The Great California Experiment – Is It Working? Regulatory and Industry Perspectives on the Success and Challenges of 2018

Dr. Jennifer Price, D.C.
Co-Founder & Director of State Compliance
Golden State Government Relations
www.goldenstategr.com
Conflict of Interest Statement:

As Director of State Compliance at Golden State Government Relations, I am a consultant to cannabis industry stakeholders, providing state licensing and compliance services. Though the subject matter of this presentation has been inspired by my experiences representing cannabis industry in the newly regulated market, this presentation has not been funded or sponsored by a cannabis business.
Assess some of the key goals of formal government regulation of the cannabis industry in California and evaluate the degree of accomplishment of those goals in the first year of regulations, based on available data.

Share the perceptions and opinions of cannabis industry stakeholders regarding the accomplishment of regulatory goals, the challenges experienced by the industry in the first year of regulation, and outlook on the future of the industry in California.
History of the Regulation of Cannabis in California

- California was the first state to allow medicinal cannabis use, and for 20 years, left it essentially unregulated, giving way to a state-sanctioned free market
  - 1996 – Proposition 215, the Compassionate Use Act, was passed by voters, allowing cannabis use for medicinal purposes if recommended by a medical doctor
    - Regulation was left to local agencies
  - 2003 – Senate Bill 420, the Medical Marijuana Program Act, allowed the medicinal cannabis industry to organize as collectives and cooperatives
    - Provided limited protections from prosecution
History of the Regulation of Cannabis in California

• By 2016, the state was finally taking action to transition to regulatory framework

  – 2015 – California enacted the Medical Cannabis Regulation and Safety Act (MCRSA) via the passing of Assembly Bill 266, Assembly Bill 243, and Senate Bill 643

  – 2016 – Revision of Senate Bill 837 and Assembly Bill 2516

  – 2016 – Voters approve Proposition 64, the Control, Regulate, and Tax Adult Use of Marijuana Act (AUMA)
History of the Regulation of Cannabis in California

- 2017 – Release of proposed regulations under MCRSA and 45-day public comment period

- 2017 – Senate Bill 94 reconciled MCRSA and AUMA, providing uniform standards for both medicinal and adult-use cannabis activity, Medicinal and Adult-Use Cannabis Regulation and Safety Act (MAUCRSA)

- 2017 – Release of proposed Emergency Regulations
History of the Regulation of Cannabis in California

- 2018 – Implementation of the Emergency Regulations
- 2018 – Revision of Emergency Regulations
- 2018 - Proposed Regular Regulations with 45-day public comment period
- 2018 – Revision of proposed Regular Regulations with 15-day public comment period
- 2018 – Final drafts of proposed Regular Regulations submitted to OAL for approval
- 2019 - Implementation of Regular Regulations – January 16th, 2019
Goals of Regulation

- Three Primary Categories

  - Limiting the impact of the illegal cannabis market
    - Supressing the presence of an illegal market for cannabis or cannabis products in the state or out of the state
    - Reducing negative environmental impacts that result from illegal cannabis activities

  - Reducing harm to public health and safety
    - Reducing and preventing crime, violence, and use of firearms in relation to cultivation and distribution of cannabis
    - Understanding and preventing drugged driving
    - Minimizing exposure to and use by minors and young people

  - Raising revenue for the state
    - Collecting additional revenue from new Excise Taxes and Cultivation Taxes
Challenges of Implementation - Logistics

- Trying to rein in a 20-year-old, fully operational, virtually uncontrolled, grey market industry is an extremely challenging undertaking on its own

  - The market place and supply chain have already found a means of existence
  
  - Years without a framework for regulating the industry made California cannabis business operators accustomed to breaking the rules to survive
  
  - Suddenly trying to halt this behavior and steer the industry towards a straight and narrow path has not been easy or well received
Challenges of Implementation - Logistics

- Choosing to address this challenge by relying on multiple state agencies to coordinate the effort as opposed to creating one single controlling entity proved to create additional complications.

