



Origins Council Comments on State Licensing Fees: December 18 CAC Meeting

Date: December 17, 2024

On behalf of Origins Council, we appreciate the opportunity to provide comment on the DCC's proposed re-evaluation of the state licensing fee structure ahead of the December 18 Cannabis Advisory Committee hearing on this topic.

A sustainable and equitable licensing fee structure is of critical importance for California's rural and legacy cultivation communities. According to an Origins Council membership survey from November 2024, "reducing state licensing" fees ranked as the third-highest policy priority for members among thirty-six potential areas of policy reform - even higher than more traditionally visible priorities such as opening interstate commerce or expanding banking access.

In preparation for this meeting, Origins Council has conducted a preliminary analysis of the existing licensing fee structure in relation to current market conditions. We look forward to further building on this analysis as this conversation continues. In short, our preliminary analysis finds the following:

- **Finding #1:** Wholesale prices for outdoor flower have dropped by 80% since licensing fees were initially set in 2017.
- **Finding #2:** Following this collapse in market prices, outdoor cultivators now pay an average of 4x or more in fees as a proportion of their annual gross revenue when compared with non-cultivation license types, and in some cases pay 10x or more proportionally to other license types.

- **Finding #3:** Compared with larger cultivators, smaller cultivators pay proportionally more per square foot in licensing fees. Larger outdoor cultivators pay an average of \$0.32 per square foot in licensing fees, whereas smaller outdoor cultivators pay at least \$0.48 per square foot, and often more.
- **Finding #4:** Larger cultivators also have more flexibility in setting their square footage than smaller cultivators. Larger “Type 5” cultivators can increase their square footage in 2,000 square foot increments without obtaining additional licensure, whereas smaller cultivators, depending on their situation, are limited to increasing their license size in 2,500, 5,000 or even 30,000 square foot increments unless they go through the burdensome process of applying multiple licenses. This inequity often results in smaller cultivators often over-paying for the actual area they have under cultivation.
- **Finding #5:** Among all DCC license types, processing and nursery licenses are the only categories where annual fees are not based on size, preventing smaller businesses from easily accessing these opportunities.

Based on this analysis, we make the following recommendations:

- **Recommendation #1:** Cultivation licensing fees should be dramatically reduced to correspond with dramatic changes in market conditions.
- **Recommendation #2:** The current inequities in licensing fees between smaller and larger farmers should be corrected.
- **Recommendation #3:** Smaller farmers should have the same ability as larger farmers to increase their cultivation size incrementally.
- **Recommendation #4:** Processing and nursery licenses should be tiered based on size as with all other license types.

We discuss each of these findings and recommendations below.

Finding #1: Wholesale Prices for Outdoor Flower have Dropped by 80% Since Licensing Fees Were Initially Set

In 2017, prior to the establishment of state regulations or a licensing fee structure, the state contracted with ERA Economics to produce a Standard Regulatory Impact Analysis (SRIA) of the proposed cultivation licensing program.¹ The findings of the 2017 SRIA were, in large part, used to inform the creation of the current licensing fee structure.

Notably, the SRIA’s analysis was based on market conditions for cannabis at that time, and the report estimated average whole prices for wholesale outdoor cannabis flower² at approximately \$1,300 per pound. The SRIA states:

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https://dof.ca.gov/wp-content/uploads/sites/352/Forecasting/Economics/Documents/Cultivation_SRIA_CD_FA_1-5-2018.pdf

² Due to time constraints, this comment focuses largely on outdoor cultivators, which comprise the bulk of cannabis cultivators in legacy production communities. In the future, we plan to update this analysis with additional information on mixed-light and indoor cultivators.

“Since quality and availability of outdoor cannabis fluctuates, the reported wholesale price is slightly lower than for cannabis produced by indoor and mixed light production. The market price ranges from \$1,000 to \$3,000 per pound with a consistent average of \$1,200 to \$1,400 per pound.”

The state’s licensing fee structure for cultivation has not changed since initial regulations were set in 2017. Since this time, however, wholesale prices for cannabis flower have dropped dramatically. According to both survey and anecdotal data from OC members and regional partners, average wholesale prices for outdoor flower are currently at about \$250/pound - an 80% decrease from the assumptions that informed the 2017.

Unlike other license types, cultivation licensing fees are set based on the cultivator’s size in square feet, not their annual gross revenue. Consequently, when market prices drop, cultivators’ gross revenue declines dramatically, and the proportion of their gross revenue allocated to annual fees increases by the same proportion. Below, we analyze the resulting inequity in licensing fees paid by outdoor cultivators compared with other license types.

Finding #2: Outdoor Cultivators Pay Multiples More in Fees as a Proportion of Gross Revenue Compared With Non-Cultivation License Types

OC has conducted a preliminary analysis of existing state licensing fees as a proportion of a licensee’s annual gross revenue, and found that outdoor cultivators currently pay substantially more in annual fees as a proportion of gross revenue than any other license type.

Our analysis finds that depending on the situation, the average outdoor cultivator pays three to four times more in licensing fees per dollar of annual revenue compared with other license types, and in some cases pays 10x or more proportionally.

As one example, a 10,000 square foot outdoor cultivator selling 500 pounds of cannabis at \$250/pound wholesale would be required to pay 3.11% of their annual revenue in state licensing fees. In comparison:

- A manufacturer grossing \$3,000,000 annually pays 0.83% of their annual revenue in state licensing fees. By comparison, the 10,000 square foot outdoor cultivator pays 3.7x more than the manufacturer as a proportion of their gross annual revenue.
- A distributor grossing \$2,500,000 annually pays 0.23% of their annual revenue in state licensing fees. By comparison, the 10,000 square foot outdoor cultivator pays 13.5x more than the distributor as a proportion of their gross annual revenue.
- A retailer grossing \$1,500,000 annually pays 0.73% of their annual revenue in state licensing fees. By comparison, the 10,000 square foot outdoor cultivator pays 4.3x more than the retailer as a proportion of their gross annual revenue.

