Origins Council is a California nonprofit education, research and policy advocacy organization dedicated to sustainable rural economic development within cannabis producing regions, and establishing nationally and internationally recognized, legally defensible, standards-based, geographic indication systems for cannabis.

OC Report: The Rural Land Use Trap
Microbusinesses, Direct Sales, and the Future of Craft Cannabis

March 7th, 2024

Introduction

From the inception of the campaign for Proposition 64 in 2015, a significant amount of conversation has focused on policies to support small, craft operators within the California cannabis market. When Proposition 64 was presented to the voting public, it included mechanisms purported to protect California's historic medical cannabis cultivation communities and their consumers in transitioning into the regulated system.

Today, these discussions remain a pressing concern for those interested in building a diverse and successful regulated cannabis market. While the legal cannabis framework has brought many challenges for small producers, approximately 2,000 small and independent craft cultivators remain within the legal California market today.

Over the past several years, however, small producers have begun dropping out of the regulated framework at an alarming rate, illustrating the pressing need to re-evaluate the mechanisms

established by Proposition 64 to support small-scale cultivators, and to determine the policy reforms that will have the greatest substantive impact for California's craft producers.

One primary mechanism proposed within Proposition 64 to benefit small cultivators was the "microbusiness" license, which authorizes at least three - and up to four - different commercial cannabis activities under a single state license. The activities that can be authorized under a microbusiness license are: 1) outdoor, mixed-light, or indoor cultivation up to 10,000 square feet; 2) manufacturing, 3) distribution; and 4) retail.

In its inception, the microbusiness license was often compared to a "craft brewery,"[1] and was framed as a specific benefit for small, rural, and legacy cultivators. Almost eight years following the passage of Proposition 64, however, the microbusiness license has not lived up to these expectations, and has provided few benefits to small, rural cultivators.

This report seeks to explain why, and what can be done about it.

Executive Summary: Findings and Recommendations

In summary, we offer the following findings regarding the microbusiness license and barriers to on-farm vertical integration for small farmers:

First, the existing state microbusiness license is not operating as an effective or even useful tool for the small, rural operators it was theoretically intended to support. A review of state licensing data shows that many of the businesses that hold microbusiness licenses are large; many do not cultivate at all; nearly all are based in urban areas; and almost none are small, rural, outdoor cultivators.

Second, what has sometimes been framed as "barriers to microbusiness licensure" for small, rural operators is better understood as barriers to the underlying manufacturing, distribution, and retail uses that would be authorized under a microbusiness license. In order to obtain a microbusiness license, an operator must comply with all of the state and local regulations underlying each of the activities authorized under a microbusiness license: a task which, even when technically possible for small farmers, is expensive and complex. The real barrier to microbusiness licensure, then, is in receiving state and local approval for these underlying uses, not in obtaining the "microbusiness license" itself.

Third, addressing the barriers to underlying manufacturing, distribution, and retail uses in rural areas is heavily complicated by rural land use constraints, CEQA requirements, state regulatory

[1] https://lostcoastoutpost.com/2016/aug/9/high-powered-sacramento-lobbyist-dropped-tell-us-a/

barriers, building and fire code standards, road standards, ADA requirements and lack of capital access for small cultivators. While these barriers can be addressed incrementally and on a piecemeal basis, no single policy reform - or even set of policy reforms - is likely to lead to a situation where most rural cultivators will be able to reliably access microbusiness licensure.

Based on these findings, we offer the following policy recommendations:

First, policymakers should meaningfully support the greatest number of small cultivators by pursuing policy solutions that disentangle small cultivator entitlements from rural land use barriers. AB 1111, legislation introduced by Assembly Pellerin in 2023 and sponsored by Origins Council to allow small producer sales at cannabis events, is a vetted and politically-viable solution which can be implemented in *this legislative session* to provide the greatest benefit to the greatest number of small farmers.

Second, the Department of Cannabis Control can immediately facilitate microbusiness licensure and on-farm vertical integration, without further statutory action, by implementing regulatory reforms that remove barriers to the underlying manufacturing, distribution, and retail activities that most affect small, rural farmers. While these reforms in themselves are not a silver bullet solution to enabling microbusiness licensure for small farmers, they can serve as an incremental step that, combined with additional action at the local level, can increase and sustain the relative viability of on-farm vertical integration over time.

