



COUNTY OF HUMBOLDT

For the meeting of: 11/12/2024

File #: 24-1504

To: Board of Supervisors

From: County Administrative Office

Agenda Section: [Time Certain Matter](#)

Vote Requirement: Majority

SUBJECT:
10:30 am - Update on Cannabis Cultivation Excise Tax

RECOMMENDATION(S):

That the Board of Supervisors:

1. Receive an update on past due billings, suspension regulations, and estimated administrative costs;
2. Set the Tax Year 2025 tax rate for Measure S at 10% of the normal cost, or choose one of the alternatives discussed in the report;
3. Direct staff to take necessary actions to implement the direction of the Board; and
4. Take other action as necessary

STRATEGIC PLAN:

This action supports the following areas of your Board's Strategic Plan.

Area of Focus: [A Diverse, Equitable & Robust Economy](#)

Strategic Plan Category: [2001 - Promote strong economic resiliency and growth](#)

DISCUSSION:

Last October your Board took several actions related to local cannabis cultivation, including requiring cultivators with outstanding balances to enter into payment plans, develop regulations allowing for suspension of permits for unpaid fees and taxes, and reinstating the Measure S tax at 10% the normal cost for Tax Year 2025. This item provides an update on activity that has taken place since that meeting, and considerations for future actions, including whether to continue with a 10% tax rate next year, or consider another rate or tax structure.

Payment Plans and Revocation of Permits for Unpaid Taxes

Payment Plans/Unpaid Balances

One action your Board took last fall was to require cultivators to enter into a payment plan by June 30, 2024, with balances to be paid in full by March 31, 2025. Nearly half of cultivators with past due balances have signed up for payment plans, and less than 10% of the total balance has been paid since October 2023. Below is information on where the county stands in regard to accounts with a balance:

	As of October, 2023	As of October, 2024
Accounts with a balance	962	771
Signed up for payment plan		418
Amounts due	\$14.19 million	\$11.97 million
Past due amount collected		\$896,985
Past due amount cancelled		\$1.32 million

Not signed up for payment	
Total number of accounts	353
Active	221
Inactive	132

At the time your Board took this action, the county had 962 accounts with outstanding balances, totaling \$14.19 million. Since then, 418 accounts have implemented payment plans indicating that they will have their balances paid off by March 31, 2025.

The Treasurer-Tax Collector has collected \$896,985.30 since October, 2023. Roughly \$1.3 million of the past due amount has been either reduced or canceled because the billed amount was not the amount cultivated or needed a clerical correction. The remaining outstanding balance stands at \$11.97 million.

The average amount owed is \$15,521. There are 550 accounts (67% of all accounts with a past due balance) that owe this amount or less.

There are 353 accounts remaining with unpaid balances that have not signed up for payment plans. Of these accounts, 132 are “inactive,” meaning the Planning & Building Department has indicated that they are no longer using their cultivation permits, adding an element of difficulty to collection of past due amounts. These inactive accounts have a total \$2.6 million past due.

Modifying Ordinance to Allow for Suspension/Revocation of Permits for Unpaid Taxes

A second action your Board took was to direct staff to modify county code to allow for suspension and revocation of permits for unpaid taxes and fees. On March 5, 2024, the Planning & Building Department brought an item to your Board amending the Zoning Ordinance to create permit suspension procedures, and subsequently contacted permit holders with outstanding balances. After verifying payment statuses (or lack thereof), Planning & Building issued suspensions, and to date 125 permits remain in suspension. Eventual revocation of a permit can only occur with Board action, and the Planning & Building Department will return to the Board after March 2025 with further recommendations regarding revocation if any accounts continue with outstanding balances.

Reinstating a 10% Cultivation Excise Tax for Tax Year 2025, Administrative Costs

A third action your Board took was to inform cultivators that Measure S taxes would be reinstated for bills issued in 2025 (for 2024 cultivation activity) at 10% of the normal amount, including Consumer Price Index increases. Bills are to be issued in March 2025 with the first installment due in May and second in October.

Amounts will be set at the following levels:

- \$0.13 per square foot for outdoor cultivation
- \$0.26 for mixed light, and
- \$0.38 for indoor

Staff are prepared to carry out Board direction related to preparation of 2025 tax bills. Staff also recommend amending the Measure S tax ordinance to allow the Board to modify the tax rates by resolution, as long as it does not increase the tax or broaden the scope, in order to provide a clear process to setting rates annually.

