6) Party for Freedom (PVV)
 - reduction of the number of coffeeshops.
 - stricter enforcement of the rules and more prosecution.
- 7) Liberal conservatives (VVD)
 - introduction of a system of membership for coffeeshops in order to reduce public nuisance and drugs tourism.
 - no coffeeshops in urban areas and near schools.
 - stricter rules and more prosecution of production and import

The four major parties who are in favor of the regulation and legalisation of soft drugs production and consumption do not have a majority in parliament at the moment. Together they occupy 67 of the 150 seats in the House of Representatives and 32 of the 75 seats in the Senate. Nevertheless in February 2015 the Liberal Party (D66) took an initiative to change the Opium Act. They presented a bill in parliament with the aim to regulate the production of cannabis. The proposal does not mean full legalisation, but tries to solve the so called front door–back doorproblem. At the moment, the sale of soft drugs in coffeeshops with a license is tolerated (front door), but the production of soft drugs and the supply to coffeeshops is prosecuted (back door). Regulation of the production and supply will according to the explanatory memorandum to the bill of the Liberal Party lead to a reduction of criminality and improved public health through better control of the quality of cannabis.

7. Production, import, export, consumption; Some estimates

Estimates about the production, import, export and consumption of drugs vary widely. It is certain, however, that the Netherlands is a major production and distribution country for cannabis as well as for synthetic drugs. For imported cocaine and heroin the Netherlands is an important distribution country, with the harbours of Rotterdam and Antwerp (Belgium) and Schiphol Airport as hubs. Because of the hidden character of drug production and trafficking it is difficult to get a good overview of the availability and the supply of drugs. Cannabis cultivation and the production of synthetic drugs often takes place indoor and is, also because of its illegal and non tolerated character, not directly visible.

Every year several thousands of illegal sites for the production of cannabis are detected. In 2014, the Research and Documentation Centre of the Ministry of Security and Justice published a report in which the total production in the Netherlands of cannabis was estimated between 200 and 550 tons. Between 80 and 90% of the production is exported, according to this report. Some experts express doubt about this percentage and give lower export estimates. The estimate of the total consumption in Western and Central Europe is 1500-2100 tons.¹²

Reliable figures about the illegal import of cannabis are not available. Most import concerns hashish which originates from Maroc, Afghanistan, India and Nepal. According to police estimates about 25% of the turnover of coffeeshops regards imported hashish¹³. Estimates of the total turnover of coffeeshops vary. The Netherlands Institute of Mental Health and Addiction estimates that the total amount of cannabis consumed by residents in the Netherlands lies between 44 and 69 tons per year. This figure excludes consumption by (drugs) tourists.¹⁴

8. National accounts estimates¹⁵

Illegal activities have to be included in the Dutch National Accounts since September 2014, affecting the figures of 2010 onwards. This is a consequence of a decision by the EU. The payments of member states to the EU are mainly based on the level of GDP, so the inclusion of illegal activities can have important consequences for the level of payments to the EU. The main aim of the inclusion of illegal activities is to increase the comparability of the data between countries.

12 WODC. De export van in Nederland geteelde cannabis, cahier 2014-19.

13 *Korps Landelijke Politiediensten, Het groene goud.* (2008).

14 *The Netherlands Drugs Situation in 2013.*

15 *The contribution of illegal activities to national income in the Netherlands.* Statistics Netherlands (CBS). (2012).

As stated before, it is much more difficult to make reliable estimates for illegal activities than for legal activities, because the information is as hidden as the activity. Estimates have to be made on the basis of scarce sources, for instance police data. The share of the illegal economy in the Dutch GDP is estimated by Statistics Netherlands (CBS) at 0.4% in 2010. This is quite low, but also in most other member countries of the EU the share is below 1%. The production and trade of cannabis accounts for about 40% of the illegal economy in terms of value added. Prostitution contributes 20% and harddrugs about 15%. The rest is mainly illegal gambling and illegal copying, fencing of stolen goods and smuggling of cigarettes. With a Dutch GDP of about € 650 billion in 2014 this would mean that the total income or value added derived from the production and the trade of cannabis can be estimated at about € 1.05 billion. This figure includes the visible part of the sector (coffeeshops).