Third, policymakers can increase flexibility for small farmers seeking to vertically integrate by implementing policy recommendation 1.2 from a recent Cannabis Policy Lab Report for licensing simplification,[2] which recommends that the state should issue one license per *location* for cannabis activities, rather than one license per commercial cannabis *activity*, and that a single cannabis license should be able to encompass multiple activities. This approach would directly address the primary conceptual confusion underlying the microbusiness approach by focusing the conversation on the relevant underlying licensed activities, and would grant cultivators the maximal amount of flexibility to obtain authorization for one, two, three, or more licensed cannabis activities appropriate for their site.

Fourth, policymakers can help accomplish the goals of microbusiness licensure and on-farm vertical integration by implementing broader changes to the commercial cannabis licensing framework, including reduced licensing fees for small cultivators and implementing policies that support increased access to retail, reduced taxation, and reduced barriers to operation.

Finally, given that microbusiness licenses are overwhelmingly not held by small, rural farmers, we believe that any proposed policy reform that would provide *exclusive* benefits to

[2] https://drive.google.com/file/d/1ZiRJcwrHVhdAFm5ZcVPcu0EGsmUr3VW_/view

microbusiness licensees should be avoided. Instead, policies designed to support small farmers should be broadly available to small farmers, regardless of whether they're vertically integrated.

Below, we enumerate the statutory, regulatory, local, state, and financial barriers to microbusiness licensure and on-farm vertical integration for small, rural farmers.

Findings: Barriers to Microbusiness Licensure for Small, Rural Farmers

1. Microbusinesses are not inherently, or even typically, small businesses.

Despite their name, nothing in California's regulatory structure requires microbusinesses to be small businesses. California law enables any business of any size to obtain a microbusiness license, so long as the licensee isn't cultivating more than 10,000 square feet at the site of their microbusiness license. A business can engage in unlimited on-site manufacturing, distribution, or retail, or hold hundreds of acres of cultivation at a different premises, and still hold a microbusiness license.

Rather than small business licenses, microbusinesses are better understood as *vertically integrated licenses*. By their nature, these vertically integrated operations tend to be larger and more highly-capitalized than the average business which is not vertically integrated.

In fact, microbusiness licensees aren't required to engage in cultivation at all. A large urban business engaged in distribution, manufacturing, and retail may - and often will - obtain a microbusiness license.[3] For microbusiness licensees who do cultivate, the 10,000 square foot cap on cultivation area per premises - which is the same regardless of the production method used by the cultivator - advantages indoor cultivators over homestead outdoor cultivators, given indoor cultivation achieves 5x or more productivity per square foot in comparison to outdoor cultivation.

Examples of large or very large companies that hold microbusiness licenses in California include Caliva (C12-0000216-LIC) - one of the largest cannabis businesses in California, which in 2019 raised $75 million in a funding round that included investments by Joe Montana[4] - and multi-state cannabis operator and international brand Cookies (C12-0000233-LIC), which claims to be the world's first legal cannabis brand worth $1 billion.[5]

[3] According to DCC licensing information on microbusinesses requested by PRA in February 2024, 144 of 406 state-licensed microbusinesses (35%) are not authorized for cultivation.
[4] https://www.businessinsider.com/caliva-raises-75-million-backed-by-joe-montana-and-carol-bartz-2019-1
[5] https://www.businessinsider.com/the-story-of-cookies-weed-brand-and-berner-2022-6

2. Microbusiness licenses are overwhelmingly held by urban, not rural, operators.

A review of DCC licensing data shows that regions with large numbers of outdoor cultivators hold very few microbusiness licenses, while urban jurisdictions with a high proportion of indoor cultivators hold a much greater concentration of microbusiness licenses. Among the 406 active microbusiness licenses held statewide, nearly all are held by businesses located in urban areas.

	# of independent cultivators	**% of cultivators with outdoor or mixed-light 1 license**	**# of microbusiness licenses**
Predominantly Rural Counties			
Humboldt	728	92%	27
Mendocino	452	94%	10
Trinity	312	91%	3
Nevada	149	92%	1
Predominantly Urban Counties			
Los Angeles	313	1%	110
Sacramento	86	0%	19
Riverside	81	11%	66
Alameda	74	0%	63

In total, the four rural counties with the greatest concentration of small, outdoor cultivators - Humboldt, Mendocino, Trinity, and Nevada - hold 1,641 cultivation licenses, but just 41 microbusiness licenses. By comparison, the single county of Alameda, which has no licensed outdoor cultivators and only 74 indoor cultivators, is home to 63 microbusiness licenses.