It is notable to observe the timing of upcoming bills and deadlines. Cultivators will be required to fully pay their unpaid balances by March 2025 and in that same month will be receiving a new tax bill. To consider impacts on individual cultivators, the average amount billed was roughly \$2,700 (total of both installments) when the county last sent out Measure S tax bills in Tax Year 2022 (which were assessed at 15% the normal cost).

Staff have prepared other options for your Board to consider should you wish to modify this prior direction, under the Alternatives to Staff Recommendation section below.

Revenue and Administrative Expenses

There has been interest in calculating how much it costs the county to administer the Measure S tax and comparing it to the revenue received. More is detailed below, but staff believe it is reasonable to assume that billing at 10% of the normal cost would provide roughly \$1 million or less in revenue in calendar year 2025 (\$500,000 in Fiscal Year 2024-25), while staff costs are likely \$200,000 to \$300,000.

Revenue

Forecasting the potential revenue is difficult because the amount of tax owed is based on actual cultivation activity that occurred during the year, and staff have limited means to confirm that information prior to issuing bills. Frequently, individuals dispute the amounts assessed after bills are issued, reporting that their actual cultivation was less than the amount assessed on their tax bill, which can dramatically decrease the total tax liability.

Therefore, a method to measure potential revenue is to evaluate Tax Year 2022 (for 2021 activity). This year had a total billing of \$3.3 million, which was for 15% of the normal cost. The accounts that have paid in full through Tax Year 2022 total \$1.5 million. However, staff have not determined whether those payments were only for the 2022 bills, and it is likely some of the payments were for past due bills.

Administrative Expenses

It must be noted that the Agricultural Commissioner’s Office is the only department that can bill staff time related to Measure S to a funding source and therefore (with few exceptions) staff have not tracked their time on Measure S activities with great detail. The information below is highly variable and represents staff’s best estimates, and the value of staff time is according to individual departments’ productive hourly rates, which includes salaries, benefits, overhead and central service costs. In addition, it does not include the Assessor’s Office time on the Assessment Appeals Board hearing Measure S refund items, or time spent on policy development by the departments listed below, as well as County Counsel’s Office, the County Administrative Office and your Board.

Department	Total Estimated Cost
Planning & Building	\$94,000
Agricultural Commissioner	\$114,000
Treasurer-Tax Collector	\$34,500
Auditor-Controller	\$13,000
Clerk of the Board	\$4,400
TOTAL	\$259,900

Regarding staff costs, the Planning & Building Department estimated that at least three different classes of employees are involved with reviewing cultivation reduction forms and cultivation areas for tax reductions, information requests, correcting and explaining tax bills, and performing analysis requests for refunds. It should be noted that this is likely a low time estimate and roughly 25% of an employee’s time on Measure S is spent on revised tax billing issues. As this work is related to tax collection and not permitting it is not activity that Planning can bill for through the fee schedule. In addition, the staff work related to reviewing cultivation reduction requests is aided greatly by the department’s use of satellite imagery, without which would require exponentially more effort to verify cultivation area.

The Agricultural Commissioner’s Office from Fiscal Years (FY) 2018-19 to 2020-21 (the last year it has data available) had an average of \$113,840 in unreimbursed cannabis inspection activity per year. This activity is required to keep cultivators permitted. The Treasurer-Tax Collector’s (TTC) activity was concentrated around times of bill issuance, and in May and October when bills had been due traditionally. However, activity has become more sporadic throughout the year due to the

authorization of payment plans and suspension of annual taxes. The TTC's activities are on administering Measure S taxes, payment plans and refunds at an annual cost of \$34,500, using staff's fully burdened rates. The Clerk of the Board's Office is involved most heavily in refunds that come before the Assessment Appeals Board, and estimates it spends 2 hours per application processing the paperwork. It FY 2023-24 it processed 20 applications with an estimated cost of \$3,535. This work is anticipated to increase if a new round of bills is sent.

Finally, the Auditor-Controller's Office is responsible for processing refunds, issuing checks and posting Measure S activity to the general ledger. This annual cost is estimated at \$13,000 per year. However, should your Board reinstate Measure S at any level staff recommend accounting for Measure S separately from normal General Fund revenues in order to track expenditures. In this case, it would require additional ongoing work by the Auditor-Controller's Office.

Other Information

Permit counts

The Planning & Building Department records show there are 1,167 cannabis permits in post-approval monitoring, and slightly under 1,000 of those are cultivation permits. The county is down to 56 interim permits. There have been a total of 143 permit holders that have submitted Temporary Cultivation Reductions (TCRs) for 2024, and 71 of those reduced their cultivation area to 0 square feet, indicating they may no longer have an intention to cultivate.

