



COUNTY OF HUMBOLDT

For the meeting of: 10/3/2023

File #: 23-1341

To: Board of Supervisors

From: County Administrative Office

Agenda Section: Departmental

Vote Requirement: Majority

SUBJECT:

Options to Consider Related to Cannabis Cultivation Excise Tax

RECOMMENDATION(S):

That the Board of Supervisors:

1. Consider reassessment of Measure S Cannabis Excise Tax rates for Tax Year 2025 (cultivation year 2024);
2. Confirm collection of taxes shall resume in November 2023 as previously directed;
3. Direct staff to return with an enforcement plan to address outstanding Excise Tax balances;
4. Provide direction as necessary.

SOURCE OF FUNDING:

General Fund

DISCUSSION:

Over the past 2 years, the Board of Supervisors has taken several significant regulatory actions related to the local cannabis industry, and this item offers an update on those impacts and considerations for future actions.

Background

In February, 2022, the Board reduced the county's Measure S Cannabis Excise Tax by 85%.

In November, 2022 your Board:

- Temporarily suspended the tax for Tax Year 2023 (Cultivation Year 2022) and Tax Year 2024 (Cultivation Year 2023). Under this action, the next payments for normal cultivation taxes would be due in Tax Year 2025 (Cultivation Year 2024), with the first installment due by May of that year and second in October; and
- Deferred all outstanding payments until October 2023, with a waiver of penalty on installments due October 2022 and with enforcement occurring following payments due in October 2023 for

any outstanding taxes owed.

In addition, on Jan. 24, 2023, your Board authorized cultivators to make partial payments for their cultivation taxes.

The tax was reduced, and payments and penalties later temporarily suspended because the cannabis industry was experiencing unsustainably low market pricing, an inability to sell existing cannabis inventory and concerns were expressed from cultivators that they would not survive current conditions without relief. The previously mentioned action, also allowed cultivators time to pay their past due taxes.

In total, cultivators have experienced both the above-described local relief but also state action as the state eliminated its own cultivation tax with Senator McGuire's bill, SB 1047. With the 2024 cultivation year approaching, your Board should discuss the Measure S Cannabis Excise Tax rate for Tax Year 2025 (Cultivation Year 2024), and any other tax modifications your Board might want to considered.

Status of Collections and Permits

The county currently has approximately 1,290 total cannabis permits in post-approval monitoring, with 1,110 of those being cultivation permits that would be subject to any future applicable Measure S taxes. The remaining 180 permits are for distribution, manufacturing, delivery and other functions outside of cultivation. The county is monitoring approximately 130 interim permits, the majority of which will likely continue in 2024. There is an item later today (File No. 23-1242, "Discussion and Staff Direction for a Possible Moratorium on Accepting New Cannabis Cultivation Permits and Discussion and Direction on Extension of Cannabis Interim Permits") to discuss the status of these permits, and more specific information on permit counts will be available at that time.

Since November 2022, the Treasurer-Tax Collector has collected \$514,662, and six accounts have made partial payment totaling \$27,216 since February. There are 962 accounts with outstanding balances totaling \$14.19 million. To date, neither the Treasurer-Tax Collector nor Planning & Building Department have taken an adverse (other than assessing penalties) or revocation actions on approved permits for failure to pay Measure S taxes. A policy issue for the Board of Supervisors is to decide if payment of taxes should be a consideration in allowing somebody to continue under an Interim Permit if their Measure S taxes are not paid, and whether the applicant can be approved for an actual permit if they are not in compliance with the County Code provisions requiring payment of taxes.

A bigger issue is whether somebody who is not paying their Measure S taxes should continue to hold a permit. The cannabis ordinances require compliance with County ordinances. Not paying taxes would be a violation of this provision. One of the difficult decisions is what is this policy decision tied to, is it a matter of amount owed, percentage owed, or being two or more years behind in tax payments? Enforcement of this would result in revocation of the permit which can only be done by the Board of Supervisors.

Potential Actions for Current Permits and Accounts

If your Board were to re-implement Measure S for Tax Year 2024 at the reduced 15% rate, the next tax bills would be due in May 2024 and October, 2024. The rates would be \$0.19 per square foot of outdoor cultivation, \$0.47 for mixed light and \$1.91 for indoor, after applying the annual Consumer Price Index (CPI) increase. Tax rates for 2025 are unknown as increases are tied to CPI, however, based on historical trends the rates are likely to increase by at least 4%. Assuming a 4% CPI increase, below is a matrix of rates that would be applied to tax bills at different discounts.

