

FEBRUARY 25, 2020

Cannabis: Proposed Consolidation of Regulation and Identifying the Elements of the Illicit Market

PRESENTED TO:

Assembly Budget Subcommittee No. 4

On State Administration

Hon. Jim Cooper, Chair

and

Assembly Business and Professions Committee

Hon. Evan Low, Chair



LEGISLATIVE ANALYST'S OFFICE

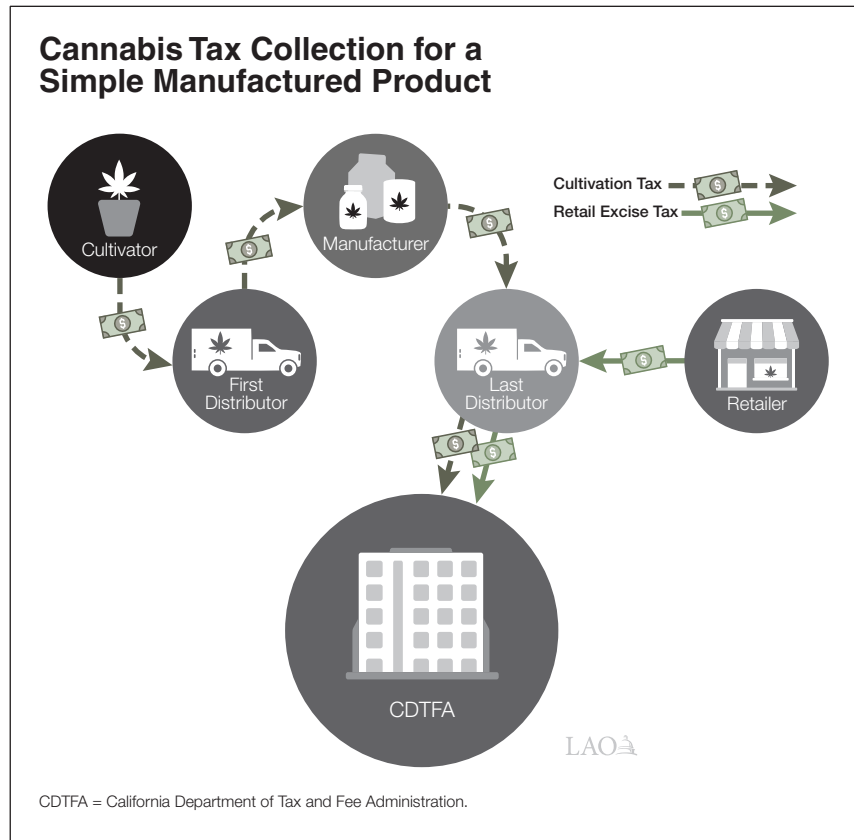
Proposition 64 Created Cannabis Regulatory and Tax Structure

- Under Proposition 64 (2016), adults 21 years of age or older can legally grow, possess, and use cannabis for nonmedical purposes, with certain restrictions.
- Various state agencies have roles related to regulating the cannabis industry. For example, three state departments—the Bureau of Cannabis Control (BCC), California Department of Food and Agriculture (CDFA), and Department of Public Health (DPH)—have responsibility for licensing different types of cannabis businesses, such as retailers, distributors, cultivators, and manufacturers.
- Proposition 64 established two state excise taxes on cannabis, which are administered by the California Department of Tax and Fee Administration (CDTFA).
 - 15 percent excise tax on retail gross receipts (known as the retail excise tax).
 - Cultivation tax on the weight of harvested plants. (Currently, \$9.65 per ounce of dried flowers, \$2.87 per ounce of dried leaves, and \$1.35 per ounce of fresh plants.)



Proposition 64 Created Cannabis Regulatory and Tax Structure

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- Cultivators and retailers bear the legal responsibility for the initial payment of the cultivation and retail excise taxes, respectively.
- However, pursuant to Chapter 27 of 2017 (SB 94, Committee on Budget and Fiscal Review), final distributors—rather than cultivators or retailers—must remit these taxes to CDTFA, resulting in a multistep payment process as shown in the above figure.



Governor's Proposals

Change Point of Collection of Cannabis Taxes

- The Governor proposes budget trailer legislation to move the responsibility for remitting the cultivation tax from the final distributor to the first distributor and the responsibility for remitting the retail excise tax from the final distributor to the retailer.
- The Governor indicates that he will consider other changes to cannabis taxes. However, to date, the administration has not provided any additional details on what specific changes are under consideration.

Consolidate Licensing Functions Into New Department

- The Governor proposes consolidating the cannabis-related licensing functions that are currently housed in BCC, CDFA, and DPH into a new department, the Department of Cannabis Control.
- The administration anticipates providing further information this spring.



Issues for Legislative Consideration

Changes to Point of Collection Would Improve Tax Administration, but Other Tax Changes Also Warranted

- We find that changing the point of collection for the retail excise and cultivation tax should improve tax administration and compliance by creating a closer nexus between the taxed activity and the responsibility for remitting taxes.
- As such, if the Legislature retains the retail excise and cultivation taxes, we recommend approving the Governor’s proposal.
- We also recommend the Legislature consider other changes to the state’s cannabis tax structure and rates.

Concept of Consolidating Licensing Functions Makes Sense, but Details Are Important

- We find that the concept of consolidating the cannabis licensing functions into a single entity focused on cannabis makes sense, and could improve the accountability and effectiveness of the state’s cannabis activities.
- However, the Legislature will want to closely evaluate the details of the Governor’s proposal to ensure it is well-planned and aligns with legislative priorities.
- Accordingly, we recommend that the Legislature request the administration to provide additional details on the plan—and the associated budget proposal and trailer bill legislation—as soon as possible.

