

## 2. TAX

# THE LEGAL REGULATION OF DRUGS: The potential to deliver tax justice

Tax policy has the potential to play a profound role in delivering drug markets that work for social justice. The vast profits generated by the drug trade constitute a highly significant proportion of some countries' revenue. Whilst estimates are difficult due to its illicit nature and vary, in 2017 Global Financial Integrity estimated the value to be between US\$426-652 billion.<sup>1</sup> This is between two and three times the global aid budget.

As we witness the beginning of the end of prohibition, with alternatives such as the decriminalisation and legal regulation of cannabis, cocaine, psychedelics, ketamine and MDMA/ecstasy on the agenda of governments across the world, it is vital that emergent reforms have global tax justice at their heart.

In 2022 the total value of cocaine shipments from Central America (excluding El Salvador) is estimated at US\$101.8 billion. The value added of cocaine movements represented 21.87% of Belize's GDP in 2002. The average value as a percentage of GDP from 2000-2018 was 6.64 percent, more than spending on education (6.34 percent) and double health spending (3.21 percent). For some years 2000-2018 Belize's cocaine movements approached or exceed average tax revenue as a percentage of GDP.<sup>2</sup>



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These revenues are both highly significant, and highly volatile. The value of cocaine across Central America jumped from US\$53 million in 2000, to nearly US\$24 billion in 2016 before reducing to nearly US\$ 14 billion in 2018.<sup>3</sup>

The people benefiting from these revenues are not the citizens of these countries that produce drugs, but organised criminals. Whilst a small portion of drug revenue may benefit rural communities, the volatility distorts the economy, creates boom and bust, and fills the pockets of organised criminals rather than boosting public services. Bringing these revenues out of the illicit sphere to being under state control where they can be taxed (which could include taxes on production, products, corporations and income from the employment generated) could provide stable and vital revenue for public good.

If Belize's 2002 cocaine revenue was taxed at the rate of tax to GDP for the country in that year (14.5 percent), the cocaine trade could have brought in US\$ 44.2 million, almost equivalent to the amount the country spent (44.3 million) on health that year. If the country had a stronger tax system, represented by a higher tax to GDP ratio (for example 34 percent, the current average OECD tax to GDP ratio) taxation from the cocaine industry could have brought in US\$ 103.5 million, more than double the health budget.<sup>4</sup>

Tax policy is a vital tool in the design of regulation that can enable the participation of small farmers and traders, support people to transition out of illegality into licit markets and provide vital revenue to improve health and reduce poverty.

## Tax for transitional justice

Recognising the racist history of prohibition, various US states have implemented social equity clauses that support disproportionately impacted communities into legal cannabis markets and direct the tax revenue to invest in health and other social programmes. Thanks to powerful advocacy New York State's cannabis regulation provides expungements for those previously criminalised. It invests 40 percent of the tax revenue from cannabis into communities that were most harmed by prohibition, 40 percent into education, and 20 percent into substance abuse and mental health services. Other US states similarly use tax revenue for health and social programmes: Illinois 20 percent, Oregon 25 percent, Colorado 60 percent and New Jersey 70 percent.

## A legal drug trade – the risks for tax justice

As we see from other trades, the potential for tax to enable or impede social justice and global power equality is huge.

Advocates for social and economic justice must seize this opportunity before big business does. The graphic below explores what could happen if advocates for economic justice fail to engage with drug reforms.

### How much tax could we gain from the drug trade?

At a conservative estimate, global drug sales could provide governments with an additional US\$150 billion in tax revenue each year.<sup>5</sup> This is enough to end world hunger four times over.<sup>6</sup>

This estimate is for a sales tax only and does not include revenue from taxes on corporations, production or income as a result of increased legal employment. As well as revenue generated by taxes, legally regulating drugs can prevent public money being wasted on failed enforcement with potential savings in the police, military, prison and judicial systems, as well as those associated with wider health harms.

### A legal drug trade: The risks we must avoid





Activist at New York cannabis protest

Tax is a key issue of both national and global equity. A common problem for poor countries is the so-called ‘race to the bottom’ in which in attempts to generate revenue from foreign investment, countries compete to offer tax breaks to foreign corporations, resulting in the benefits leaving the country, most often ending up in wealthier ones.<sup>7</sup> In countries with weak capacity for tax planning and collection companies can offer “help” in the form of “tax advice” or “consulting”, enabling them to influence tax policy in their own interests. Tax policies that prioritise the needs of domestic producers and domestic revenue generation are therefore vital.

Drug reform and tax policy further overlap in the case of illicit financial flows. In 2017 Global Financial Integrity listed drugs as having the second highest value out of 10 illicit industries.<sup>8</sup> The illicit drug trade also fuels a number of the other industries listed such as illegal mining, logging and fishing, and illegal trade in wildlife, weapons and human trafficking, as drug gangs use their existing trafficking infrastructure to diversify into other criminal activities.<sup>9</sup> Organised crime fuels corruption, undermines states and creates the conditions in which illicit activities can occur. Meanwhile the low taxes and high levels of secrecy in the global tax

architecture allows organised criminals to funnel their wealth accrued from drugs and other crimes into tax havens around the world. The UNODC estimates that in 2019 Mexico received inward illicit financial flows of US\$11 billion from cocaine, methamphetamine, and heroin while Colombia received between US\$1.5 and US\$10 billion.