Prior Actions

Below summarizes other actions taken by the Board related to Measure S taxes and past due amounts:

- February 2022: Reduced the county's Measure S Cannabis Excise Tax by 85%.
- November 2022: Temporarily suspended the tax for Tax Year 2023 (Cultivation Year 2022) and Tax Year 2024 (Cultivation Year 2023). Under this action, the next payments for normal cultivation taxes would be due in Tax Year 2025 (Cultivation Year 2024), with the first installment due by May of that year and second in October.
- November 2022: Suspended penalties and interest on the second installments of payments for Tax Year 2021 (Cultivation Year 2020) and both installments due in Tax Year 2022 (Cultivation year 2021). All other prior penalties and interest remained unchanged.
- January 2023: Authorized cultivators to make partial payments for their cultivation taxes.

It should be noted that there are still unresolved legislative actions, including legislation and regulations around hemp entering the cannabis marketplace and the county's diminishing ability to participate in the state's local equity grant program, amongst others, that may have an adverse economic impact on cultivators.

SOURCE OF FUNDING:

General Fund

FINANCIAL IMPACT:

<i>Expenditures</i>	FY24-25	FY25-26 Projected*	FY26-27 Projected*
<i>Budgeted Expenses</i>	<u>\$259,900</u>	<u>\$269,745</u>	<u>\$283,232</u>
<i>Additional Appropriation Requested</i>	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>
Total Expenditures	<u>\$259,900</u>	<u>\$269,745</u>	<u>\$283,232</u>

**Projected amounts are estimates and are subject to change.*

<i>Funding Sources</i>	FY24-25	FY25-26 Projected*	FY26-27 Projected*
<i>General Fund</i>	<u>\$500,000</u>	<u>\$1,000,000</u>	<u>\$1,000,000</u>
Total Funding Sources	<u>\$500,000</u>	<u>\$1,000,000</u>	<u>\$1,000,000</u>

**Projected amounts are estimates and are subject to change.*

Narrative Explanation of Financial Impact:

Staff are estimating that a cannabis excise tax assessed at 10% the normal cost would generate roughly \$1 million in revenue in FY 2025-26, however, no revenue was budgeted in FY 2024-25. Staff costs related to Measure S as described in the discussion will be incurred whether or not the county receives Measure S revenue. The staff costs here grow by 5% each year to account for salary and benefit increases. It is critical to note that the General Fund continues to operate in a deficit and the County Administrative Office would recommend funding existing unfunded activities with this revenue, as opposed to expanding service.

STAFFING IMPACT:

Narrative Explanation of Staffing Impact:

There is significant staff time associated with processing the Measure S tax, and there would be significant staff time needed to revise the measure for a future ballot. In the past, Measure S has provided funding for staff and services in the Sheriff's Office, Aviation, Planning & Building, County Administrative Office - Economic Development, and others. Restoration of this funding source could provide needed funds for staffing, grant matches and professional services, such as those offered through California Cannabis Authority (CCA).

OTHER AGENCY INVOLVEMENT:

Humboldt County Grower's Alliance, CCA,

ALTERNATIVES TO STAFF RECOMMENDATIONS:

Measure S was conceived at a time when cannabis prices were much higher, and the cost of regulatory compliance was not considered. It was anticipated that the revenue from cannabis farms would be much higher and paying taxes would not be an issue. This is not the case. The price a farmer can get for cannabis is often set very close to the cost it took to produce. Therefore, the Board has taken many actions to balance the need for local revenue to maintain and increase public services and trying to provide a fair rate for cultivators. While your Board has directed that the rate for Tax Year 2025 be set at 10% of the normal value to be applied to all cultivation, it has also expressed a desire to consider other structures, including potentially taking a restructured measure back to voters.

The Commercial Marijuana Cultivation Tax Ordinance states that rates will be set at \$1 for outdoor cultivation, \$2 for mixed light, and \$3 for indoor. However, your Board may reduce the tax rates within those cultivation types, or uniformly, as has been done the prior 3 years.

Below are options to consider that would be possible to implement under the current ordinance, and options that would require voter approval.

Options that can be implemented under the current ordinance:

1. Continue with a low percentage that allows some revenue.
 This is the current staff recommendation as it was directed by your Board last year. This approach maintains the tax in the spirit of Measure S while simultaneously acknowledging the current market struggles. While the delinquency rate on this tax seems likely to continue, it should provide some revenue to pay for administering the activity, as well as some revenue for other services.