The reason for this inequity is largely (though not entirely) due to the aforementioned collapse in wholesale cannabis prices since 2017. At the 2017 prices that informed the current licensing fee structure, the same 10,000 square foot outdoor cultivator would pay just 0.74% of their gross annual revenue in licensing fees; much more in line with the proportion paid by other license types.

These figures are based on an initial analysis of licensing fees and projected revenue that we hope to build on over time to account for, e.g. cultivation method, potential crop loss or inability to make sales, whether a cultivator grows their fully-allotted cultivation area, etc. That said, we expect the general direction of these findings to hold regardless of the assumptions used, and would expect that more precise assumptions would likely show a net *worse* situation for most small cultivators.

Finding #3: Small Cultivators Pay Proportionally More per Square Foot Compared With Large Cultivators

In addition to the inequity between the cultivation sector and other license types, small cultivators also pay proportionally more per square foot than larger cultivators under the current licensing fee structure.

In short, larger outdoor cultivators pay an average of \$0.32 per square foot in licensing fees, whereas smaller cultivators pay at least \$0.48 per square foot.

- A “small” 10,000 square foot outdoor cultivator pays an annual licensing fee of \$4,820, or \$0.48 per square foot.
- By comparison, a “medium” 43,560 square foot (one acre) outdoor cultivator pays an annual licensing fee of \$13,990, or \$0.32 per square foot.
- A “large” type 5 outdoor cultivator pays an additional \$640 per 2,000 square feet of cultivation area over one acre; also at a rate of \$0.32 per square foot.

Finding #4: “Large” Type 5 Cultivators Have Additional Flexibility To Increase in 2,000 Square Foot Increments. This Flexibility is Not Available to Smaller Cultivators

As discussed above, “large” Type 5 cultivators have the ability to increase their cultivation square footage in 2,000 square foot increments at any cultivation size above one acre (DCC regulation § 15014.2). Smaller cultivators, however, lack access to this option, and are limited to the following license sizes:

- 2,500 square foot (“cottage” outdoor cultivation)
- 5,000 square feet (“specialty” outdoor cultivation)
- 10,000 square feet (“small” outdoor cultivation)
- 43,560 square feet (“medium” outdoor cultivation)

Because small cultivators are often limited in the amount they can cultivate under local ordinances, and have limited flexibility in terms of the square footage of state license they can apply for, this often results in smaller outdoor cultivators paying even more than \$0.48 per square foot for their limited cultivation area.

For example: a cultivator authorized for 8,000 square feet of outdoor cultivation area under their local ordinance is likely to obtain a 10,000 square foot “small” state cultivation license. At the \$4,820 annual fee, this cultivator is paying \$0.60 per square foot - nearly twice the rate a “large” Type 5 cultivator would pay per square foot.

Smaller cultivators could theoretically apply for multiple state licenses to more closely correspond to their locally-authorized area (e.g. one “cottage” and one “specialty” license would license 7,500 square feet of cultivation). However, this can be challenging given the administrative burden of managing multiple different licenses; and differs from the opportunities available to larger, Type 5 cultivators, who can increase their square footage in 2,000 square foot increments under a single Type 5 license.

Finding #5: Nursery and Processing Licenses are the Only State License Types Not Tiered Based on Size.

Under the current licensing fee structure, all nursery licenses currently pay an annual \$4,685 licensing fee regardless of size, and all processing licenses currently pay \$9,370 regardless of size. This is distinct from cultivation licenses, which pay tiered annual licensing fees based on size, and non-cultivation licenses, which pay tiered annual licensing fees based on gross annual revenue.

The lack of fee tiering for cultivation-adjacent licenses creates an ironic situation where small cultivators - and only small cultivators - are denied access to affordable licensure in ways that do not affect any other license type.

Affordable access to nursery and processing licenses would have dramatic benefits for many small cultivators. Due to existing restrictions on genetic transfers by cultivators, access to nursery licenses are essential to access specialty and legacy genetics; and streamlined access to collective processing facilities would make a major difference in terms of quality control for post-processing activities. Under the current licensing fee structure, a small or cottage-scale farm and large industrial nurseries and processors pay the same, flat fee for these activities.

Tiering of license fees based on size is also required by statute. BPC 26180(c) states that:

“All license fees shall be set on a scaled basis by the department, dependent on the size of the business.”

Initial Recommendations for a Sustainable and Equitable Licensing Fee Structure

Based on this analysis, we recommend the DCC implement the following changes as part of their re-evaluated licensing fee structure:

- Recommendation #1: Cultivation licensing fees should be dramatically reduced to correspond with dramatic changes in market conditions.
- Recommendation #2: The current inequities in licensing fees between smaller and larger farmers should be corrected.
- Recommendation #3: Smaller farmers should have the same ability as larger farmers to increase their cultivation size incrementally.
- Recommendation #4: Processing and nursery licenses should be tiered based on size as with all other license types.

We look forward to learning more about the DCC's ideas for reforming the licensing fee structure, as well as the economic analysis of the licensing fee structure that we understand is currently in process. As this process continues, we hope to collaborate with the DCC on implementing a sustainable and equitable licensing fee structure.

Thank you for your consideration,



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