Whilst removing prohibition will have an impact on illicit flows, those same tax havens also facilitate the flight of capital earned legally. The Tax Justice Network estimates that countries are on course to lose US\$4.8 trillion in tax to tax havens over the next 10 years.<sup>10</sup> It is therefore vital that drug and tax justice advocates join together to close the global tax loopholes to ensure that the profits from a licit drugs trade are able to benefit citizens of the countries that produced them.

## Tax justice in a legal drug trade - key principles

If constructed using principles of transitional justice, drug reforms could generate new, stable forms of revenue for countries to strengthen tax collection capacity, reduce poverty and improve public health. This will only be possible with the deliberate development of new markets that **rectify the injustices of prohibition and global tax abuse.**

- **Put people first.** Governments must explicitly refuse big industry’s offers of tax ‘expertise’ and instead draw on the experiences of those who have achieved tax justice as part of their reforms (see above) as well as current farmers, small scale traders and those currently persecuted under prohibition.
- **Balance priorities for public health.** Models of regulation will differ based on context. More stringent regulation might improve public health and increase tax revenue, but may fail to completely eradicate the illicit market. Conversely, keeping prices low might achieve the latter but minimise the tax gains. Key is finding a model that can work to maximise the benefits of regulation whilst minimising the harms caused by any additional illicit consumption that may occur. The public health priorities of the given context must be central to any reforms.
- **Fair rates.** Address the barriers to market for small producers (in particular recognising the current absence of loans for substances that are currently illicit.) Set tax rates for small farmers that enable their participation and allow for transition to a licit market. Scale tax revenues based on the place of different actors in the value chain. Where foreign companies are involved ensure they pay fair rates of tax.

- **Generate revenue for tax capacity, health and public services.** Ensure that both the cost savings and potential tax revenue from prohibition are used to strengthen society and improve public health.
- **Use tax to support trade and environmental justice.** Support producers in traditional countries of production by ensuring that countries of the Minority World reduce tariffs on imports from them and use tax rates to encourage environmentally sustainable production.
- **Join up advocacy for drug policy reform and tax justice.** Work together to end illicit financial flows and shut down the global network of tax havens to prevent the theft of citizen's resources.

## What comes next? Let's shape it.

**Are emerging drug reforms on your agenda? Advocacy for a tax justice approach to drug reforms must happen now.**

Contact [c.james@healthpovertyaction.org](mailto:c.james@healthpovertyaction.org) to contribute to the ongoing conversation to ensure drug reforms deliver economic justice.

Published March 2025.

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Cover image: Advocates for the legalisation of marijuana taking part in the annual NYC Cannabis Parade, May 2018. © Richard Levine/Alamy Live News

Design and layout: [causeeffectdesign.co.uk](http://causeeffectdesign.co.uk)

## Endnotes

1. [Transnational\\_Crime-final-\\_exec-summary.pdf \(gfintegrity.org\)](#) Total global spend on aid in 2023 was US\$223.7 bn US\$Development finance data – OECD
2. All cocaine estimates in this section are from 'Acknowledging Cocaine Capital in Central American Development' – Journal of Illicit Economies and Development (lse.ac.uk) Population and government expenditure data from World Bank <https://data.worldbank.org/>
3. Ibid.
4. Ibid.
5. Our figures in detail: Estimates of the global drug trade vary but we have taken a conservative figure of half a trillion US\$ (based on the 2017 GFI figure of US\$426 US\$652 billion). There is no global figure available for global tax to GDP ratio. We estimate it at 30 percent for the following reasons. The OECD average is 33.5 percent. OECD countries account for 41 percent of world GDP. Some non-OECD countries have higher ratios than the OECD average, but most have lower. A majority of countries (96 out of the 181 for which figures are available) have a ratio of at least 20 percent. So, we estimate the global average at between 20 and 33.5 percent. Then we add in the factor that taxes from drugs will almost certainly be at a higher rate than the average tax from the rest of

GDP. Globally the average tax on cigarettes is 66.9 percent in high income countries and 56.5 percent in lower income countries. Considering all the above, we base calculations of tax from drugs at a conservative figure of 30 percent. This results in the estimate of total tax from drugs per year being US\$150 billion (30 percent of 500 billion). However, total government revenue gains could be much more. The tax figure is a conservative estimate and only covers sales taxes, excluding taxes on production, corporations, or income (from increased licit employment). It would cost less to regulate the drugs market than it currently does to wage the war on drugs (which currently costs over US\$100 billion a year). There would also be wider savings from the collateral damage of current drug policy (reduced costs of healthcare, reduced harm to the environment, reduced armed conflict, more stable and less corrupt governance.)

6. [How much money would it take to end world hunger?, Oxfam \(oxfamamerica.org\)](#)
7. [Health-and-Tax-briefing-WEB-2.pdf \(healthpovertyaction.org\)](#)
8. [Transnational Crime \(gfintegrity.org\)](#)
9. [REPORT-Revealing-the-Missing-Link-to-Climate-Justice-Drug-Policy.pdf \(healthpovertyaction.org\)](#)
10. [The State of Tax Justice 2023 – Tax Justice Network](#)



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