

CONCURRENCE IN SENATE AMENDMENTS

AB 564 (Haney)

As Amended September 5, 2025

Majority vote

SUMMARY

Reduces the cannabis excise tax rate from 19% to 15% beginning October 1, 2025 and until May 1, 2028.

Senate Amendments

- 1) Reduce the cannabis excise tax rate to 15%, beginning on October 1, 2025, and until May 1, 2028.
- 2) Change the existing requirement that the California Department of Tax and Fee Administration (CDTFA) adjust the cannabis excise tax rate on or before May 1 every two fiscal years (FYs) to begin in the 2028-29 FY, rather than 2025-26 FY.
- 3) Change, from May 1, 2025, to May 1, 2028, the deadline for the requirement that the CDTFA report to the Legislature the estimated amount of cannabis cultivation tax revenues that would have been collected prior to the cannabis cultivation tax's repeal.
- 4) Require the CDTFA, for the purposes of complying with Revenue and Taxation Code Section 41, to report the estimated amount of gain or loss in cannabis excise tax revenues resulting from this bill's provisions, and find and declare that the specific goal of this bill's reduction is to provide immediate tax relief to the cannabis industry, which may be measured by the revenue gain or loss information required to be submitted by the CDTFA.
- 5) Require the Department of Cannabis Control (DCC), in consultation with the CDTFA and Legislative Analyst's Office, to submit a report to the Legislature containing certain information about the cannabis market, and recommendations for changes to the Cannabis Tax Law. This reporting requirement is repealed as of January 1, 2029.

COMMENTS

- 1) *Cannabis market outlook report:* In January of this year, ERA Economics, an agricultural and resources economics consultancy, prepared a report for the DCC, the *California Cannabis Market Outlook 2024 Report* (CCMO Report). The CCMO Report evaluated the overall state of the cannabis market in California, examining the supply and demand of cannabis, cannabis business licenses, and the illicit market.

The CCMO Report describes the fluctuation in demand, supply, and price of cannabis. Cannabis prices peaked in the third quarter of 2021 and have been declining since. "This downward trend is driven entirely by prices – quantity sold, in terms of flower weight, and units of edibles and vape cartridges, has continued to increase."

Contrary to arguments made by the cannabis industry, the legal market is not failing. The report states:

The total value of retail sales in the licensed market is down, leading some to conclude that the licensed market is failing or shrinking. The total volume of retail sales for nearly all product categories is up. That is, the decrease in the total dollar amount of retail sales is driven by lower prices, not less production to a contraction in the licensed market. The licensed market is continuing to grow.

Wholesale cannabis flower prices "dropped dramatically from the peak in 2020" resulting in "financial stress on cultivation and other cannabis businesses."

- 2) *Contextual factors and wholesale prices:* The CCMO Report did not examine the cause of wholesale price decreases. Rather, the report simply noted the trend and underscored that the legal market is expanding in the aggregate. Given this, one might reasonably ask what factors led to drastic decreases in prices that undercut potential revenue gains from the increase in legal product sold. While a full examination of factors is beyond the scope of this analysis, two critical factors likely impacted cannabis prices. The first was the COVID-19 pandemic. Amidst ongoing stay-at-home orders and work from home accommodations, many Californians lacked the ability to engage in recreational activities beyond their home. An article published in the National Library of Medicine finds that "qualitative data revealed that increases in cannabis and alcohol use were largely attributed to changes in employment and staying at home resulting in fewer impediments and boredom."

The second was the modification to cannabis taxes. The cultivation tax, as a flat amount tax, put downward pressures on cannabis production. Cultivators would have to pay the tax on the amount of cannabis grown no matter the sale price of the cannabis. When the state suspended the cultivation tax, the state removed this disincentive to grow.

In combination, the increased demand due to pandemic conditions and the suspension of the cultivation tax incentivized cultivators to produce greater amounts of cannabis. The data presented in the CCMO Report regarding the decline in the wholesale price of cannabis coincides with the tapering off of COVID-19 restrictions, though the report does not make a determination one way or the other to this effect. One might reasonably conclude that the decrease in wholesale cannabis prices is a correction to the lower, but still increasing, mean growth of the legal market.

