Hello CAC cultivation subcommittee members,

Ahead of tomorrow's meeting, we wanted to reshare our comments from the last CAC meeting, with an emphasis on direct-to-consumer sales. In short, our recommendations are:

- Support for DTC sales for small producers at events in California.
- Support for DTC sales for small producers in interstate commerce, and at the federal level, through policies such as the SHIP Act.
- Amend DCC regulations to remove barriers to rural microbusiness licensure, including state security requirements, requirements for a separate wall, and insurance liability requirements.

While the agenda itself doesn't reference direct-to-consumer sales, we're assuming that will be the general direction of the meeting given the guest speakers and the discussions at the last two meetings.

Considering the lack of a specific policy proposal on the agenda, we encourage the subcommittee to be conservative in the specifics of any recommendation, since there will be limited opportunity for input from stakeholders and the DCC on these details at the meeting itself.

That said, we hope that the CAC can affirm the general message of the critical need for direct sales for small producers, and look forward to hearing from the guest speakers at the hearing.

Thank you for your consideration,

--
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Policy Director, Humboldt County Growers Alliance
Policy Chair, Origins Council
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January 18, 2023

Dear Cannabis Advisory Committee Members and DCC staff,

On behalf of Origins Council (OC), representing nearly 900 small and independent cannabis businesses in partnership with regional trade associations in Trinity, Mendocino, Sonoma, Humboldt, Nevada County, and Big Sur, we are writing to offer comments on the agenda for the January 19 CAC cultivation subcommittee meeting.

The policy areas on the subcommittee's agenda - including fallowing, changes to license size and type, and direct-to-consumer sales - are some of the most critical issues affecting small cannabis producers, and we deeply appreciate the subcommittee's prioritization of these issues.

Some issues under consideration in tomorrow's meeting are highly technical, and may benefit from additional and iterative discussions between stakeholders and the DCC. For this reason, we have briefly summarized our bottom-line recommendations for the subcommittee at the top of this document.

Below these summary recommendations, we consider the issues raised in the agenda in further detail, to the extent that this is useful for both the subcommittee's deliberation tomorrow and subsequent consideration by the DCC.

Thank you for your consideration, and we look forward to working with the DCC, advisory committee, and state policymakers on these important topics going forward.

Summary of OC Recommendations for Cultivation Subcommittee

Recommendation #1: Mixed-Light to Outdoor Transitions
Establish a process for cultivators to easily transition from “mixed-light 1” to “outdoor” license types under the new DCC definition of light deprivation. This process should include mechanisms to facilitate transition for cultivators who will seek to roll two separate licenses into a single “outdoor” license, including in situations where the licenses renew at separate times. Consider adapting the licensing conversion process currently in place for Type 5 operators to support these transitions.

Recommendation #2: Fallowing and Temporary Size Reductions
Establish a state-level process to temporarily reduce or suspend cultivation from year to year. Any mechanism proposed for fallowing should include the ability for farmers to 1) retain immature plants and genetic resources on-site, 2) conduct ancillary activities, such as processing, 3) store cannabis on-site and transact cannabis which has already been harvested, 4) fallow a license for the time period associated with a growing season, rather than for a one-year period associated with license renewal dates, and 5) pay a significantly reduced annual licensing fee.

Recommendation #3: Same Or Reduced Impact Changes
Consider the creation of license subtypes via checkbox to allow licensed operators to “activate” or “deactivate” certain activities or scale of activities, authorized under the license, and to receive correlative fee reductions when remaining activities result in reduced or same impact.

Recommendation #4: Direct-to-Consumer (DTC) Sales at Cannabis Events in California
Enact statutory changes that enable small producers to sell directly to consumers at licensed cannabis events within California. To support success at these events, the DCC should also 1) amend regulation §15052(a)(2) to remove the requirement for products in final packaged form to be retested following returns, and 2) consider changes to DCC regulations to facilitate small-scale events, including changes to the fee structure for events.

Recommendation #5: DTC Sales in Interstate Commerce
Prioritize pathways for small producer DTC sales within any interstate commerce compact negotiated between states under the SB 1326 framework. The state should also support small producer DTC sales as part of any interstate commerce framework adopted at the federal level.