In rural counties such as Humboldt where there are relatively larger numbers of microbusiness licenses (27), these licenses are overwhelmingly held in industrially or commercially-zoned areas in larger incorporated towns such as Arcata and Eureka. These businesses typically operate principally as cannabis distributors, and have obtained microbusiness licenses in order to vertically integrate into other, secondary activities such as manufacturing and retail delivery.

3. The high barriers to obtaining microbusiness licenses in rural areas reflect the high barriers to obtaining licenses for the underlying manufacturing, distribution, and retail activities.

All microbusiness licenses are required to obtain state and local authorization for the underlying cannabis activities authorized under the license. DCC regulations under §15500(a) require that a microbusiness licensee *must* engage in at least three different commercial cannabis activities, inclusive of cultivation, manufacturing, distribution, and retail sale, in order to obtain a microbusiness license.

> *"In order to hold a microbusiness license, a licensee must engage in at least three (3) of the following commercial cannabis activities: cultivation, manufacturing, distribution, and retail sale. License types created by the Department in regulation shall not be considered qualifying commercial cannabis activities for purposes of obtaining a microbusiness license, except for the Type N manufacturing license and the distributor transport only license."*

Subsections (e), (f), (g), and (i) of §15500 then require that a microbusiness licensee must follow all state regulations and procedures that would be applicable if they applied for a license for any of these underlying activities independently. At the local level, the same constraints apply: to obtain local authorization for a microbusiness license, the permittee must have local land use approval for each of the underlying activities authorized under the microbusiness license.

The barriers to obtaining a microbusiness license, then, are effectively identical to the barriers to obtain the underlying licenses for manufacturing, distribution, or retail activity.

In forums such as the state's Cannabis Advisory Committee, discussion has often focused on how to make access to microbusiness easier for small and rural businesses. For the above reasons, however, this question misses the point. The relevant question is not how to make microbusiness licensure easier, or even more highly incentivized, but rather how to address barriers to licensing for the *underlying activities* of manufacturing, distribution, and retail.

If underlying barriers to (for example) distribution licensure were addressed, a small rural farmer could choose to apply for a license either for distribution, or for a microbusiness that includes distribution as an authorized use: the difference, in practice, is likely to be relatively minor. A narrow focus on microbusinesses, then, misses the larger context of how the licensing framework as a whole either enables or restricts small, rural operators from obtaining licensure for various commercial cannabis activities.

4. The microbusiness license is incompatible with rural land use constraints for most rural operators.

The lack of microbusiness adoption in rural areas is primarily due to structural factors associated with rural land use. Rural land use constraints, CEQA requirements, state regulatory barriers, building and fire code standards, road standards, and ADA requirements make the microbusiness license - even in a best-case scenario with improved regulations - an extremely limited tool for most small rural farmers.

It's critical to note that the significant majority of the nearly 2,000 small outdoor cannabis farmers in California are not just rural; they are *remote*, and are often located many miles from services or high-quality paved roads, as well as many hours away from California's large urban centers.

In this sense, the analogy between the microbusiness license and "craft breweries" is instructive. Just as craft breweries are typically located in industrially and commercially-zoned areas in urban areas, microbusiness licenses have overwhelmingly been located in the same types of areas, for the same reasons.

One Mendocino County cultivator explains the building code, ADA, and financial barriers to obtaining a microbusiness license:

> *"In terms of obtaining a microbusiness license in Mendocino County with a cultivation licensing on the same premise there are some major obstacles to overcome.*
>
> *The first obstacle that comes to mind is the extreme red tape and permitting costs for commercial facilities. As of the first week of February 2024 permitting fees were drastically increased on just about every category from building and planning. Having a facility with employees that commercially operate non-cultivation businesses such as manufacturing, processing, or distribution requires a commercial structure that is ADA compliant. To build such structures in rural type areas is very cost prohibitive especially with large permitting fees and additional engineering plans (usually required for ADA designs).*
>
> *Besides the building of structures, the zoning may not allow for certain commercial activities in many areas where cultivation occurs, or at the very least, a major use permit may be required which has increased in application price from $5k to $10k recently, in addition to being a very arduous process. It may be difficult to meet the security requirements by the state for a micro-license due to insufficient electricity or internet availability at many Mendo cultivation locations.*

The economical difficulties to compete against businesses in better zoning/location and that specialize in a particular license activity (manufacturing, distro, retail, ect) and do not cultivate is a major barrier to overcome. Those non-cultivation license types are in heavy competition currently and it would appear to be extremely difficult to enter into that competition with the previously mentioned obstacles. The ROI is just not there for most cultivation sites in Mendocino County that are usually on RL, AG, or some other rural zoning."