- 3) *Complicating factors in success of the legal cannabis industry:* Turning to the text of Prop. 64 itself, more complicating factors regarding the success of the legal cannabis industry arise. Prop. 64 gave wide leeway to local jurisdictions regarding cannabis legalization and taxation. This has led to a patchwork implementation of the cannabis regulatory system throughout California. Thus, those jurisdictions that choose to legalize and tax cannabis receive tax revenues that may then go toward combating the illicit market. These enforcement actions increase costs for illegal market participants. One might reasonably question whether reducing taxes would have any significant impact on the illicit market given whole swathes of the state do not engage in the legal cannabis system, a problem that this bill does not address.

Moreover, the wide authority of local jurisdictions to enact taxes on cannabis has resulted in compounding taxes. A compounding tax is one in which the underlying taxable amount includes amounts of taxes levied elsewhere in the supply chain. In other words, Prop. 64 allowed locals to apply a tax on a tax, a principle that generally counters sound tax policy. This, however, was authorized by Prop. 64 and was ostensibly a factor in garnering approval

of the initiative in areas of the state that generally opposed legalization of cannabis. Thus, lowering the tax rate at the state level still does not alleviate the fundamental issue of the compounding taxation authorized in Prop. 64.

- 4) *Bearing the burden:* Prop. 64 prescribed that two types of taxes be imposed on cannabis as opponents note. When the Legislature modified the imposition of cannabis taxes, it effectively cut the taxes of the cannabis industry and backfilled these losses with other revenues. The Legislature required that the percentage rate increase to the cannabis excise tax that occurred in July of this year must be sufficient to cover the lost revenue from the suspension of the cultivation tax, and limited the cumulative rate to no more than 19%. Absent this maximum rate restriction, the rate would have increased to approximately 19.6% to fully compensate for lost cultivation tax revenues. Losses resulting from reductions in cannabis taxes generally cause reductions in funding to childcare, environmental, tribal resource, and law enforcement programs; these entities likely bear the majority, if not the entirety, of the loss.

According to the Author

In 2024, active cannabis licenses decreased by 18% and retail sales value decreased by 4.4%, all while the illicit market retained its stronghold over consumers seeking more economic options. California's cannabis industry is in dire economic straits, with sales revenues declining since 2021 and many licensees shutting their doors or on the verge of closure[.] Only 40% of cannabis consumed in California comes from the legally licensed marketplace according to the [Department of Cannabis Control] (DCC). Consumer demand for cannabis is highly elastic depending on price. California has just half the cannabis sales per capita of other states with lower taxes (Oregon, Michigan, Missouri). If California were on par in per capita sales with states like Michigan, it would be generating \$13 billion in annual sales, and the state would be collecting substantially more tax revenue. Preventing a tax increase will keep the legal market from becoming even less competitive with illegal legacy marketers and prevent further closures and bankruptcies in the legal industry.

Arguments in Support

The California Cannabis Industry Association, writing in support of this bill, states, in part:

Since legalization, California's cannabis industry has created hundreds of thousands of jobs, from farming to retail sales, and is a major industry for entire regions of the state. But the cannabis industry in California has been deeply impacted by a history of high taxation, leaving room for the illegal market to thrive while small business owners and operators struggle to stay alive. At the same time, states like Michigan have seen significant growth in their industries due to lower taxes and friendlier policies.

Just last year, Michigan surpassed the once-dominant California cannabis market, outperforming California's sales by seven million units and over \$200 more in per capita sales. If California were on par in per capita sales with Michigan, it would be generating \$13 billion in annual sales, and the state would be collecting substantially more tax revenue. Instead, the taxable sales for cannabis in 2024 was just \$4.6 billion – far short of its potential.