- Department of Consumer Affairs – **Bureau of Cannabis Control**
- California Department of Food and Agriculture - **CalCannabis**
- California Department of Public Health - **Manufactured Cannabis Safety Branch**
- State Water Resource Control Board
- State Water Quality Control Board
- California Department of Fish and Wildlife
- California Department of Tax and Fee Administration
- California Department of Pesticide Regulation
- California Occupational Safety and Health Administration
Challenges of Implementation - Logistics

- Local jurisdictions have struggled to keep up with pace of the state in creating their own ordinances and permitting processes
  - Jurisdictions that were proactive about commercial cannabis activity and created ordinances in advance of the 2018 state licensing process created them without knowing what the state standards would be
  - Some jurisdictions had not developed their ordinances and permitting processes in time for temporary licensing
The implementation of Emergency Regulations, their subsequent revision, followed by the introduction of Regular Regulations within the span of just over a year has manifested a constantly moving target for licensees and have been implemented on short notice:

- Packaging and labeling requirements
- Phasing in of 3 levels of laboratory testing requirements
- Business hour requirement by CDFA
- Transportation vehicle requirements

The passing of Prop 64 ultimately resulted in MAUCRSA replacing MCRSA, and with that, a complete overhaul to the regulations that were already in the works to regulate medicinal cannabis.
Challenges of Implementation - Timeline

- By government standards, commercial cannabis regulation was placed on a short timeline to implement the regulatory process, and an even shorter timeline for existing operators to come into compliance and transition to the regulated market
  - Passing of bills in 2016 with Jan 1, 2018 deadline, further complicated by passing of prop 64 in 2017
  - 1-year transition period with temporary licensing

- Short time between release of regulations and their effective dates
Challenges Faced by Regulators

- The temporary licensing process
- Short timelines and continuous changes in requirements
- Unfilled staff positions, both for licensing and enforcement
- Licensing restrictions on canopy size resulting in numerous cultivation applications to be processed for single operations, on a single property, operated by a single entity
- Under Pressure to meet additional deadlines dictated by statute which are not directly related to the basic licensing and enforcement processes
  - Appellation Program no later than January 1, 2021
  - Cannabis Organic Program no later than January 1, 2021
  - Recommendations for addressing impaired driving no later than January 1, 2021
- Addressing regulatory language that in practice resulted in problems with operational functionality
- Track and Trace unavailable to temporary licensees reduces monitoring capability
Challenges Faced by Applicants and Temporary Licensees

- Short timelines
- Local permitting processes causing conflict with the ability to obtain temporary or annual licenses
- Concern over ability to obtain annual licenses in time for the expiration of temporary licenses and potential to be forced to shut down
- Continuous changes in packaging and labeling requirements wreaking havoc on the entire supply chain
- Cultivators facing complications with the Water Boards and/or Fish and Wildlife
- Difficulties with lab testing results
- Difficulties with banking
- High cost of entry into regulated market combined with very small margins is resulting in business closures or dependence on mergers and acquisitions is eliminating smaller businesses who cannot cope with the financial demands of licensing and coming into compliance and posing a major threat to larger businesses too
- Black market appears to be continuing to thrive
Measures of Success of Regulation in 2018: Materials & Methods

- Research articles and statistical data was collected from various sources including:
  - Research journals, online publications
  - Privately commissioned studies and reports
  - The reports, updates, press releases, and publicly available data of government agencies including BCC, CDFA, CDPH, LAO, CDTFA, DEA

- Limitations of Research
  - The available information and statistics for 2018 was limited as we are currently only in the first few weeks of 2019 at the time of this presentation
  - Very little available data and information on the California cannabis industry prior to 2018 for making comparisons, despite having had an active medicinal market for over 20 years
Measures of Success of Regulation in 2018: Limiting the Impact of the Illegal Cannabis Market – Suppressing the Black Market

