

Date of Hearing: April 17, 2024

ASSEMBLY COMMITTEE ON APPROPRIATIONS

Buffy Wicks, Chair

AB 2888 (Chen) – As Amended April 3, 2024

Policy Committee: Business and Professions

Vote: 18 - 0

Urgency: No

State Mandated Local Program: No

Reimbursable: No

SUMMARY:

This bill requires a cannabis licensee to pay for goods and services of another licensee no later than 15 days after the final date in the invoice, and requires the licensee who has not been paid to report the unpaid invoice to the Department of Cannabis Control (DCC). The bill requires DCC to: (1) notify a licensee of a report of an unpaid invoice and (2) issue a warning or citation, or take other disciplinary action if the licensee fails to pay the invoice in full within 30 days of notification. The bill prohibits the licensee, until they have paid their outstanding invoice in full, from purchasing goods and services from another licensee on credit.

FISCAL EFFECT:

Costs to DCC of an unknown amount, potentially in the millions of dollars annually (Cannabis Control Fund).

Without knowing the number of impacted licensees and how prevalent the issue of nonpayment is, DCC states it was required to make assumptions to arrive at a cost estimate. DCC assumed:

- 1) Approximately 40%, or 3,800, of the 9,524 active licensee population, will fail to pay an invoice within the specified 15-day timeframe, and half of those licensees will have a second instance of failure to pay within 12 months, totaling 5,700 notices/letter of warnings issued within a 12-month period.
- 2) Approximately 40% of the 5,700 instances of a failure to pay will resolve, and 3,400 instances of noncompliance will have to be addressed through a progressive disciplinary approach ranging from a Notice to Comply, to a license revocation.

As the cases increase in complexity, enforcement will require a significant increase in legal resources. DCC estimates it will need at least \$13.2 million for the first year and \$12.4 million ongoing for various legal, compliance, and administrative staff to implement this bill (Cannabis Control Fund).

COMMENTS:

- 1) **Purpose.** This bill is sponsored by the California Cannabis Industry Association, the California Cannabis Manufacturers Association, and the Cannabis Distribution Association. According to the author:

AB 2888 is about fairness, both for the licensees who have played by the rules, and for Californians who agreed to a certain framework when cannabis was first legalized. This measure restores trust in an industry that has suffered because of bad-faith actors who have not held up their end of the bargain. Without ensuring timely payment, California's legal cannabis industry may never recover, this is a step towards building a marketplace that was envisioned when the Medicinal and Adult Use Cannabis Regulation and Safety Act which was passed in 2016.

2) **Background.**

- a) **Retail Cannabis Credit.** Because commercial cannabis activity is not legal at the federal level, the legal cannabis industry does not have access to the same banking, credit, or financing options available to other industries. Instead, the cannabis industry is mostly cash-based. According to the sponsors, cannabis businesses offer goods on credit to make up for the lack of normal financing options. They also note the credit terms may be extended to 60, 90, 120, or more days for payment. However, because there is no way to verify the creditworthiness of any other cannabis licensee, licensees are at risk of becoming overleveraged, owing more debt than they can pay back. The sponsors state the “debt bubble,” may lead to a destabilization of the industry. This bill is aimed at preventing further overleveraging by requiring licensees to pay within 15 days of the date on the invoice of cannabis products and establishing reporting and disciplinary requirements for licensees who fail to pay. The requirements are loosely based on California “tied-house” restrictions on alcohol manufacturers and the payment timelines between prime contractors and subcontractors.
 - b) **DCC Asserts a Remedy Already Exists.** DCC notes there is a legal system in place for businesses to seek a remedy for contract violations and nonpayment of services, and this bill essentially replicates within DCC the functions of the civil court system for contract violations.
 - c) **DCC Budget.** According to the Legislative Analyst's Office (LAO), the Governor proposes a total of \$171 million for the support of DCC in 2024-25, primarily from the Cannabis Control Fund, which receives revenues largely from cannabis licensing fees. The LAO also reports the Cannabis Control Fund is structurally imbalanced, meaning that its expenditures exceed its revenues. The fund balance has declined 52%, from \$169.1 million in 2021-22 to a projected \$80.5 million in 2024-25. DCC notes that if this bill increases DCC's expenditures beyond its current revenues, it will need to revise its license fee structure to implement the bill.
- 3) **Prior Legislation.** AB 766 (Ting), of the current legislative session, was substantially similar to this bill and was held in this committee.

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