Humboldt cultivators face similar barriers. Humboldt's cannabis ordinances allow on-farm vertical integration only in limited zoning districts, and prohibit these activities in FP and TPZ zones where many legacy cultivators are based (Humboldt County Code 55.4.10.3). These uses are also required to meet Category 4 road standards, or provide an engineer's report confirming the functional capacity of the road to accommodate the proposed activity (Humboldt County Code 55.4.7.3). These road standards are either expensive or not possible to meet in many cases. As in Mendocino County, buildings used in association with these activities are further required to meet expensive commercial building code requirements and ADA standards.

Humboldt cultivators are governed under two different and related local ordinances. "Ordinance 1.0," passed in 2016, was written primarily to transition pre-existing legacy cultivators into the legal market, while "Ordinance 2.0," passed in 2018, was written to govern new cultivation and expansion of activities by existing cultivators.

To comply with CEQA obligations under Humboldt's EIR for Ordinance 2.0, pre-existing legacy cultivators who propose any new development activities are required to comply with a variety of biological resource protection measures that frequently require additional studies performed by subject-matter experts, and which may require additional measures for compliance.

55.4.12.1.10 Performance Standard – Biological Resource Protections

Projects proposing new development activities shall provide the necessary information to implement the following mitigation measures from the Final Environmental Impact Report:

Mitigation Measure #	Description of Mitigation
3.4-1a	Biological reconnaissance surveys
3.4-1b	Special-status amphibian surveys and relocation/buffers
3.4-1c	Western pond turtle surveys and relocation/buffers
3.4-1d	Nesting raptor surveys and relocation/buffers
3.4-1e	Northern Spotted owl surveys
3.4-1f	Special-status nesting bird surveys/buffers
3.4-1g	Marbled murrelet habitat suitability surveys/buffers
3.4-1i	American badger surveys and buffers
3.4-1j	Fisher and Humboldt marten surveys and den site preservation/buffers
3.4-1k	Bat survey and Buffers
3.4-1l	Vole survey and relocation/buffers
3.4-3a	Special-status plants surveys
3.4-4	Protection of sensitive natural communities, riparian habitat, wetland vegetation
3.4-5	Waters of the United States
3.4-6b	Retention of Fisher and Humboldt marten habitat features

Any uses that involve “public accommodation” on cannabis farms, such as tourism or on-farm sales, must meet additional standards under Humboldt’s ordinance (Humboldt County Code 55.4.12.14). These include additional special permit requirements, road and driveway standards, parking requirements, and a requirement for ADA-compliant bathrooms.

In Nevada County, local officials have made authorization for on-farm vertical integration and microbusinesses a priority, including by amending the county’s EIR to include these uses in agriculture and forestry zones approved for cultivation. While these local ordinance amendments have removed some barriers to on-farm vertical integration, many Nevada County farmers still face similar barriers to cultivators in Humboldt and Mendocino counties. All accessory structures used for commercial cannabis, except for storage, must comply with F1 commercial building code standards, including Title 24. All commercial cannabis farms utilizing a building for manufacturing, distribution or retail sales must comply with extensive commercial fire code regulations; and commercial buildings with employees must comply with ADA standards. To date, one on-farm microbusiness with retail is currently moving through Nevada County’s local permitting and state approval process. There are two microbusinesses without retail that are currently in the local and state approval process.

In Trinity County, three microbusinesses have received state licenses; however, none of them are currently functioning with all of their state-approved activities due to incomplete local approvals. In addition to facing similar barriers as other counties, Trinity microbusiness hopefuls have faced additional barriers due to a refusal by local fire chiefs to complete the necessary review for permits to be approved. One microbusiness licensee has invested over $1 million while being unable to operate due to lack of sign-offs. Additionally, many Trinity cultivators are now dropping their distribution-transport only state licenses - the most accessible ancillary activity which can be included in a microbusiness - due to an inability to afford state regulatory requirements on insurance and vehicles.

In Big Sur, multiple generations of cannabis farmers are credited for their contributions to higher standards, best practices, and unique cultivars. Upon adoption of Proposition 64 in Monterey County, however, the Big Sur community was prohibited from participation. In response, the community of Big Sur cannabis farmers organized to legalize cannabis cultivation in the region and approached the California Coastal Commision to ask for their help on the grounds of historic and economic preservation. The CCC agreed and ordered Monterey County to work with Big Sur farmers.