- Illegal Cannabis Market Prior to Regulation
  - A Medical Cannabis Cultivation Program (MCCP) Standardized Regulatory Impact Assessment (SRIA), prepared for the CDFA in January of 2017, deduced the following baseline numbers for pre-regulatory black-market cannabis sales
    - Estimated quantity of cannabis for illegal sale within-California = 1.6 million pounds
    - Estimated quantity of cannabis for illegal export = 11 million pounds
  - In 2017 the US Drug Enforcement Agency (DEA) Cannabis Eradication/Suppression Program seized and destroyed nearly 2.5 million cannabis plants, and 91,871 pounds of processed cannabis in California
Measures of Success of Regulation in 2018: Limiting the Impact of the Illegal Cannabis Market - Suppressing the Black Market

- Illegal Cannabis Market Since Regulation
  - Knowing the impact of regulation on the illegal market is very complicated to achieve - so little data available on California illegal market cannabis activities prior to regulation to use for comparison
  - 2018 data points yet available at the time of this presentation
Measures of Success of Regulation in 2018: Limiting the Impact of the Illegal Cannabis Market - Suppressing the Black Market

- Measuring Success
  - Verifiable evidence of suppression of the illegal cannabis market by the regulated market will take time

  - Analysis of a 2018 online survey of 1,750 cannabis consumers from CA and CO by the cannabis retail delivery platform Eaze revealed:
    - 18% of CA cannabis consumers are still purchasing from an unlicensed source, and 84% of those consumers are highly likely to purchase from an illegal source again
    - Tax rates are a driving factor of illegal market purchases in CA
      - 23% of illicit market supporters would purchase from the legal market if taxes were reduced 5%
      - 32% of legal market supporters would purchase from the illegal market if taxes were increased 5%
Measures of Success of Regulation in 2018: Limiting the Impact of the Illegal Cannabis Market - Suppressing the Black Market

State Licensing Statistics for 2018

<table>
<thead>
<tr>
<th>License Type</th>
<th>Temporary Licenses</th>
<th>Annual Licenses</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cultivation</td>
<td>6828</td>
<td>3</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>1232</td>
<td>14</td>
</tr>
<tr>
<td>Retail</td>
<td>630</td>
<td>8</td>
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<tr>
<td>Non-Storefront Retail</td>
<td>318</td>
<td>0</td>
</tr>
<tr>
<td>Distributor</td>
<td>1224</td>
<td>1</td>
</tr>
<tr>
<td>Distributor - Transport</td>
<td>183</td>
<td>0</td>
</tr>
<tr>
<td>Laboratory</td>
<td>54</td>
<td>0</td>
</tr>
<tr>
<td>Event Organizer</td>
<td>95</td>
<td>6</td>
</tr>
</tbody>
</table>
Measures of Success of Regulation in 2018: Limiting the Impact of the Illegal Cannabis Market
- Suppressing the Black Market

- Temporary application process at first glance appears to have had some success

- Cultivation license numbers are deceiving and not impressive compared to estimates of the pre-existing number of cultivators
  - For the approximately 6,800 active temp licenses at the end of 2018, only about 2,800 entities that hold them, and of those, many are different entities within the same operation
  - With a report from the California Grower’s Association in 2018 estimating that California had 68,000 cultivators prior to the regulated market, 2,800 licensees is alarmingly low at about 4%
Measures of Success of Regulation in 2018: Limiting the Impact of the Illegal Cannabis Market - Suppressing the Black Market

- Assessment
  - Success in suppressing the illegal market has yet to be proven
  - As of 2018, in-state illegal market sales have not ceased
  - Illegal export is not likely to decrease until out-of-state demand decreases and/or the regulated market causes the risk premium to reduce drastically enough that illegal export is no longer appealing
Measures of Success of Regulation in 2018: Limiting the Impact of the Illegal Cannabis Market – Reducing Environmental Impact