2. A graduated tax with rates based on impact.
 Larger farms have higher impacts (roads, tax collection, etc.) and thus could warrant a higher tax rate, while remaining within the rate parameters established by the ordinance. Your Board could also choose to specify that revenues from the measure are used to address specific activities, including long-term impacts from cannabis cultivation (like improvements to roads, environmental remediation, social and health-related impacts) or existing expenditures like staffing mentioned above or CCA membership. On June 21, 2016, the Board considered adopting tiered tax rates broken down by total amount of cultivation per taxpayer. Below is a sample tax structure, which has similar tiers of cultivation area. The smaller operations as a general practice have lower impact, and also produce less commercial product, lowering their income and thereby ability to pay higher taxes.

Indoor	Up to 1,000 sq ft	Up to 5,000 sq ft	5,0001 and over	
Tax rate as %	5%	7.5%	10%	
Tax rate as \$	\$ 0.19	\$ 0.29	\$ 0.38	
Mixed Light	Up to 5,000 sq ft	Up to 10,000 sq ft	10,0001 and over	
Tax rate as %	0%	5%	10%	
Tax rate as \$	\$ -	\$ 0.13	\$ 0.26	
Outdoor	Up to 5,000 sq ft	Up to 10,000 sq ft	10,001 to 22,000	22,001 and over
Tax rate as %	0%	5%	7.5%	10%
Tax rate as \$	\$ -	\$ 0.06	\$ 0.10	\$ 0.13

Again, revenue estimates are highly volatile in the current environment, however, as stated above, the average tax bill in 2022 was \$2,800 and average amount past due is just over \$15,000. These bills are more likely for relatively smaller cultivation operations, and by reducing or eliminating the tax on them it could potentially improve the rate at which operators pay taxes on time. While it could occur that many cultivators reduce their operations to achieve a lower or even possible 0% tax rate, staff believe it is reasonable to estimate that a graduated tax rate as proposed would provide at least \$500,000 per fiscal year.

3. Assess Measure S at the adopted tax rate.

This would set the rate at \$1.28 for outdoor cultivation, \$2.56 for mixed light, and \$3.84 for indoor, which includes increases for CPI. Revenue estimates for this amount are more difficult as the higher tax rate would likely increase the delinquency rate for payment. Tax bills, while subject to actual cultivation, would be at least \$13.9 million (if all cultivation was outdoor), based on Tax Year 2022 bills. Average tax bills would be at least \$11,900, and assuming a delinquency rate of 50%, revenue would be at least \$6.9 million.

4. Set tax rate at zero.

Your Board could continue with a suspension of the cultivation tax. The state eliminated the cannabis cultivation tax on state licenses, and Humboldt County aggressively advocated for this action to protect farmers, especially small farmers given how the state cannabis market has evolved. County departments would continue to incur some expenses regarding Measure S activity, particularly related to ongoing refunds, however, that activity would taper off.

Options needing voter approval:

1. Using state information as basis for a production-based cultivation tax.

This would base an excise tax on the amount of cultivated cannabis that enters the state licensing system, as reported by the state. In January, the State of California began allowing local agencies to have access to METRC, the program it uses to track and trace cannabis activity, including cultivation, through the supply chain. This could potentially relieve some workload from staff when it comes to calculating taxes owed. However, it should be noted that a common complaint of the METRC system is that it is porous and can encourage diversion of cannabis away from the regulated market.

2. Pursuing a cannabis business tax.

As stated above, the delinquency rate continues to be an issue to providing revenue related to the cultivation tax. One difference between this measure and other existing local measures is that sales tax and transient occupancy taxes are collected during an actual transaction, while the cultivation tax is collected separately. In the topic of revising the cultivation tax, it may be worth considering altering it to be a business tax on gross receipts of cannabis-related sales as it would put the responsibility on the vendor to collect the tax and remit to the Treasurer-Tax Collector. Similar measures have been passed in other local jurisdictions. The state currently imposes a 15% tax on gross receipts on retail sale of cannabis or cannabis products. One of the state's rationales for eliminating the cultivation tax was that it could still fund public health and related programs with sales taxes on cannabis products. However, it should be noted that if revenues fall the state will increase this sales tax from 15% to 19% in order to maintain services.

3. Researching other potential approaches and measures.

There are a variety other local revenue measures related to cannabis that have been implemented since adult use commercial cannabis was legalized in California in 2016, each with varying levels of success. Staff could work with CCA and its partner agency, California Public Policy Consulting, and others to research options to bring back to your Board for consideration. This service is included with the county's CCA membership.

ATTACHMENTS:

1. Current Balances as of Oct. 22, 2024
2. Public Comment Letters

PREVIOUS ACTION/REFERRAL:

Meeting of: Oct. 3, 2023; March 5, 2024; June 21, 2016
File No.: 23-1341; 24-253; 16-4433