Estimates by the CBS of the production and consumption of cannabis are based on various sources, among others police data, the European Monitoring Center for Drugs and Drug Addiction, etc. A distinction is made between trade of cannabis on the one hand and production of cannabis on the other hand. Traders in the CBS definition are coffeeshops and illegal/invisible traders who import marijuana or hashish and resell it. Producers are mainly illegal cannabis growers in the Netherlands who produce the so-called nederweed or Dutch marijuana. On the basis of a study by the Netherlands Institute of Mental Health and Addiction it is assumed by the CBS that about half of the amount of nederweed and imported cannabis is sold in coffeeshops and the rest by illegal sellers.

In the National Accounts cannabis bought by foreign tourists in Dutch coffeeshops is considered as export. In addition, there is direct export not going through coffeeshops. This illegal export is estimated by the CBS to exceed € 1 billion. The input by coffeeshops consists of the costs of the shop (rent, energy costs, etc) and the cost they have to make to purchase the nederweed and to import foreign weed and hashish. Assumptions had to be made by the CBS about the input costs as a percentage of the turnover.

9. Calculations by the Bureau of Economic Policy Analysis

In the Netherlands the Bureau of Economic Policy Analysis is the independent institution that makes the official economic forecasts. They also make calculations of the economic and budgetary effects of policy changes. This task is especially interesting during election time, when all political parties present their plans for the coming years. The Bureau makes calculations of the effects of all these programs. The resulting estimates in terms of economic growth, unemployment, inflation and

the effects on disposable income are of course important for the political parties. The programmes of the political parties are in general very detailed and it is quite a challenge for the Bureau to give a clear picture of the economic and budgetary effects and to do that timely.

According to the Bureau the introduction of an excise as mentioned in the political programmes of several political parties has a revenue effect of € 0.3 billion. In the publication of this estimate the Bureau is not explicit about the tax base, the tax rate and other assumptions made for the calculation¹⁶. As indicated later in this paper a revenue of € 0.3 billion corresponds to a relatively moderate excise tax rate. The potential revenue of an excise tax on soft drugs is higher.

10. Drugs related public expenditures

Public expenditures in relation with Opium Act offences are estimated at € 395 million in 2011, of which € 287 million related to hard drugs and € 107 million to soft drugs. In 2011 health insurance companies reimbursed € 250 million for the treatment of non-alcohol addictments. However, health insurance companies only finance part of the total addiction care. The total expenditure on the treatment of hard and soft drug addictments is estimated to be around € 350 million in 2011¹⁷. It is estimated by the Bureau of Economic Policy Analysis that legalisation of soft drugs leads to a decrease of public expenditures (courts, police) of € 0.2 billion.

11. Soft drugs and income tax

As a general rule, income tax is payable even on profits made on illegal activities. Therefore, although the sale of cannabis in coffeeshops is illegal (but tolerated and visible), coffeeshops pay income tax on the profit they make as well as wage tax and social security premiums for their employees. The administration of coffeeshops is often imperfect, mainly because there is no administration of the supplies. In those cases the profit is estimated on the basis of information derived from indirect sources. The profit of a coffeeshop is in many cases taxed at a marginal rate of 52%. This is the highest bracket of the personal income tax which starts at a relatively moderate taxable income of about € 57,500. In the corporate income tax there are two brackets. In the first bracket (profit up to € 200,000), the tax rate is 20%. Higher profits are taxed at a marginal rate of 25%. Distributed net corporate profits are taxed at the progressive personal income tax rate. The turnover of coffeeshops is estimated by the CBS at € 600 million. According to the CBS this is a conservative estimate.

16 Bureau of Economic Policy Analysis. *Keuzes in Kaart*. 2013-2017.
17 *The Netherlands Drugs Situation in 2013*. Pages 30-31.

Most coffeeshop owners oppose to legalisation or more regulation of the retail trade and production of cannabis because they fear a negative effect on prices and on profits. If this is correct, this could also have a negative influence on the tax revenue collected from coffeeshops. Legalisation or regulation will on the other hand make it easier for the tax authorities to check the administration of the coffeeshops, because the purchases of cannabis will be recorded on the basis of invoices in their administration. This will have a positive effect on tax revenues.