- Negative Environmental Impacts of Illegal Cannabis Activities Identified in (MCCP) (SRIA)
  - Impacts on water supply & water quality as a direct result of illegal cannabis activity which is endangering public safety, endangering fish species, and impacting other wildlife
    - Causing erosion and sediment discharge
    - Water is illegally diverted from streams and other water sources that local wildlife depends on
  - Trash, human waste, pesticides, fertilizers, and petroleum hydrocarbons are being discharged into the environment
Measures of Success of Regulation in 2018: Limiting the Impact of the Illegal Cannabis Market – Reducing Environmental Impact

- **Measuring Success**
  - Positive influence of regulation on the environment will take time to become observable
  
  - Success will only be achieved if a significant number of illegal operators either convert to the regulated market and comply with environmental laws, or cease operations
Measures of Success of Regulation in 2018: Reducing Harm to Public Health and Safety – Reducing Crime & Violence

- **Existing Research is Positive**
  - Though specific statistics are not available to gauge the success of regulation in 2018 on reducing crime and violence, there are studies that support a strong likelihood of improvement
  
  - A 2017 study on the effects of medical marijuana laws on US crime in Mexico border-states found that violent crimes related to marijuana were reduced (Gavrilova et al, 2017)
    
    - FBI data shows California saw a 15% reduction in violent crime with the introduction of a medical cannabis program in 1996
    - The legal market competes with the illegal market and drives down prices across the board, making the cost of conducting and enforcing illegal activity through violence less financially viable
Measures of Success of Regulation in 2018: Reducing Harm to Public Health and Safety – Reducing Crime & Violence

– A 2016 report on marijuana incarcerations in California found a 21% decline in marijuana-only incarcerations and 42% decline in marijuana-plus-other-offenses incarcerations from 2010 to 2015 (New Frontier Data, 2016)

– A study published in 2018 in the Journal of Economic Behavior & Organization (Chu and Townsend, 2018) found that for states with medical marijuana laws:
  • No causal effects of medical marijuana laws on violent or property crime at the national level
  • No strong effects within individual states, except for in California where the medical marijuana law reduced both violent and property crime by 20%.
Measures of Success of Regulation in 2018: Reducing Harm to Public Health and Safety – Reducing Crime & Violence

- **Measuring Success**
  - The measure of success achieved by regulations has yet to be seen because it will need to be analyzed over a period of years.
  
  - Evidence from other states and California are indicating that legalization, even when unregulated, tends to decrease crime, so the likelihood of success in reducing violence and crime by creating a regulated market is high.
Measures of Success of Regulation in 2018: Reducing Harm to Public Health and Safety – Preventing Impaired Driving

- Cannabis-induced impairment while driving is a very difficult situation to study

- According to a presentation by Thomas D. Marcotte, PhD, at the UC San Diego Center for Medical Cannabis Research Symposium in June 2018 entitled “Cannabis & Public Safety: The Challenge of Cannabis Impaired Driving”:
  - Effects are not standardized – a “per se law” cannot be applied like it can with alcohol
  - No reliable assessment of impairment
Measures of Success of Regulation in 2018: Reducing Harm to Public Health and Safety – Preventing Impaired Driving

- Different modes of consumption, smoking vs. ingesting, have different effects and by different mechanisms
- Results in a controlled environment vs. real-life situations vary
  - In controlled environments it is evident that cannabis can cause impairment in braking and reaction times
  - In practice, most cannabis users drive with caution
    - More likely to judge themselves as being impaired
    - Tend to leave more headway between themselves and the car in front
    - Less likely to attempt passing another vehicle
Measures of Success of Regulation in 2018: Reducing Harm to Public Health and Safety – Preventing Impaired Driving

- **Measuring Success**
  - California has been attempting to address this particular public health and safety concern for some time, prior to prop 64
  - Don’t have a handle on the mechanisms of impairment and certainly don’t have the technology to standardize a way to gauge level of impairment yet
  - A lot of additional research over the coming years will be necessary, but some areas of focus should be:
    - Dosing
    - Field sobriety tests
    - Saliva tests
  - The success of regulation to prevent drugged driving has yet to be seen, but progress is being made in understanding it
Measures of Success of Regulation in 2018: Reducing Harm to Public Health and Safety – Minimizing Use by Minors & Young People

- The effects of the regulated commercial cannabis in 2018 on exposure and use by minors and young people in California are not clear yet as minimal data is available.

