



Monterey County

Board of Supervisors
Chambers
168 W. Alisal St., 1st Floor
Salinas, CA 93901

Board Report

File Number: 22-623

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Status: Agenda Ready

In Control: Board of Supervisors

File Type: General Agenda Item

- a. Receive a status update on the commercial cannabis industry's ability to pay delinquent and current taxes due on or before July 31, 2022;
- b. Consider commercial cannabis business tax options and direct staff on which options to further develop then return to the Board of Supervisors; and
- c. Provide further direction as appropriate.

RECOMMENDATIONS:

It is recommended that the Board of Supervisors:

- a. Receive a status update on the commercial cannabis industry's ability to pay delinquent and current taxes due on or before July 31, 2022;
- b. Consider commercial cannabis business tax options and direct staff on which options to further develop then return to the Board of Supervisors; and
- c. Provide further direction as appropriate.

SUMMARY/DISCUSSION

Within the last week the Program has received multiple messages regarding operators' ability to timely pay their commercial business tax on July 31, 2022. These comments were echoed at the Cannabis Program Monthly Industry meeting held on June 13, 2022. Many cannabis industry operators do not believe they can make the commercial business tax payment due on or before July 31, 2022.

The Program requested and gained approval of the Board Cannabis and Budget Committees to bypass and present directly to the full Board. Staff's intention is to inform the Board of a current situation that could impact the collection of the commercial business tax, the vitality of our commercial cannabis businesses, impacts to the progress and completion of infrastructure improvements that will have a direct relation to our local economic businesses, and workforce reductions to name a few.

Staff has had several meetings with CAO Executive management, the Office of the County Counsel, and the Budget Office. On June 13, 2022, the Program scheduled a meeting with the Assistant County Administrative Officer, Budget Director, Office of the County Counsel, Treasurer-Tax Collector Office, and the Program to discuss this matter.

What does this mean?

Commercial cannabis business operators found delinquent after August 1, 2022, will be out of compliance with the following.

- Monterey County Code section 7.02.150(A)(4):
“The applicant is delinquent in payment of County taxes, fines or fees associated with said business”
- Monterey County Code section 7.02.160(A)(5):
“Failure to pay business property taxes or business license taxes or fines or penalties associated with said business when due and payable”
- Monterey County Code section 7.100.080:
“Unless otherwise specifically provided under other provisions of this Chapter, the taxes required to be paid pursuant to this Chapter shall be deemed delinquent if not received by the Treasurer-Tax Collector on or before the due date as specified in Sections 7.100.060 and 7.100.070.”
- Monterey County Code section 7.90.070(F)(3):
“Any application for modification or renewal shall be denied if: The permittee is delinquent in payment of any state, County, or other local taxes.”
- Monterey County Code section 7.90.100(A)(21):
“A permittee shall not be delinquent in the payment of all applicable state taxes and fees, County taxes and fees, and other local agencies’ taxes and fees.
- Monterey County Code section 7.90.130(G):
“Failure to pay all applicable taxes and fees required by the state, County, or other local agencies.
- “Good Standing Criteria states:
“The subject property and business must be current on all applicable taxes.”

What are the financial impacts?

If the majority of operators are found delinquent there will be impacts to Fiscal Year (FY) 21-22 and 22-23 depending on the delinquency amount. To further complicate this matter the proposed cannabis allocations for FY 22-23 are estimated at \$6.154m for cannabis program allocations and \$977,163 for non-cannabis allocations respectively. After the FY 21-22 budget closes there could be less than \$3m in the cannabis assignment balance.

What is the guideline to make a commercial cannabis business tax payment?

The commercial cannabis business tax is an annual tax, due and payable in quarterly installments. Operators can make partial payments of the annual tax at any time during the fiscal year, provided the quarterly installment is paid by the respective due date (October 31, January 31, April 30, or July 31). For example, operators have the option to pay monthly or weekly, provided the quarterly installment is received by the due date. Penalties and interest accrue on delinquent amounts due until paid in full.

What are the concerns for the Provisional Cannabis Business Permit (PCBP) stand-alone ordinance?

The failure to timely pay on July 31, 2022, has a related and equally serious consequence. Under existing law, it would mean that each such operator would be disqualified from the Board’s recently approved Provisional Cannabis Business Permit Program (PCBP Program), which will supplant the good standing regime.

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Although good standing will be going away, entry into the PCBP program is tied to existing good standing criteria, a choice necessary to clearly define the class of PCBP program participants. The relevant good standing criterion here requires operators to be “current on all applicable taxes.” This criterion applies not only to County commercial cannabis taxes, but also to the Monterey County Regional Fire District (MCRFD) commercial cannabis tax. MCRFD currently has 45 active commercial business operators in their district; 8 additional businesses have shut down and were considered delinquent. MCRFD reports a 58% delinquency rate of which 3 operators are on payment plans.