The production of cannabis takes place on a very small scale in cellars and attics of houses and on a larger scale in barns, greenhouses and in the open air, hidden between other crops such as corn. The small scale production is often for the grower's own consumption only and is not prosecuted if it concerns less than 5 cannabis plants. The production on a larger scale for the supply of coffeeshops and for export will, in general, not be taxed because these activities are not visible for the tax authorities. Only in case of detection taxes and fines will be payable.

No estimates are available of the potential revenue from producers if the production would be legalised or regulated, but on the basis of the conservative CBS estimate of the turnover of coffeeshops the tax revenue from producers could be in the order of € 0.1 billion. Although legalisation or regulation would no doubt lead to additional income tax revenue from producers, it may not be assumed that the full potential revenue can be collected because there will always remain a black market. As a result of regulation additional energy tax will be collected as well. According to a report by the energy sector the market value of electricity stolen by producers of cannabis amounts to € 200 million per year, of which € 130 million can be attributed to energy tax.

12. Soft drugs and Value Added Tax

Coffeeshops do not pay value added tax (VAT) on the sale of cannabis. This is a consequence of the fact that the VAT is a harmonized tax in the EU. According to EU-rules no value added tax is levied on illegal activities. Legalisation of the sale of cannabis in the Netherlands would not automatically make cannabis taxable for the VAT. Also, in the other member states of the EU the sale of cannabis would have to be made legal and an adjustment of international treaties and of the EU-rules governing the VAT would be necessary.

It is remarkable that until 2007 coffeeshops could fully deduct the VAT paid on the goods and services they purchased even in cases where their only business activity was the sale of cannabis. Most coffeeshops also sell non-alcoholic drinks and food, but cannabis is often 90% of their turnover. The consequence was that most coffeeshops got on balance substantial refunds of VAT because in-

put-VAT exceeded output-VAT or output-VAT was zero. Since 2007 input-VAT of coffeeshops is only deductible in as far as the input can be attributed to legal business activities, that is to say the sale of non-alcoholic beverages and food, etc.

Even when detected, producers of cannabis do not pay VAT on their output for the same reason as coffeeshops do not pay VAT. Understandably, they also will not claim VAT refunds on their inputs, such as electricity and grow lamps. But if the production of cannabis is not the only business activity of a grower it will be difficult for the tax authorities to discover incorrect deductions of input-VAT. Legalisation of the production and retail trade of soft drugs would lead to the same discussion about EU-aspects as mentioned before with regard to the legalisation of coffeeshops. An adjustment of the EU-rules governing the VAT would be necessary in order to be able to levy VAT on the production.

13. Soft drugs and excise duties

EU member states are obliged to apply excise duties to alcohol, tobacco and energy products. As there are no tax controls at the borders between the member states, general rules as well as specific rules apply for each category to facilitate cross-border trade and to prevent competitive distortions. EU-legislation on excise duties includes rules with respect to the tax structure, minimum rates, exemptions and general rules for producing, storing and moving these goods around the EU.¹⁸

Member states are free to levy indirect taxes on other consumption categories than tabac, alcohol and energy products, as long as they make sure that these taxes do not have a negative influence on the position of competitors in neighbouring countries. The Netherlands for instance levies a purchase tax on new passenger cars, but was forced by the EU about ten years ago to introduce a refund on exported second hand cars. The refund is equal to the implicit tax on the remaining value of the car at the time of exportation. In the discussion about an indirect tax on soft drugs in the Netherlands the principle of free movement of goods and the avoidance of competitive distortions within the EU will probably not play a role as long as export and import of soft drugs remains illegal.

Cross-border effects place considerable constraints on the possibilities to increase the level of indirect taxes. The border region between the Netherlands, Belgium and Germany is densely populated and, therefore, more than marginal price differences of for instance tabac, alcohol and fuel can have severe cross-border effects. Consumers are free to buy these products in another member state in a quantity that is clearly meant for their own personal use. Recent increases of the

¹⁸ <http://www.ec.europa.eu>.

excises on tabac, alcohol and fuel gave rise to much publicity and political debate about expected and perceived negative effects for these sectors.

In the case of the introduction of a tax on soft drugs in combination with regulation it may be expected that drugs tourism to the Netherlands will decrease. It may, however, be expected that this effect will be relatively small. The effect on drugs tourism of the enforcement of the residence criterion in all municipalities will be more substantial. Furthermore, regulation may have effects on the production and import of illegal soft drugs. In principle regulation, it makes it possible to ban imported soft drugs from coffeeshops. This will lead to a shift from import of hashish to home grown cannabis.

