To: Monterey County Board of Supervisors

Re: Item #25 on the August 23, 2022 Agenda, Cannabis Tax

The consensus of the industry is that a tax rate of $0.75/sq.ft. (With proportional reductions for indoor, nursery and outdoor) is a sustainable tax rate in the current market. This rate also provides significant relief for the Fiscal Year 21/22 quarters that will improve the survival rate come the tax due dates of October 31 2022 and January 31 2023. The current rate of $2.00 will result in many closures and sales for pennies on the dollar and canopy could be reduced by as much as half. Businesses leasing properties are not good candidates for acquisition and even some property owners are likely to fail. A FY 22/23 rate of $1.00 would generate an estimated $3,965,000 of revenue to fund a right-sized enforcement program. (See below.)

I was there when the staffing allocations were negotiated. Everybody was thinking cannabis was a nearly endless source of revenue, based on the HCD report. There is no way that process could have resulted in an appropriate allocation of resources for the future. Departments made large requests with no experience to guide them and those requests were mostly granted. This may be difficult to unwind, but it must be done swiftly to face the new reality that the revenue stream will be much lower than expected. Whether by lowering the tax rate or by the attrition of our businesses, cannabis revenue will be lower for the near future.

You also need to provide policy direction on Good Standing Criteria item #3 regarding tax delinquency. As it stands, failure to pay all taxes on the due date results in immediate closure of the business. That is a harsh response and inconsistent with currently accepted practices for dealing with delinquent taxpayers.

Type	Sq Ft Canopy	Tax Rate ($/SF)	Revenue
Mixed-Light	2,800,000	1.00	$2,800,000
Indoor	90,000	1.50	$135,000
Nursery	1,200,000	0.50	$600,000
		Cultivation Total	$3,535,000
		Gross Receipts Tax	$430,000
		TOTAL	$3,965,000

Respectfully,

Robert Roach
Executive Director, MCCIA

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<u>Alternate Option Proposal</u>

* The figures outlined in this option have been calculated based upon the methodologies used by the treasury tax collectors office to calculate fiscal impacts to reduction in cost and relief.

Option #6: Retroactive Rate Reduction to FY 21-22 Quarter 2, 3 and 4 and adoption of good faith payment deferral for FY21-22 Balances unpaid to January 31 2023 as enacted in July:

FY 21-22 rates for Quarters 2, 3, and 4 could be retroactively reduced to $0.75 for all commercial cultivation tax rates and extended and adopted through FY 22-23, this proposition providing a middle ground to previously suggested options.

· Plan Details: Payments due for FY 21-22 to be collected at the newly approved date by the BOS of January 31st 2023 and tax credits to be extended to operators who paid previously.

FY 21-22 commercial cannabis tax collected to date: $6,862,435.
· Total tax credits due: $252,145.05.

· Total remaining delinquent commercial cannabis cultivation taxes due for FY 21-22 Q1: $444,496 to be extended to the January 31st 2023 date.

· Estimated FY 21-22 total commercial cannabis to be collected: $7,963,426.

· Equity Impact: This option would be applied to all cultivation operators, so there would be no equity impact.

<u>Benefit to Operator:</u>

· Significantly reduces FY 21-22 tax burden by approximately $7,667,782.

· Avoids the duplicative tax burden in FY 22-23 of making a FY 21-22 payment plan payment monthly in addition to current FY 22-23 quarterly cultivation tax payment.

· Tax credits due on future obligations in the amount of $252,145.05 to operators that paid timely.

· Allows Operators to reduce FY 21-22 tax burden and start FY 22-23 in good standing and gives operators maximal chance of survival whilst allowing for program cost recovery.

Benefit to County:

· Avoids added administrative costs required by implementing payment plans.

· Higher probability of receiving the remaining FY 21-22 tax amounts due.

Consequence to Operator:

· Requires 9 operators who were delinquent in Q1 of FY 21-22 to become current on or before January 31, 2023 to remain operational.

Consequences to County:

· Fund balance is reduced by $11,125,504 relative to the original FY 21-22 cultivation cannabis tax revenue projection of $19,088,930.

· This loss may need to be subsidized by other discretionary revenue sources, but there are no impacts to operations because FY 21-22 has already closed.

This Option fits between options 3 and 4 as outlined by the board. To summarize it encompasses five core areas of benefit to county and industry to best ensure a thriving local economy. Cost recovery and allowing operators to continue in good faith and standing being the primary outcomes to minimize local market contraction.

- Cost recovery for the program and enabling cannabis pays its way and can support the necessary regulation of industry moving forward.
- Instead of extending refunds, this option eliminates the need for refunds and instead extends tax credits on future obligations to ensure fair and equitable treatment of all operators and avoids the county having to return funds.
- Enables the Program to continue the support of operators that have worked diligently to operate in good faith and build a reputable legal cannabis industry in Monterey.
- Enables operators to reduce the currently proposed liability from FY 21-22 to a more manageable level by January 31 2023 instead of kicking the can down the road and likely having to further push back collections.
- Moving ahead into FY 22-23 the rate of $0.75/ft across the board would enable maximal operator attrition with a manageable rate and avoid further delinquencies in a depressed marketplace to enable program cost recovery.

In an effort to project cost recovery for FY 22-23, working off the original lofty FY 21-22 projections of $19,088,930 and re-allocating to $0.75/ft of canopy tax and estimating a 20% exit rate of canopy in FY 22-23 for operators that have closed up operations the projected collections for the year would be estimated at an approximate;

$2,290,671 - Calculated as follows; *** (See reference below)

$19,088,930 / $5 = 3,817,786 Sqft / Canopy (FY21-22 Initial Estimate from 2020)
3,817,786 Sqft / Canopy - 20% canopy reduction estimate = 3,054,228 Sqft Canopy for FY 22-23
3,054,228 Sqft Canopy * $0.75 = $2,290,671 Total tax reclamation from cultivation for FY 22-23.

This would likely require a right sizing of the program for cost recovery and as operators likely exit the industry further a quarterly true up provision should be added so that operators in the county would rectify the added tax burden with increases in canopy per square foot pricing, along with right sizing of the program to accommodate for the potential of a shrinking pool of operators.

Another common sense provision would be to add in a tax escalator if or when prices moderate or stabilize above marginal cost of production. So both operators pay their fair share and the county can increase tax collections as the industry matures and navigates out of delinquency and depression.

These measures may be seen as severe in context to the unachievable expectations of FY 21-22 projections at $5/ft. The goal we should all share as a community is to see a thriving Monterey County cannabis economy that sees a net increase in both businesses and jobs added to the workforce and operator pool.

This option would also give operators a level playing field of competition with other highly productive cultivation counties who have dropped their rates to comparative figures.

As mentioned previously, in the early cannabis industry pre commoditization, cannabis was able to add tens of millions of tax revenue to the general fund for worthy causes. The focus now as the industry navigates consolidation should be focused on cost recovery and regulatory efficiency.

This investment and leadership now will maximize the potential for a thriving industry in Monterey whilst still enabling cost recovery for the needed regulation of the Cannabis Program in Monterey County.

*** To be as accurate as possible the exact canopy data as of August 1st 2022 should be calculated along with the program cost allocation to extrapolate forecasted cost recovery metrics. Option 6 proposed figures should be calculated by the following to ensure feasibility;

(Forecast program cost) - (Manufacturing / Distribution / Retail Tax) ÷ (Active canopy square feet)

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