- Of the available data on youth throughout the US in recent years, the research is indicating that legalization is not resulting in increased use by young people.
  - A 2017 study in Washington and Colorado titled “Association of State Recreational Marijuana Laws With Adolescent Marijuana Use” (Cerda et al, 2017) found:
    - Legalization decreased perceptions of harmfulness of cannabis of 8th and 10th graders in Washington after legalization, as well as states that did not legalize, but no changes in perception for Colorado.
    - Cannabis use in Washington was increased as compared to states that did not legalize, where use decreased slightly.
    - In Colorado, no significant increase in use was found.
    - By 12th grade, no significant difference in perceptions of harmfulness or use for Washington or Colorado compared to states that did not legalize
Measures of Success of Regulation in 2018:
Reducing Harm to Public Health and Safety –
Minimizing Use by Minors & Young People

- In study on cross-sectional nationally representative surveys of US students, conducted annually, 1991–2014, on perceived harmfulness of marijuana and marijuana use (Keyes et al, 2016) it was found that the passage of medical marijuana laws (MML) is associated with:
  - Increases in perceived harmfulness among young adolescents
  - Marijuana use has decreased after passage of MML among those who perceive marijuana to be harmful

- A meta-analysis of 11 studies from the results 4 national surveys of adolescents (Sarvet et al, 2018) discovered:
  - None of the 11 studies found significant changes in past-month marijuana use following MML passage within MML states compared to comparable changes in non-MML states
  - Current evidence does not support the hypothesis that MML passage is associated with increased marijuana use prevalence among adolescents in states that have passed such laws up until 2014
In California, use by teens was already on the decline leading up to the regulated market 2018, lending further support to the findings of other studies across the country that cannabis legalization, regardless of regulation, does not result in increased use in youth – it may actually decrease use.

- The biennial statewide “California Healthy Kids Survey,” which assesses substance use among other things, found that in 2015-17 marijuana use among high school students declined:
  - 9th graders: 10% use, down 4 points
  - 11th graders: 17% use, down 3 points
Measuring Success

- The data to measure the impact of the 2018 regulated market on youth exposure and use is not yet available.
- Evidence supports a strong likelihood that it will be found that regulation of cannabis does not impact, and may even reduce, youth exposure and use.
Measures of Success of Regulation in 2018: Raising Revenue for the State

- Collecting additional revenue from Excise Taxes and Cultivation Taxes
  - Predicted Tax Revenue for the State
    - Legislative Analyst’s Office (LAO) June 2018 budget package assumed that cannabis related tax revenues would bring:
      - $185 million in 2017-18
      - $630 million in 2018-19
    - The LAO released a “Cannabis Tax Revenue Update” on November 15th, 2018
      - The update reported that the administration had recalculated their tax estimates:
        - 2017-18 was re-estimated at $84 million
          - $101 million below previous projections
        - 2018-19 now projected to be about $410 million if rapid growth continues, or
          - $280 million if assuming a more conservative growth rate
          - $220 - $350 million below previous projections
Measures of Success of Regulation in 2018: Raising Revenue for the State

- Tax Collection in 2018 Calendar Year
  - Cannabis Related Excise, Cultivation, and Sales Tax Collections reported by California Department of Tax and Fee Administration (CDTFA) for 2018:

<table>
<thead>
<tr>
<th>Type of Tax</th>
<th>1st Quarter</th>
<th>2nd Quarter</th>
<th>3rd Quarter</th>
<th>Combined Totals</th>
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</thead>
<tbody>
<tr>
<td>Excise Tax</td>
<td>$32 Million</td>
<td>$43.5 Million</td>
<td>$52.4 Million</td>
<td>$127.9 Million</td>
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<tr>
<td>Cultivation Tax</td>
<td>$1.6 Million</td>
<td>$4.5 Million</td>
<td>$12 Million</td>
<td>$18.1 Million</td>
</tr>
<tr>
<td>Sales Tax</td>
<td>$27.3 Million</td>
<td>$26.2 Million</td>
<td>$28.7 Million</td>
<td>$82.2 Million</td>
</tr>
</tbody>
</table>
### State Costs of Regulation

- The 2017-18 Budget: California Spending Plan, released by the LAO in June 2017 allotted a sum of $123.8 million of cannabis-related funding to state agencies involved in the regulation and enforcement of commercial cannabis activities.

- The 2018-19 Budget: California Spending Plan released by the LAO in June 2018 has roughly doubled the budget for cannabis regulation and enforcement, adding an additional $129.4 million of funding for the next two years.
  
  - **Total Annual Funding for Cannabis Regulation and Enforcement = $253.2 million**
Measures of Success of Regulation in 2018: Raising Revenue for the State

- Measuring Success
  - Tax revenue from cannabis was drastically less than initially predicted in the first year of regulation, but has increased quarterly by an average of 33%
  - At a cost of nearly $124 million for the 2017-18 fiscal year, California suffered a loss of almost $40 million to operate the cannabis regulatory program in 2017-18
  - The projections for revenue in 2018-19 are uncertain as the tax revenue growth rate is unpredictable
    - With low-end cost estimates coming in at $280 million, State likely to break even in 2018-19 with potential to profit
Industry Perspectives

Materials and Methods

- A survey consisting of multiple-choice questions and the opportunity for comment on the question topic was created for industry stakeholders
  - Questions addressed demographic information, perceptions of the success of the regulatory goals, challenges experienced by stakeholders during the transition to regulation, and perceptions of outlook for the future of the industry in California under the regulated market
  - Participation was anonymous
  - Participants were recruited via email and text using client and colleague contacts, and inclusion in a membership update email to the members of the California Cannabis Industry Association
- A total of 9 participants

Limitations

- Limited resources to proactively seek survey participation resulted in small sample
What is your involvement in the California Cannabis Industry?

9 responses

- 44.4%: Cannabis Business Owner/License Holder
- 22.2%: Executive at a Licensed Cannabis Business
- 11.1%: Manager at a Licensed Cannabis Business
- 11.1%: Investor/Financial Interest Holder in a Licensed Cannabis Business
- 11.1%: In the process of local permitting and/or state licensing
In which type(s) of commercial cannabis activity(ies) is your business licensed or seeking licensing? (check all that apply)

9 responses

- Manufacturing (including extraction, infusion, etc.): 5 (55.6%)
- Distribution (including transportation, delivery, etc.): 6 (66.7%)
- Laboratory Testing: 7 (77.8%)
- Retail: 4 (44.4%)
- Microbusiness: 0 (0%)
- Cannabis Events Organizer: 0 (0%)
Was your cannabis business engaged in commercial cannabis activity in California prior to January 1, 2018?

9 responses

100% Yes
0% No
Were you as an individual engaged in commercial cannabis activity prior to January 1, 2018?

9 responses

- Yes: 88.9%
- No: 11.1%
One goal of regulating the California cannabis industry is to reduce the illegal sale and out-of-state diversion...Illegal sales and out-of-state diversion?

9 responses

- 66.7%: It has increased illegal sales and out-of-state diversion
- 33.3%: It has had no impact/effect/change on illegal sales and out-of-state diversion
- Unsure / Not applicable
Industry Perspectives: Accomplishment of Regulatory Goals

- Comments:
  - We need more local governments to onboard cannabis licensing
  - The base price for flowers on the traditional market has increased from $600 to $1100 over the previous year. There are fewer underground growers, but a continuing demand for illicit cannabis because of high taxes and limited availability of legal cannabis products at a limited number of legal retailers in California. Many now Legal states cannot supply their in-state demand from in-state cultivators, and so the illicit market comes to the rescue. Apparently cross border seizures have increased.
One goal of regulating the California cannabis industry is to improve public safety by reducing and preventing violence in the California cannabis industry?