The revenue of a tax on soft drugs of course depends on the tax rate and the tax structure. Soft drugs have a small volume and a high value. In this respect, they are comparable with tabac. In fact, soft drugs are much more expensive per gram than tabac. In the Netherlands the tax rate on cigarettes is about 72.5% of the consumer price including tax. This is above the EU minimum. The tax on an average package of cigarettes of 19 cigarettes with a consumer price of € 6.00 amounts to € 4.35, of which € 3.31 is excise and € 1.04 is value added tax. This leaves € 1.65 for manufacturers, trade and tobacconists. This means that the tax rate on cigarettes is about 260% of the price before tax. The total excise revenue of tabac (including roll your own) in the Netherlands is about € 2.6 billion per year.

The average price of cannabis in a coffeeshop is about € 10.00 per gram, the exact price depending on the kind of cannabis and the quality¹⁹. The higher the THC-content the higher the price. Hashish is somewhat more expensive than marijuana. With one gram of cannabis about 5 joints can be rolled, so one joint costs about € 2.00. Assuming an average price of € 10.00 per gram, the introduction of a tax on cannabis at a rate comparable with the excise plus value added tax on cigarettes of 260% would result in a tax rate of € 26.00 per gram.

Estimates vary as to the total consumption of cannabis in coffeeshops. On the basis of a conservative estimate of the consumption of 60 ton cannabis per year, in theory a total tax revenue of € 1.55 billion per year would result if a tax rate comparable to the tax rate on cigarettes would be introduced. A tax rate at this level would however lead to a potential shift to the black market. A more moderate rate of say € 10.00 per gram would result in a revenue of about € 0.6 billion.

It may be expected that the price increase of soft drugs as a result of the introduction of an excise tax will have some behavioural effects in the form of lower consumption. The demand for soft drugs is, however, inelastic. On the other hand

19 <http://www.jellinek.nl>.

it may be expected that prices before tax will decrease considerably as a consequence of the regulation of the production. To the extent that on balance after tax prices would increase, illegal production becomes more profitable in as far as profit margins for illegal producers will rise. For regular soft drugs users an on balance price increase is an incentive to avoid the tax by growing cannabis on a small scale at home. So if these effects are taken into consideration the revenue of the tax might be lower than the revenue on the basis of the current turnover in coffeeshops. Some sources mention a negative effect of 20%.²⁰

Collection and enforcement of an indirect tax on soft drugs will lead to administrative costs for the tax administration. This will diminish the decrease in public expenditure (police, courts) as a consequence of legalisation or regulation of the retail trade and the production of soft drugs. Collection and enforcement costs of the tax will depend on questions such as: is cannabis for medicinal purposes taxable, taxed at a lower rate or not taxed at all; will the tax rate be defined on the basis of weight or value; does the THC-content influence the tax rate or not; will there be an exemption for small scale production at home; and probably most important: will the tax be levied from the producer or from the coffeeshop owner.

14. Potential budgetary effects

The conclusion can be that the potential total budgetary effects of the introduction of an indirect tax on the consumption of soft drugs in combination with regulation of the production and supply of soft drugs are substantial. On the basis of a tax rate of 100%, which is moderate compared to the tax rate on cigarettes, these effects can be roughly estimated as follows:

<u>Introduction of an excise</u>	
• Tax base € 600 mln; tax rate 100%	€ 0.6 billion
• Implementation costs	-/- € 0.1 billion
<u>Introduction of regulation</u>	
• Income tax on production	€ 0.1 billion
• Higher energy tax revenue	€ 0.1 billion
• Better tax compliance of coffeeshops	€ 0.1 billion
• Lower drugs related public expenditures	-/- € 0.2 billion
Total budgetary effect	€ 1.0 billion

²⁰ <http://www.sargasso.nl/duopolie-wietoogst>.

In addition, to the positive effects on the government budget the regulation of the production will lead to safer production circumstances and a better quality of the cannabis products with lower health risks. The price of cannabis before tax will decrease because of the regulation and the sale of imported cannabis in coffeeshops can be put to a stop because the front door-back door problem of coffeeshops is solved as a consequence of regulation.