Recommendation #6: Microbusinesses and On-Farm Vertical Integration
Remove existing barriers to microbusiness licensure in DCC regulation, including 1) exempting all areas of a microbusiness premises from video surveillance, lock, and alarm requirements in §15044, §15046, and §15047, if the premises is located on the same site as an outdoor or mixed-light 1 cultivation license, 2) removing the requirement for a wall to separate non-storefront retail areas from the non-retail areas of a microbusiness, and 3) appropriately reducing or waiving liability insurance requirements for distribution based on size and type of distribution.

Comments on Agenda Item #3: Change of License Size and Type

1. *Transition from Mixed-Light 1 to Outdoor Licenses*

In amended DCC regulations enacted on November 7, the DCC redefined “outdoor” cultivation to include the use of light deprivation. This change, which OC strongly supports, would theoretically enable many farmers who currently utilize light deprivation under a “mixed-light 1” license type to instead cultivate under the less expensive “outdoor” license type.

Implementing this change, however, requires a process for the streamlined transition from “mixed-light 1” to “outdoor” licenses. We appreciate that the DCC has expressed interest in establishing this process.

In establishing this process, the DCC should consider that many cultivators currently hold multiple licenses to cultivate using different methods: for example, both 1) a "specialty outdoor" license where they cultivate outdoors and without a structure, and 2) a "specialty mixed-light 1" license where they cultivate utilizing light deprivation in a hoop-house or other structure.

With the redefinition of "outdoor" cultivation to include light deprivation, these cultivators will likely want to convert their two licenses into a single "small outdoor" license. This process should be streamlined under whatever solution the DCC adopts.

A streamlined solution should consider that, in some cases, two separate cultivation licenses may renew at different times: for example, one "specialty mixed-light 1" may renew in February and one "specialty outdoor" license may renew in May. One mechanism to deal with these rolling deadlines may be to establish a mechanism for the cultivator to renew their mixed-light license as a "specialty outdoor" license in February, and then roll both licenses into a single "small outdoor" license in May, while also rendering the initial “specialty outdoor” license inactive. Licensing fees for the “small outdoor” license could be proportionately reduced to account for licensing fees already paid in February.

Pursuant to statutory requirements, as of January 1st, 2023, an eligible licensee may convert active and previously active cultivation licenses into a Large (Type 5, 5A, or 5B) or Medium cultivation license. The DCC has created a process for licensing conversion to accommodate this opportunity, which includes the ability to prorate licensing fees if applicable. This same process could be adapted and used by the DCC to allow qualified provisional or annual Mixed Light licensees to convert to provisional or annual Outdoor licenses.

> **OC Recommendation:** Establish a process for cultivators to easily transition from “mixed-light 1” to “outdoor” license types under the new DCC definition of light deprivation. This process should include mechanisms to facilitate transition for cultivators who will seek to roll two separate licenses into a single “outdoor” license, including in situations where the licenses renew at separate times. Consider adapting the licensing conversion process in place for Type 5 operators to support these conversions.

2. ***Temporary Suspension of License Size or Reduction of Cultivation Area ("Fallowing")***

Origins Council strongly supports the establishment of a process at the state level to enable cultivators to "fallow" (temporarily reduce or suspend) cultivation from year-to-year.

In other sectors of agriculture, farmers commonly adjust their production in response to market and environmental conditions, cutting back during periods of oversupply and expanding in periods of undersupply.

Under current state regulatory procedures, however, fallowing is currently not possible for cannabis farmers outside of case-by-case disaster relief provisions. Current procedures require cannabis farmers to either renew their state license each year and pay an annual licensing fee, or to forfeit their license and reapply from square one at a future date.

> **OC Recommendation:** Establish a state-level process to temporarily reduce or suspend cultivation from year to year. As expressed in our previous comment to the CAC, we believe it is critical that any mechanism proposed for fallowing should include the ability for farmers to 1) retain immature plants and genetic resources on-site, 2) conduct ancillary activities, such as processing, 3) store cannabis on-site and transact cannabis which has already been harvested, 4) fallow a license for the time period associated with a growing season, rather than for a one-year period associated with license renewal dates, and 5) pay a significantly reduced annual licensing fee.