Two years later, an ordinance was passed that theoretically enabled Big Sur farmers to become legal; however, it included over fifty individual requirements to satisfy eleven different agencies, resulting in insurmountable costs of hundreds of thousands of dollars to become legal. To this day, permitting cultivation of seven plants in Big Sur costs roughly the same to permit as a large greenhouse in Salinas. Discretionary land use permitting and CEQA requirements are by far the

most limiting, and often farmers are forced to develop beyond their needs to meet industrial agricultural standards.

Given the incredibly high barriers that Big Sur farmers have faced to licensing their small-scale cannabis cultivation, the notion of adding additional permitted activities on-farm is well beyond the reality of the current situation. Throughout Monterey County, only one microbusiness license has been approved, in an industrial area in the city of Greenfield. This licensee was recently approved to expand their indoor cultivation to 34,000 square feet,[6] and even prior to this expansion was large enough to remit over $130,000 per year in local cannabis taxes to the city.[7]

Similarly, small and rural cultivators in Santa Cruz County have faced substantial barriers to operating simply as cultivators; much less vertically integrating into other activities. Most rural parcels (including those zoned A, RA, SU, and TP) are limited in the allowed cannabis activities, and parcels located in allowable zones are further restricted by large setback requirements and acreage minimums. Obtaining a use permit from the planning department for any project not located on a CA-zoned parcel could cost hundreds of thousands of dollars and take over a year to complete.

As in other counties, F1 commercial building code requirements in Santa Cruz County create substantial barriers to on-farm vertical integration. Most rural parcels lack the road width, building specification, and water storage capacity required under this designation. And politically, the county and all municipalities within the county have numerical caps in place for retail licenses; and attempts to add new retail opportunities, including for microbusinesses, have been opposed by established retail license holders.

The net result is that four of five microbusiness licenses in Santa Cruz County are held in urban areas in either Santa Cruz or Soquel, with only one microbusiness license issued on a rural parcel in the county.

Overlaying all of this, is the blanket Statewide mandate for site-specific CEQA review and certification of every commercial cannabis project licensed by the Department of Cannabis Control. It is important to note that California has applied CEQA to commercial cannabis activities in an anomalous way, compared to how CEQA is applied to non-cannabis commercial activities, especially when contrasted with other commercial agriculture.[8] This approach undermines the ability of local jurisdictions to avail themselves of various land use regulation tools for commercial cannabis activities, such as ministerial permitting or use by right under existing general plans and zoning codes for similar commercial activities. It also subjects licensed farms to far greater thresholds of compliance, as well as increased costs and timelines,

[6] https://www.ksbw.com/article/cannabis-industry-growing-in-city-of-greenfield/45348046
[7] https://ci.greenfield.ca.us/DocumentCenter/View/3593/PC-Agenda-Packet-120523?bidId=
[8] https://drive.google.com/file/d/1JSxt-znZZw0JcDNv38BkPcMN8-3axwDc/view?usp=sharing

in order to qualify for additional on-site distribution, manufacturing and retail activities, if those activities are even authorized in their zoning district and parcel size to begin with.

In summary, the local land use barriers associated with permitting non-cultivation activities on rural cultivation sites create a situation where on-farm vertical integration is either expensive, or not possible at all, for most farmers. While local policy can mitigate these barriers, it cannot eliminate them entirely; and even under a best-case scenario, on-farm vertical integration is likely to be expensive and challenging for the significant majority of small rural farmers.

5. State regulatory requirements for underlying manufacturing, distribution, retail, and other activities create further barriers to microbusiness licensure and on-farm vertical integration in rural areas.

In addition to local land use barriers, Department of Cannabis Control regulations establish additional barriers to on-farm vertical integration by rural operators.

In Origins Council's April 19, 2022 comments on proposed DCC rulemaking[9], we provided extensive comment on barriers to on-farm vertical integration and microbusiness licensure beginning on page 21. These recommendations were not adopted in the subsequent rulemaking and are reprinted below; they remain relevant today. Relevant barriers encompass both the microbusiness license itself, and the underlying activities that would comprise a microbusiness license.

Recommendations included in Origins Council's April 2022 comments include:

- Exempt all areas of a microbusiness premises from video surveillance, lock, and alarm requirements in §15044, §15046, and §15047, if the premises is located on the same site as an outdoor or mixed-light 1 cultivation license. Apply the same exemption to manufacturing, distribution, or retail licenses located on the same site as an outdoor or mixed-light 1 cultivation license. Since the inception of the regulated cannabis framework, state regulators have exempted cannabis cultivators from the video surveillance, lock, and alarm requirements applicable to all other license types.