9 responses

- 22.2%: It has increased violent crimes
- 22.2%: It has had no impact or change on violent crimes
- 55.6%: Violent crimes have been reduced somewhat
- 22.2%: Violent crimes have been reduced significantly
- 0%: Unsure / Not applicable
Industry Perspectives: Accomplishment of Regulatory Goals

- Comments:
  - There has been increased enforcement against those growers causing environmental damage
One goal of regulating the California cannabis industry is to raise revenue for the state. Based on your experience...erms of raising revenue for the state?

9 responses
Industry Perspectives: Accomplishment of Regulatory Goals

Comments:

‒ We need more licensed businesses and less illicit business. Licensed businesses pay taxes... TAXES ARE TOO HIGH!!!!!!

‒ So few were able to obtain permits at city, county, and state level because of all the fees, inspections, restrictions, while the rules and regulations, kept changing. Many jurisdictions forbid any cannabis business.
In your experience, has the one year transition been long enough for your business to transition into full compliance with statute and regulations?

9 responses

- Yes: 33.3%
- No: 66.7%
- Unsure / Not Applicable: 0%
Industry Perspectives: Challenges Experienced in 1\textsuperscript{st} Year of Regulation

- Comments:
  - The timeline for this is completely untenable even with all the resources in the world
  - Yes for distributors, no for manufacturers.
Industry Perspectives: Challenges Experienced in 1st Year of Regulation

Have you or your business experienced delays or difficulties in your state licensing due to issues or hold-ups with your local permitting?

9 responses

- 66.7% Yes
- 22.2% No
- 11.1% Unsure / Not applicable
Industry Perspectives: Challenges Experienced in 1\textsuperscript{st} Year of Regulation

- Comments:
  - It would seem some cities and counties can lag on permitting more than others.
Are you concerned that your temporary license might expire prior to your annual license application being processed, temporarily as a result?

9 responses

- Yes: 44.4%
- No: 11.1%
- Unsure / Not Applicable: 44.4%
Industry Perspectives: Challenges Experienced in 1st Year of Regulation

- Comments:
  - I really hope this would not happen but it is causing us anxiety
Industry Perspectives: Challenges Experienced in 1st Year of Regulation

In your experience, do you believe reasonable time was allotted for complying with packaging and labeling requirements and changes?

9 responses

- Yes: 33.3%
- No: 66.7%
- Unsure / Not applicable: 0%
Industry Perspectives: Challenges Experienced in 1st Year of Regulation

- Comments:
  - Multiple changes have lead to increased costs for brands.
Has your business experienced issues or difficulties with lab testing results?
9 responses

- 88.9% Yes
- 11.1% No
- Unsure / Not applicable
Industry Perspectives: Challenges Experienced in 1st Year of Regulation

- Comments:
  - Running wrong tests. Large Variations for results from same lab. Some Labs test higher for potency than others. Levels of "shade" still exist at the lab level.
  - Labs should not be the gatekeepers of the supply chain without ample time to validate they are doing things replicable and correctly. There needs to be a way to dispute lab results if there is ample evidence or reason to believe the lab or equipment made an error.
  - Timeframes & multiple unique integrations.
Industry Perspectives: Challenges Experienced in 1st Year of Regulation

Does your business experience difficulties with banking?

9 responses

- Yes: 88.9%
- No: 11.1%
- Unsure / Not applicable: None
Industry Perspectives: Challenges Experienced in 1st Year of Regulation

Comments:

– We have already lost one bank and had to find another.

– We have cannabis banking now but it’s very difficult to work with and time consuming.
Industry Perspectives: Outlook on the Future of Cannabis Industry in CA

Of the existing commercial cannabis operators in California, what portion do you believe will survive for 5 or more years in the regulated market?