3. ***Mechanism for Licensing/Project Changes with Same or Reduced Impact.***

Mechanisms for streamlining changes to license type, size, and operations - including enabling transitions to outdoor licensure, and implementing a state fallowing program - must be streamlined and dynamic enough to serve a range of unique operator circumstances.

An approach worth considering involves the creation of license subtypes via checkbox to allow licensed operators to "activate" or "deactivate" certain activities authorized under the license, and receive correlative fee reductions when remaining activities result in reduced or same impact.

For example, a reduction in the square footage otherwise allowed to be cultivated under a license, or "deactivating" the use of lights otherwise allowed under a mixed-light license, could enable an operator to retain their original state license while operating with the same or reduced impact.

This approach would ensure that there are no CEQA implications that may arise from a change in state license type, given that the options for changes would be confined to the authorized activity already under review or certified under CEQA.

<u>OC Recommendation</u>: Consider the creation of license subtypes via checkbox to allow licensed operators to “activate” or “deactivate” certain activities or scale of activities, authorized under the license, and to receive correlative fee reductions when remaining activities result in reduced or same impact.

4. <u>OC Responses to Stakeholder Questions for Agenda Item #3</u>

<u>Question: What challenges currently exist that prevent cultivators from changing their state license size or type?</u>

The sunsetting of issuance of new provisional licenses requires that operators with provisional licenses maintain their license as active and meet the rolling benchmarks related to environmental review in order to renew their provisional license. Should their provisional license lapse or be revoked, they will be unable to continue operations and will have to start over with their licensing application process, and will not be able to operate again until completing CEQA review and certification, completing local permitting and being issued an annual license from the State. Therefore, provisional licensees may not be able to simply change to a different size or type of provisional license, they would need to secure a local permit, complete CEQA review and certification, and secure an annual state license for the new (changed) activity before they could initiate this new (changed) activity.

However, on page 3 of the DCC’s Final Statement of Reasons for the amended DCC regulations enacted on November 7, the DCC state’s the following:

> *“The definition of mixed-light cultivation in proposed subsection (ss) has been changed to remove light deprivation. This change is necessary to align with the statutory parameters for mixed-light cultivation found in Section 26061 of the Business and Professions Code (BPC) which provides that mixed-light includes the use of natural and supplemental artificial lighting but does not include light deprivation. Thus, the Department determined that light deprivation should not be an activity that is limited to mixed-light cultivators but should be available to both mixed-light and outdoor cultivators."*

There are thousands of provisionally licensed operators that are over 5 years into the permitting and licensing process and have still not achieved an annual state license, so the risk operators face associated with losing their provisional license, and all associated compliance and business investments, is extraordinary.

Changes to a provisionally licensed project still undergoing permitting and environmental review can cause further delays and complications to the review and permitting process.

These protracted timelines are indicative of universally slow processing times on the State and local level, which has become a significant deterrent for operators needing or wanting to make

changes to their project, their license type or their license size, irrespective of holding a provisional or annual State license.

Lastly, the cost associated with changes to permitting and licensing is a significant issue, particularly for small businesses. Farmers need to take advantage of cost savings but if it costs too much to make the change, they will not be able to benefit from cost savings of switching. The costs are direct (local and state fees) and indirect (compliance materials, reports, diagrams, etc).

Question: What implications may exist for local permits that should be considered?

As mentioned above, the primary considerations for local permits pertain to processing and review timelines for local jurisdictions.

Depending on local requirements related to conforming state licensing type/size with local permitting type/size, complications could arise. For example, in jurisdictions where this type of conformance is required, and the local permitting definition of Outdoor does not include the recent rule change that the state has made to allow the use of light deprivation, an ordinance change might be required before applicants and permit holders may take advantage of a change from Mixed Light to Outdoor.

Question: What implications may exist for local or state CEQA review that should be considered?