  The DCC provided this exemption out of a recognition that extensive security requirements are impractical in remote rural areas, stating in their Initial Statement of Reasons that: *"The Department has determined that requiring the same level of video surveillance for cultivation locations that may be very large, outdoors, and located in rural areas where it may be difficult to access internet or electricity, would be unreasonably onerous and in some cases not possible."*

[9] https://drive.google.com/file/d/1JDlogddddcinQkKjQmvhBWZ4KMMJSRLw/view

Because the security exemptions applied to rural cultivators are not applied to microbusiness license-holders, however - or applicants for manufacturing, distribution, or retail licenses on a rural farm - these impractical security restrictions become applicable as soon as a rural cultivator seeks to vertically integrate on-farm, and are either expensive or impossible to comply with for many farmers.

- Don't require a wall to separate non-storefront retail areas from the non-retail areas of a microbusiness - §15500(j) in DCC regulation requires a wall to separate retail and non-retail areas of a microbusiness premises for both storefront and delivery-only retail. For a microbusiness located on a homestead farm, this section may require the construction of an unnecessary wall, and in some cases may render microbusiness licensure impractical.

- Establish tiered licensing fees based on size for nursery and processing licenses - while not directly relevant to microbusiness licensure, this regulatory restriction is applicable to other attempts to vertically integrate on a farm. All nursery licenses currently pay an annual $4,685 licensing fee regardless of size, and all processing licenses currently pay $9,370 regardless of size. This is distinct from cultivation licenses, which pay tiered annual licensing fees based on size, and non-cultivation licenses, which pay tiered annual licensing fees based on gross annual revenue. The lack of fee tiering for cultivation-adjacent licenses creates an ironic situation where small cultivators - and only small cultivators - are denied access to affordable licensure in ways that do not affect any other license type.

- Establish tiered or waived insurance requirements for small distributors and transport-only self-distributors - §15308 in DCC regulation currently requires all distributor licensees, regardless of type or size, to carry at least $2,000,000 in general liability insurance. This includes transport-only self-distribution licensees, who are generally carrying nominal amounts of product, and who are definitionally limited only to carrying their own products. Insurance requirements for these licensees are not necessary and constitute a significant barrier to licensure. Many cultivators, in fact, are now dropping their transport-only licenses due to the expense associated with insurance requirements.

- Remove or amend premises requirements for distribution transport-only licenses - for small cultivators, transport-only licenses are necessary for a variety of critical tasks which are not practical or appropriate to handle through a third-party distributor. Many cultivators, however, have struggled with state land-use and building requirements for transport-only licenses. Since the transportation-only license has no land use impact and does not authorize cannabis storage, it should be clarified that the license does not have

any state land use requirements other than the requirement to have a premises of some sort to provide for records storage of the shipping manifests. If the DCC believes this solution is not possible under current statute, an alternative would be to remove the requirements for a transport-only premises to be "permanently affixed to the ground" and not located in a residence, which would establish more flexibility for a small, separate premises to be designated for recordkeeping only, such as a locked drawer with a fixed location.

It should be noted that the above regulatory recommendations are not an exhaustive list of the state DCC regulations that rural cultivators would be required to follow to obtain authorization for these activities; they are limited to those regulations which we believe are clearly not applicable or appropriate for small rural cultivators. Even under a scenario where these recommendations are adopted, rural cultivators would be required to follow all of the (often expensive) state regulatory requirements applicable to any other manufacturer, distributor, or retailer.

6. Microbusiness licenses may offer some benefits to rural farmers in comparison to applying for multiple underlying licenses independently, but these benefits are limited and circumstantial.

Given the barriers identified in the above analysis, it's worth asking an additional question: if microbusiness licenses trigger the same barriers to licensure as applying for the underlying licenses independently, are there benefits unique to microbusiness licenses which should incentivize farmers to apply for a microbusiness license, rather than multiple underlying licenses?

6a. Microbusinesses do not provide exclusive access to vertical integration.

It's important to note that, despite occasional claims to the contrary, microbusinesses do *not* provide exclusive access to vertical integration. California law allows all licensees to fully vertically integrate, with one exception: a person who holds financial interest in a "large" cultivation license cannot also hold a license for distribution.[10] However, the utility of this restriction has been undermined by the common practice of "license-stacking," where larger cultivators hold multiple - sometimes even dozens - of "small" or "medium" cultivation licenses rather than a single "large" cultivation license. As a result, as a practical matter, all California licensees are legally permitted to vertically integrate.