Once good standing is replaced by the PCBP, delinquent operators would be operating without County authority and be potentially subject to immediate shutdown. Staff could, at the Board’s direction, amend existing good standing criteria to avoid this result, but allowing businesses to operate while delinquent would likely disincentivize them to pay outstanding taxes owed and could be seen as inequitable to other operators that have and will pay their taxes timely.

The tax delinquency problem is not unique to Monterey County. Other counties face similar issues. In preparing this Board Report, staff reached out to these counties to gather possible ideas as to how to proceed.

What are other counties doing to assist local operators?

- Sonoma County TTC promulgated rules and have created a payment plan process.
- Santa Cruz County has not denied or suspended commercial cannabis licenses for unpaid taxes yet, but has:
 - Given *three-month* conditional annual licenses to those with unpaid taxes, requiring the licensee to become current on taxes before receiving an annual license.
 - Deny requested license transfers related to a sale of a business until all taxes are paid in full.
 - Set up payment plans when folks fall behind or, if because of an audit, it is discovered they owe more than they paid.
- Santa Barbara County sent the DCC a “Subsequent Letter of Non-Compliance” for licensees who did not report or pay taxes due.
 - Their TTC Office are in the process of setting up a financial monitoring and audit contract with HdL for all operators.

Some commercial cannabis operators have closed or are in the process of closing operations. The Program reported to the Board Cannabis Committee at the May 6, 2022, meeting, there have been 24 businesses who closed since CY 2019. Commercial cannabis businesses fail due for many reasons including 1) they no longer have the financial means to remain profitable; 2) their business plans are over extended due to rapid growth/expansion; and/or 3) they are delinquent on local and/or state taxes. Given this is a new business industry facing significant challenges from the wholesale price drop and other effects of the pandemic, it can fairly be assumed that many additional businesses are likely to close.

Staff has prepared the following options for the Board to review and direct staff on which options to

further pursue.

- Option #1: Refer this item to the Board Cannabis Committee, which is scheduled to meet on July 7, 2022 Based on the Committee direction, present to the Budget Committee scheduled for July 27, 2022.
- Option #2: Leave the process as is, see how many operators ultimately do not pay timely and then decide how to proceed as to delinquent operators based on that information.
- Option #3: Leave the process as is and move forward with the business closure process if an operator is found to be tax delinquent on August 2, 2022. The Board could establish a threshold, such as operators who are more than two or three quarters delinquent.
- Option #4: Leave the process as is but establish a moratorium period for operators that cannot pay to begin the process of scaling down operations by allowing the permittee to finish harvests, submit all required documents including a cessation of business and formally cease operations, and, if possible, get one last chance to come current by a specific date.
- Option #5: Adopt a proposed Ordinance to retroactively reduce the tax rate for the second, third and fourth quarters of Fiscal Year 2021-2022 to an amount determined by the Board of Supervisors. As an example, the Board could retroactively reduce the rate to the newly adopted cultivation tax rates set to take effect on July 1, 2022 for FY 22-23. Staff could be directed to determine a rate which would avoid refunds of commercial cannabis business tax paid by operators that timely paid the 2nd and 3rd quarter of Fiscal Year 2021-2022. In such a case, those operators would receive a credit towards the 4th quarter. This option is distinct in that it provides an equitable accommodation to those operators that did timely report and pay the 2nd and 3rd quarters. It would not directly prevent delinquency, but it would likely reduce the number of operators that would fail to pay timely at the end of the 4th quarter.

After the Board has given direction on which option(s) to further develop unless it is intended to remain with the status quo, the Program, Office of the County Counsel, Treasurer-Tax Collector's Office, and the Industry will require close collaboration.

OTHER AGENCY INVOLVEMENT:

The CAO Executive Management, Office of the County Counsel, CAO Budget Office, and Treasurer Tax Collector's Office met on June 13, 2022, to discuss the issue, share input and address any concerns stemming from the proposed options. The Monterey County Regional Fire District was interviewed by the Program Manager.

FINANCING:

Any commercial cannabis business tax delinquency not received by August 31, 2022 will have a direct impact on the FY 2021-22 budget. For example, if \$5 million are delinquent by that date, the general fund will have a funding gap of \$5 million. Actual impacts will vary due to the degree of uncertainty with the industry and its ability to operate for the current and future fiscal years.

BOARD OF SUPERVISORS STRATEGIC INITIATIVES:

The Monterey County Cannabis Program addresses each of the Strategic Initiative Policy Areas that promote the growth of a responsible and legal Monterey County cannabis industry.

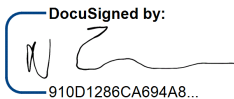
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Mark a check to the related Board of Supervisors Strategic Initiatives

- X Economic Development
- X Administration
- X Health & Human Services
- X Infrastructure
- X Public Safety

Prepared by: Joann Iwamoto, Program Manager II

Approved by: Nicholas E. Chiulos, Assistant CAO

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