Fallowing would reduce the environmental impacts of any given project. Should the DCC determine that a State fallowing program is a project under CEQA, the "common sense" CEQA exemption under subsection (b)(3) of Cal. Code Regs. tit. 14 § 15061 should apply:

> *(a) Once a lead agency has determined that an activity is a project subject to CEQA, a lead agency shall determine whether the project is exempt from CEQA.*
> *(b) A project is exempt from CEQA if:*
>> *(1) The project is exempt by statute (see, e.g. Article 18, commencing with Section 15260).*
>> *(2) The project is exempt pursuant to a categorical exemption (see Article 19, commencing with Section 15300) and the application of that categorical exemption is not barred by one of the exceptions set forth in Section 15300.2.*
>> *(3) The activity is covered by the common sense exemption that CEQA applies only to projects which have the potential for causing a significant effect on the environment. Where it can be seen with certainty that there is no possibility that the activity in question may have a significant effect on the environment, the activity is not subject to CEQA.*

This determination regarding the State fallowing program should prevent any CEQA requirements from arising on the jurisdictional level related to fallowing.

Transitioning from ML1 licensing to Outdoor licensing for existing light deprivation activities currently underway should not trigger additional CEQA review, so long as the premises, infrastructure and activities already under CEQA review (in the case of provisional licenses) or certified for that project under CEQA (in the case of annual licenses) does not change.

Should Outdoor licensees wish to take up light deprivation methodologies under their licenses, related proposed changes to the premise, infrastructure and farming practices may trigger additional environmental review under CEQA.

A check the box approach, whereby certain activities are deactivated and then reactivated under a license without changing license types for type or size changes within certain parameters, would avoid licensing interruption and could avoid the need for further or delayed CEQA review if the activities were already covered in the original license type and size and simply not fully utilized by the cultivator.

Question: What implications may exist for provisional license status that should be considered?

As mentioned above, the statutory requirements associated with provisional licensing, and the related impacts to local CEQA review and permit application processing, are the primary considerations.

Question: Would temporary reductions in cultivation license size support opportunities for those who wish to engage in local fallowing programs or otherwise reduce their canopy size?

Yes, this would be a significant benefit to cultivators if the cost and burdens of implementing the reduction were not too onerous and would not interrupt licensure at the local or state levels.

Question: Is there a reason to limit temporary reduction opportunities to certain cultivation licenses (outdoor, mixed-light tier 1, mixed-light tier 2, and/or indoor)?

We do not see a reason to limit temporary size reductions or fallowing to specific license types. However, because outdoor and mixed-light licenses are seasonal - whereas indoor and mixed-light tier 2 licenses can potentially produce year-round - different logistical procedures may be needed to accommodate fallowing for these license types.

Question: Which type(s) of activities allowed under a cultivation license does the subcommittee anticipate cultivators would need to continue?

As stated above, we believe it is critical for cultivators to be able to conduct ancillary activities under a fallowed license. These activities include 1) retaining immature plants and genetic resources on-site, 2) conducting ancillary activities, such as processing, 3) storing cannabis on-site, and 4) transacting cannabis which has already been harvested.

Question: What pros and cons should be considered for the potential filing periods during which temporary license reductions could be sought: license period (from renewal until expiration date), seasonal, or calendar year? The filing period is the timeframe during which a cultivator would request a temporary reduction, and the 12-month timeframe during which the reduction would be active.

In order to be practically viable for outdoor and mixed-light 1 cultivators, a procedure for fallowing must account for seasonal challenges in the cultivation cycle. For an outdoor or mixed-light 1 cultivation license which renews in the middle of a seasonal cultivation cycle - for example, in August - a twelve-month fallowing period would effectively prevent a cultivator from growing in both 2023 and 2024.

To address this issue, we propose that an outdoor or mixed-light 1 cultivator may submit a request to fallow for a twelve-month period at any time prior to May 15, 2023, regardless of when their license is slated to expire.

Between January 1, 2024 and May 15, 2024, the cultivator may then choose to either reactivate their original license, or continue to fallow in 2024.

If the cultivator chooses to reactivate their license for 2024, their licensing fee would be discounted proportionally based on the date their fallowing request was granted, given that they have already paid a licensing fee for parts of the 2023 growing season that they did not utilize. For example, if a cultivation license was renewed on August 1, 2022, and a cultivator's fallowing request was granted as of February 1, 2023, their licensing fee upon reactivation in 2023 would be 50% of the normal cost.

If a process for fallowing is implemented in the middle of the 2023 growing season, additional, one-time mechanisms may be necessary to enable cultivators to fallow in 2023 without affecting their ability to cultivate in 2024.

Question: Should a cultivator be allowed to rescind their temporary license-size reduction request, and if so, what parameters should be considered?