6b. Microbusinesses may offer administrative benefits compared with obtaining multiple licenses.

[10] DCC regulations, §16300.1

Microbusiness licensure does offer some potential administrative benefits in relation to applying for multiple separate licenses. Administratively, a microbusiness licensee is required to manage only one license, which renews annually, rather than multiple separate license renewals throughout the year. A single premises map underlying a microbusiness license may be easier to create and have approved than multiple different premises maps, and there may be administrative benefits to managing a single license in the METRC system.

6c. Microbusinesses may offer financial benefits compared with obtaining multiple licenses, but these benefits are circumstantial and do not apply to all applicants.

Because annual DCC licensing fees are calculated differently for a microbusiness license than for licenses for underlying activities, there may also be financial benefits to consolidating multiple licenses into a single microbusiness. Whether there is a financial benefit, however, depends on 1) which specific activities a licensee is applying for, and 2) what their anticipated annual gross revenue is.

The lowest annual licensing fee for a microbusiness is $5,000 per year, applicable to microbusinesses with under $1 million in annual gross revenue. This licensing fee can be compared to annual fees for the underlying activities, as follows:

License	**Annual Fee**
Cultivation - 2,500 square foot outdoor	$1,205
Cultivation - 5,000 square foot outdoor	$2,410
Cultivation - 10,000 square foot outdoor	$4,820
Cultivation - 10,000 square foot indoor	$35,410
Manufacturing - under $100,000 gross revenue	$2,000
Distribution - under $1 million gross revenue	$1,500
Self-distribution transport-only - under $1,000 gross revenue	$200
Retail - under $500,000 gross revenue	$2,500

For the smallest possible microbusiness operator - cultivating less than 2,500 square feet outdoors, and engaging in small-scale manufacturing and self-distribution - the annual licensing fee for a microbusiness would be $5,000, compared with a total licensing fee of $3,405 to hold

three licenses independently. In this case, holding a microbusiness license would be more expensive than holding the underlying licenses separately.

A relatively larger outdoor farmer, however, would likely save money under a microbusiness license. A 10,000 square foot outdoor farmer also engaged in small-scale manufacturing and self-distribution would pay $7,020 for these licenses separately, and can save about 30% on their licensing fees by consolidating into a microbusiness.[11]

A larger indoor cultivator may see greater financial benefits from microbusiness licensure, depending on what other activities they're licensed for and their annual gross revenue. A 10,000 square foot indoor cultivator who's also engaged in small-scale manufacturing and distribution would pay $38,910 for these separate licenses. Because indoor cultivation produces significantly higher yields than outdoor cultivation on the same scale, this licensee is likely grossing considerably more than an outdoor farmer - perhaps $2-4 million annually. Whether they would save money with a microbusiness, then, depends on where they fall within this range.

If the licensee is grossing between $2-3 million, their license fee would be cut almost in half, to $20,000. If they're grossing between $3-4 million, their microbusiness license fee would be $32,000, and they would still save considerably. If their gross revenue exceeds $4 million, however, their microbusiness license fee would be $45,000, and they may save money by applying for licenses separately.

In summary, microbusiness licensure may offer some administrative and financial benefits in comparison to holding separate licenses for the underlying activities, but these benefits are likely to be limited and for most licensees, and particularly for small, rural cultivators.

In the recommendations section below, we offer options for alternative policy approaches that can capture the hoped-for benefits of the microbusiness license, but which are more consistent with the on-the-ground realities of rural land use.

Recommendations: Addressing Barriers to On-Farm Vertical Integration and Microbusiness Licensure for Small, Rural Farmers

As discussed in the findings above, challenges with microbusiness licensure and on-farm vertical integration include the following:

[11] A licensee of this size almost certainly makes well under $1,000,000 in gross revenue, and therefore would pay the lowest-tier $5,000 microbusiness annual licensing fee.

- The structure of the state microbusiness license has led to a situation where many or most existing microbusiness holders are 1) not small businesses, 2) not cultivators, and 3) not rural operators.

- Rural land use constraints, CEQA requirements, building and fire code standards, road standards, and ADA requirements make the microbusiness license an extremely limited tool for most small rural farmers. Similar challenges apply to other forms of on-farm vertical integration. Rural land use policy changes can incrementally address, but not fully resolve, these barriers.

- State DCC regulations include other barriers which constrain on-farm vertical integration and microbusiness licensure.