Taxes as high as 45% in some areas of California have suffocated California's infant legal cannabis industry before it had a chance to develop into a strong, sustainable economy and culture. The legal cannabis industry needs a lifeline to ensure that the industry is able to survive and support hundreds of thousands of workers. Allowing the legal cannabis industry

to regain its foothold is a simple way to bring more revenue to our economy and combat the illegal market.

Arguments in Opposition

A coalition of childcare, tribal, and environmental advocates, writing in opposition to this bill, states, in part:

When voters approved Proposition 64, they were explicitly promised that hundreds of millions of dollars annually of Cannabis Excise Tax and Cultivation Tax revenues would be permanently dedicated for the Tier 3 programs, to protect children, youth and the environment. This revenue is a significant funding source for childcare for low-income families, youth substance use prevention programs, environmental remediation including restoration of watersheds damaged by cannabis cultivation, and law enforcement programs.

Many of our organizations refrained from opposing the 2022 cultivation tax only because an agreement was reached, and it was clearly required in law under AB 195, that a compensatory adjustment of the excise tax of up to 19% to maintain revenue neutrality would be implemented this year. Even with that adjustment it is unclear if it will fully compensate the loss of the cultivation tax [...] If the Legislature fails to uphold the promise made in AB 195, in our estimate, between \$145 to 182 million dollars annually for Tier 3 childcare, youth, environmental, and law enforcement program or other needed investments would be lost.

FISCAL COMMENTS

According to the Senate Committee on Appropriations the CDTFA indicates that this bill would result in reduced cannabis excise revenues of \$135 million in 2025-26, and \$180 million in 2027-28 (Cannabis Tax Fund). Additionally, the estimated sales and use tax revenue loss for 2025-26 would be \$11.7 million, \$5.2 million of which would come from the General Fund.

Furthermore, the estimated sales and use tax revenue loss for 2027-28 would be \$13.3 million, \$6.6 million of which would come from the General Fund. The department would incur administrative costs of \$145,000 in 2025-26 and \$4,000 in 2026-27 to implement the provisions of the bill (Cannabis Tax Fund).

VOTES:

ASM BUSINESS AND PROFESSIONS: 14-0-4

YES: Berman, Flora, Ahrens, Alanis, Bauer-Kahan, Caloza, Chen, Elhawary, Haney, Krell, Lowenthal, Macedo, Nguyen, Pellerin

ABS, ABST OR NV: Bains, Hadwick, Irwin, Jackson

ASM REVENUE AND TAXATION: 6-0-1

YES: Gipson, Carrillo, DeMaio, Garcia, McKinnor, Quirk-Silva

ABS, ABST OR NV: Ta

ASM APPROPRIATIONS: 13-0-2

YES: Wicks, Arambula, Calderon, Caloza, Dixon, Elhawary, Fong, Mark González, Hart, Pacheco, Pellerin, Solache, Tangipa

ABS, ABST OR NV: Sanchez, Ta

ASSEMBLY FLOOR: 74-0-5

YES: Addis, Aguiar-Curry, Ahrens, Alanis, Alvarez, Arambula, Ávila Farías, Bauer-Kahan, Bennett, Berman, Boerner, Bonta, Bryan, Calderon, Caloza, Carrillo, Castillo, Chen, Connolly, Davies, DeMaio, Dixon, Elhawary, Ellis, Flora, Fong, Gabriel, Gallagher, Garcia, Gipson, Jeff Gonzalez, Mark González, Haney, Harabedian, Hart, Hoover, Jackson, Kalra, Krell, Lackey, Lee, Lowenthal, Macedo, McKinnor, Muratsuchi, Nguyen, Ortega, Pacheco, Papan, Patel, Patterson, Pellerin, Petrie-Norris, Quirk-Silva, Ramos, Ransom, Michelle Rodriguez, Rogers, Blanca Rubio, Sanchez, Schiavo, Schultz, Sharp-Collins, Solache, Soria, Stefani, Tangipa, Valencia, Wallis, Ward, Wicks, Wilson, Zbur, Rivas

ABS, ABST OR NV: Bains, Hadwick, Irwin, Celeste Rodriguez, Ta

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