Yes, seasonal cultivars may choose to fallow at the beginning of the year, and based on changing circumstances later in the year decide they want to plant a late season crop. In order to accommodate this, operators should be able to rescind their temporary license-size reduction status prior to the proposed 12 month term concluding.

Comments on Agenda Item #4: Direct-to-Consumer Sales and Vertical Integration

OC strongly supports the subcommittee's decision to prioritize discussion on direct-to-consumer (DTC) sales. In an OC survey of 167 members in November, DTC sales were overwhelmingly identified as small producers' top policy priority.

While the agenda materials for the subcommittee consider DTC sales primarily in terms of the microbusiness, we encourage the subcommittee to expand their discussion to also encompass other mechanisms for DTC sales within and beyond California. Policies to expand access to on-farm vertical integration and microbusiness licensure are critical; however, these policies are also complex and likely to take time to implement due to considerations involving CEQA, local land use, and the interplay between state and local regulations.

Additional policy options are available that can accomplish DTC sales in a timely and straightforward manner, while state and local governments work through a longer-term process to increase access to on-farm vertical integration.

As conversations regarding interstate commerce and federal legalization advance, we also believe it is critical that the subcommittee consider the importance of DTC sales within a future interstate commerce framework.

For this reason, we strongly recommend that the committee consider multiple mechanisms for DTC sales for small producers. Specifically, we recommend the committee consider DTC sales within three contexts:

1) direct-to-consumer sales for small producers at licensed cannabis events within California;
2) direct-to-consumer sales for small producers within an eventual framework for interstate commerce; and
3) on-farm vertical integration for small producers through access to microbusiness or other mechanisms.

5. ***Direct to consumer sales for small producers at licensed cannabis events.***

In 2022, Assemblymember Jim Wood introduced AB 2691, which would have established a temporary event retailer license authorizing small cannabis cultivators and manufacturers to sell their own tested final form products directly to consumers at licensed temporary events.

AB 2691 was supported by a broad coalition of legacy farmers, BIPOC and social equity operators, craft producers, and consumer and patient rights advocates, and proposes a straightforward and timely mechanism for small producers to begin to reach consumers directly, without triggering the land use challenges associated with on-farm vertical integration. Although AB 2691 garnered significant support, it was not able to pass in 2022, and would require statutory changes to be implemented in the future.

OC Recommendation: Support statutory changes that enable small producers to sell directly to consumers at licensed cannabis events within California.

In conjunction with the adoption of legislation to enable DTC sales at cannabis events, we believe it will be necessary for the DCC to consider regulatory changes to facilitate the success of these events.

Specifically, current DCC policy on returns in §15052(a)(2) establishes major barriers to successful event sales. Returns of cannabis products to a distributor or producer are necessary for any products which are not sold at an event itself; however, §15052(a)(2) as written establishes an unnecessary requirement for these products to be retested following returns, resulting in significant additional costs for small producers. These rules are already producing major challenges for cannabis events; if direct sales were authorized for small producers at events, these challenges would only expand.

OC Recommendation: Amend regulation §15052(a)(2) to remove the requirement for products in final packaged form to be retested following returns.

DTC sales at cannabis events would provide substantial opportunities for cannabis tourism through small-scale events in rural areas. However, current DCC regulations tend to encourage large-scale and multi-day events, and establish barriers to the successful operation of small-scale events.

Applying for licensure for a single cannabis event requires, at a minimum, $5,000 in start-up licensing costs: $1,000 for an event organizer application, $3,000 for the lowest annual tier of event organization (0-5 events), and $1,000 per event held. For comparison, Type 58 or Type 77 alcohol event permits issued under the California ABC cost just $100.

OC Recommendation: Consider changes to DCC regulations to facilitate small events, including changes to the fee structure for events.

6. ***Direct to consumer sales for small producers in interstate commerce.***

In 2022, Governor Newsom signed SB 1326 (Caballero), which gives the Governor the authority to negotiate compacts for interstate commerce with other cannabis-legal states if certain preconditions are met.

Shortly after the signature of SB 1326, Rep. Jared Huffman (D-CA) introduced the SHIP Act in the U.S. House of Representatives, which proposes to guarantee small producers access to DTC interstate shipping and sales within an eventual federal framework for cannabis legalization.