Discount		Rate By Grow Type		
Reduction Amount	Applied Amount	Outdoor	Mixed Light	Indoor
85%	15%	\$ 0.19	\$ 0.39	\$ 0.58
75%	25%	\$ 0.32	\$ 0.64	\$ 0.96
67%	33%	\$ 0.42	\$ 0.85	\$ 1.27
50%	50%	\$ 0.64	\$ 1.28	\$ 1.93
33%	67%	\$ 0.86	\$ 1.72	\$ 2.58
25%	75%	\$ 0.96	\$ 1.93	\$ 2.89
15%	85%	\$ 1.09	\$ 2.18	\$ 3.27
0%	100%	\$ 1.28	\$ 2.57	\$ 3.85

For Tax Year 2022 (cultivation year 2021), the Treasurer-Tax Collector sent out 1,270 bills totaling \$3.259 million, and has collected \$1.884 million to date. These taxes were billed at the 85% reduction amount.

Revisiting the Tax Year 2024 rates may pose challenges as tax bills are based on cultivation that took place in 2023, which is nearly over, and cultivators operated in the current year assuming no taxes would be due next year. In addition, the county allows cultivators to file Temporary Cultivation Reduction (TCR) forms, which declares a cultivators' intention to reduce their cannabis cultivation, thereby reducing the amount of local taxes owed. Likely due to the suspension of Measure S taxes this year, many cultivators did not file TCR's in 2023, though staff anticipates a large number of cultivators to file TCR's going forward.

It should be noted that there are still pending legislative actions, including the local Humboldt Cannabis Reform Initiative (Measure A), set for the March, 2024 ballot, that may have an immediate adverse economic impact on cultivators.

Measure S Ballot Measure

Your Board previously directed staff to research the possibility of placing a measure on the ballot in 2024 to reform Measure S. By way of background, the Humboldt County Superior Court required the county to calculate the amount of taxed owed according to the area actually used for cultivation, rather than the square footage recorded on cultivators' permits. This ruling has led to the county issuing refunds and encountering increased administrative challenges. Aside from these changes, the structure of the Measure S tax poses challenges for cultivators as there is no mechanism to adjust for the actual

amount of cannabis produced and sold, crop damage and other aspects related to competing in the cannabis market.

When Measure S was originally considered by the Board, local cultivators expressed interest in adopting a production-based model of taxation. This method was discussed and ultimately discarded due to the county’s inability to track the amount of cannabis produced and sold. The state had not yet adopted its track and trace system, and even after adopting its METRC system the state did not share information with local governments. However, beginning Jan. 1, 2024, the state will begin allowing counties to have access to METRC data, including the ability to see cannabis movement through the supply chain. While it remains unclear the level of detail that will be available to local governments with this new development, it appears there may be the opportunity to access data that would provide enough information upon which to base a production tax.

Staff are proposing to keep Measure S in its current structure for the time being. Staff will use the 2024 cultivation season to work with the METRC system and local cultivators to determine the usefulness of the data metrics. In addition, Measure A, if passed, will have significant impacts on the cannabis community that would need to be further analyzed. If needed, staff will return to your Board at a future date with a recommended path forward, such as a measure appearing on the 2026 ballot.

FINANCIAL IMPACT:

Expenditures	FY23-24	FY24-25 Projected	FY25-26 Projected
Budgeted Expenses (refunds)	\$500,000	TBD	TBD
Additional Appropriation Requested			
Total Expenditures			
Funding Sources	FY23-24 Adopted	FY24-25 Projected*	FY25-26 Projected*
General Fund Contribution	\$500,000		
Measure S Revenue	\$0	TBD	TBD
Total Funding Sources			

**Projected amounts are estimates and are subject to change.*

Narrative Explanation of Financial Impact:

The financial impact is difficult to estimate due to limited available information about cultivation activity over the last 2 fiscal years while the cannabis excise tax was suspended. Since the tax was suspended, the market has fluctuated, state regulations have changed, and cultivators were not submitting their typical TCR’s, which reduces their tax liability. Staff is preparing for far less activity than prior years, and potentially more delinquent or non-payment by cultivators. The county most recently billed for Tax Year 2022, collecting \$3.7 million to date. Future revenue would be dependent on your Board’s direction.

STAFFING IMPACT:

Narrative Explanation of Staffing Impact:

Measure S has provided funding for staff and services in the Sheriff's Office, Aviation, Planning & Building, County Administrative Office - Economic Development, and others. Restoration of this funding source could provide needed funds for staffing, grant matches and professional services.

Directing staff to report back to your Board regarding development of a potential 2026 ballot measure, after monitoring progress with the METRC system would allow staff time to become familiar with the system and provide a more well-researched recommendation in the future.

STRATEGIC FRAMEWORK:

This action supports the following areas of your Board's Strategic Framework.

Core Roles: Support business, workforce development and creation of private-sector jobs

New Initiatives: N/A

Strategic Plan: 3.2 - Stabilize and support a successful cannabis economy

OTHER AGENCY INVOLVEMENT:

Local cultivators

ALTERNATIVES TO STAFF RECOMMENDATIONS:

Your Board could choose

ATTACHMENTS:

1. List of outstanding balances

PREVIOUS ACTION/REFERRAL:

Meeting of: Nov. 29, 2022; Jan. 24, 2023

File No.: 22-1509; 23-35