9 responses

- 55.6% believe all operators will survive
- 33.3% believe most operators will survive
- 11.1% believe some operators will survive
- 0% believe a few operators will survive
- 0% believe none of the operators will survive
- 0% unsure

2019 North American Cannabis Summit
Industry Perspectives: Outlook on the Future of Cannabis Industry in CA

- **Comments:**
  - The regulations, taxes, and lag time from government will kill the industry. They need to make some changes before Big Pharma, tobacco, and alcohol companies have nothing to purchase in 5 years.
  - Inevitable consolidation of a fragmented market. Big fish swallowing up the best mom and pop operators. Worst mom and pop operators will fail unfortunately.
  - "the goal should be to prevent the growth of a large, corporate marijuana industry dominated by a small number of players." - Gavin Newsom
  - Less than 3% of business will survive. It is an extinction.
Do you believe your business will survive 5 or more years in the California cannabis industry?

9 responses

- 77.8% Yes
- 11.1% No
- 11.1% Unsure
Industry Perspectives: Outlook on the Future of Cannabis Industry in CA

- **Comments:**
  - I'm worried we may only have one year left, but we luckily still have the option of finding more investors.
  - Only focused on real estate, not directly the supply chain so we're insulated for the most part.
  - Experience
Of the portion of cannabis businesses you expect to survive 5 years or more, what portion do you anticipate will...
Industry Perspectives: Outlook on the Future of Cannabis Industry in CA

- Comments:
  - Maybe one or two will remain independent but most will be bought out.
  - Very few, less than 2-3%.
  - Hopefully there will be incentives for innovation & for new brands to emerge.
Does your business anticipate or hope to be acquired by a larger or better funded entity?

9 responses

- Yes: 66.7%
- No: 22.2%
- Unsure: 11.1%
Comments:

- It's the only viable exit strategy.

- Biggest players are buying good licenses, not spending the time to do entitlements themselves.

- We had to sell 51% of the business to a publicly traded Canadian company to continue to have enough operating capital.
Conclusions

- **In General:**
  - The transition from a 20-year-old unregulated legal market to a regulated legal market has been a tremendous undertaking, both for the state and for cannabis businesses, with many growing pains
  - Success at achieving goals of regulation has been limited
  - Businesses participating in the regulated market are struggling to stay in operation
Conclusions

- **From the Regulatory Perspective:**
  - 2018 has provided little insight into the overall success of the goals of regulation; more time is required to truly measure success.
  - Reducing and eliminating the black market is a long way off with only an estimated 4% of cultivators coming into the regulated market in the first year.
  - The ability to significantly reduce the environmental impact of illegal cannabis cultivation will depend on significantly decreasing illegal cultivations which has yet to occur.
  - Reducing and preventing crime, violence, and use of firearms in relation to cannabis activity is likely to be successful based on reduced crime during the unregulated medical cannabis laws, and evidence from other states who have already implemented regulations.
  - Understanding and preventing drugged driving has a long way to go to achieve success.
  - Minimizing exposure and use by minors seems to be trending towards success.
  - Collecting additional revenue from taxation of commercial cannabis activity was not a success based on initial projections, however, tax revenue is on the rise and will likely improve over time with more businesses entering the regulated market.
Conclusions

- **From the Industry Perspective:**
  - Licensees are facing a variety of issues which are threatening the survival of the industry.
  - Obstacles from local government, meeting the state requirements which have been in constant flux, complications within the supply chain make operations difficult.
  - Taxation has a choke-hold on profit margins for businesses and continues to encourage customers to use the black market.
  - Operators seem to be lacking faith in the success of the regulated market.
  - There is a sense within the regulated industry that businesses will need to merge or be acquisitioned by larger companies to survive.

- **Overall, success has been limited in 2018 from both regulatory and industry perspectives, but there’s more change to come.**
References & Presentation
Available by Request
jenn@goldenstategr.com