As federal cannabis policies evolve, the structure of interstate commerce will be perhaps the single most critical issue affecting the long-term success of small-scale cannabis producers across the United States. California must take a lead in supporting interstate DTC sales if California's cannabis legacy is to be sustained over the coming decades.

> **OC Recommendation:** The state should prioritize pathways for small producer DTC sales within any interstate commerce compact negotiated between states under the SB 1326 framework.
>
> **OC Recommendation:** The state should support small producer DTC sales as part of any interstate commerce framework adopted at the federal level.

7. ***On-farm vertical integration and microbusiness licensure.***

As California discussed the potential for adult-use cannabis legalization in 2015 and 2016, the microbusiness license was established within Proposition 64 in an attempt to establish exclusive access to on-farm vertical interaction specifically for small, rural producers.

Since Proposition 64's implementation, however, the microbusiness license has failed to achieve its intended purposes. Overwhelmingly, microbusiness licenses have been utilized to facilitate vertical integration by medium and large-scale businesses in urban areas, while only a handful of microbusiness licenses have been granted to small farmers based in rural areas.

Some barriers to rural microbusiness licensure stem from regulatory approaches at the state level, while others exist as a consequence of local land use regulation and CEQA limitations. Some jurisdictions, such as Nevada County, have begun to move forward to amend local land use regulations to better accommodate on-farm vertical integration and microbusiness licensure.

While both state and local barriers must be addressed for small and rural producers to effectively access this license, and there may be inherent limitations to vertical integration for some farms in some regions, the DCC can begin to clear the way by addressing several specific technical regulations at the state level.

7a. Align Microbusiness Security Requirements with Existing Security Requirements for Cultivation

Recognizing the unique situation facing small rural farmers, DCC regulations currently exempt cultivation premises from certain security requirements applicable to other licensed operations, including requirements for video surveillance, alarm systems, and locks. However, state regulations have never exempted non-cultivation areas of a microbusiness premises from these security requirements, effectively locking small farmers out of access to microbusiness licensure.

In its recent regulatory promulgation, the DCC's ISOR stated that rural cultivation operators are exempt from state security requirements due to unique practical considerations on rural farms. The ISOR stated: *"The Department has determined that requiring the same level of video surveillance for cultivation locations that may be very large, outdoors, and located in rural areas where it may be difficult to access internet or electricity, would be unreasonably onerous and in some cases not possible."*

The logic in the DCC's ISOR extends equally to non-cultivation areas of a microbusiness premises located in an outdoor, rural area. Because it is "unreasonably onerous and in some cases not possible" to install compliant video surveillance and alarm systems in these areas, microbusiness licensure will not be attainable if licensees are required to install these systems as a condition of licensure.

> **OC Recommendation:** Exempt all areas of a microbusiness premises from video surveillance, lock, and alarm requirements in §15044, §15046, and §15047, if the premises is located on the same site as an outdoor or mixed-light 1 cultivation license.

7b. Remove the requirement for a wall between retail and non-retail areas of a microbusiness premises.

§15500(j) of DCC regulation currently requires a wall to separate retail and non-retail areas of a microbusiness premises. While we can understand this requirement in the context of a storefront retail premise which is open to the public, we do not see the applicability to a non-storefront retail premises. For a microbusiness located on a homestead farm in particular, this section may require the construction of an unnecessary wall, and in some cases may render microbusiness licensure impractical.

> **OC Recommendation**: Don't require a wall to separate non-storefront retail areas from the non-retail areas of a microbusiness.

7c. Remove the liability insurance requirement for a distributor self-transport licensee, and tier these insurance requirements by size for all distribution licensees.

§15308 currently requires all distributor licensees, regardless of type or size, to carry at least $2,000,000 in general liability insurance. This requirement is also applicable to microbusiness licensees engaged in distribution.

> **OC Recommendation:** We recommend that these insurance requirements are waived for self-distribution licensees, who are generally carrying nominal amounts of product, and who are definitionally limited only to carrying their own products. Insurance requirements for these licensees are not necessary and constitute a significant barrier to licensure. We also recommend that insurance requirements are tiered based on the size, and amount of product carried, by a distributor.