- Even under a best-case scenario with improved state and local regulations, microbusiness licensure and on-farm vertical integration are inherently expensive and complex activities that require capital expenditure which is often not available to many small farmers.

Given these challenges, we offer the following policy recommendations:

1. Decouple small cultivator entitlements from rural land use barriers by passing AB 1111 in the 2024 legislative session.

Given the challenges associated with development on rural lands, representative organizations of small cannabis farmers in California have long advocated for policies that support small cultivators without triggering rural land use considerations.

First and foremost among these policies is the ability for small cultivators to sell their own products directly to consumers at state and locally-authorized cannabis events. A regulatory framework for these events already exists at the state and local level; however, cultivators are currently prohibited from selling their products at these events unless they also hold a retail license.

Consequently, representative organizations of small cannabis farmers have introduced legislation to authorize small cultivator sales at cannabis events in the California state legislature dating back to 2018. The current iteration of this legislation is AB 1111, introduced by Asm. Pellerin and sponsored by Origins Council, which would allow small cannabis cultivators under an acre in size to sell their products directly to consumers at a limited number of state and locally-authorized cannabis events annually.[12]

[12] https://leginfo.legislature.ca.gov/faces/billNavClient.xhtml?bill_id=202320240AB1111

Because these events are held off-farm, small cultivators can be authorized to sell at events without triggering the land use barriers associated with on-farm vertical integration. AB 1111 passed through the Assembly by a 74-1 vote in 2023 and currently sits in Senate Appropriations Committee as a two-year bill, where it remains eligible for further consideration in the 2024 legislative session.

AB 1111 is a vetted and politically-viable solution which can be implemented in this legislative session, and would provide broad benefits to small cultivators regardless of their local land use situation. The approach in AB 1111 also enables small cultivators to obtain the benefits of vertical integration at much lower cost than holding a full-time authorization for additional commercial cannabis activities on the farm itself.

2. To facilitate on-farm vertical integration, focus policy efforts on removing state and local barriers to underlying nursery, processing, manufacturing, distribution, and retail activities, rather than removing barriers to the "microbusiness license" itself.

Proposals to improve access to microbusiness licensure have often missed the critical point: for small rural operators, the relevant barriers are to the underlying commercial cannabis activities authorized by a microbusiness, not to the "microbusiness license" itself.

At the local level, county governments can consider policies that reduce barriers to on-farm nursery, processing, manufacturing, distribution, and retail activities that underlie microbusiness licensure, regardless of whether they are applied for separately, or under an umbrella "microbusiness" license. It is critical to remember, however, that in many cases the ability for county governments to address these issues is likely to be constrained by building code, fire code, and CEQA requirements outside their immediate control.

At the state level, as discussed below, the DCC can take steps to improve access to microbusiness licensure by addressing regulatory barriers to the underlying licensed activities. Again, however, expectations for the results of such reforms should be tempered given the many barriers to on-farm vertical integration that will remain in any case.

3. Amend DCC regulations to incorporate Origins Council's April 19, 2022 recommendations for increased access to microbusiness licensure and on-farm vertical integration, including by addressing security and insurance requirements.

The Department of Cannabis Control can immediately facilitate microbusiness licensure and on-farm vertical integration, *without further statutory action*, by implementing regulatory reforms that remove barriers to the underlying manufacturing, distribution, and retail activities

that most affect small, rural farmers. As discussed in greater detail in the prior section, these recommendations include:

- ➔ Exempt all areas of a microbusiness premises from video surveillance, lock, and alarm requirements in §15044, §15046, and §15047, if the premises is located on the same site as an outdoor or mixed-light 1 cultivation license. Apply the same exemption to manufacturing, distribution, or retail licenses located on the same site as an outdoor or mixed-light 1 cultivation license.
- ➔ Don't require a wall to separate non-storefront retail areas from the non-retail areas of a microbusiness.
- ➔ Tier licensing fees based on size for nursery and processing licenses.
- ➔ Tier or waive insurance requirements for small distributors and transport-only self-distributor.
- ➔ Remove or amend premises requirements for distribution transport-only licenses.

4. Implement Cannabis Policy Lab Recommendation 1.2 to issue one state license per location for cannabis activities, rather than one license per commercial cannabis activity.

A recent Cannabis Policy Lab Report on licensing simplification[13] recommends that the state issue one license per *location* for cannabis activities, rather than one license per commercial cannabis *activity*, and that a single cannabis license should be able to encompass multiple activities.

This approach would directly address the primary conceptual confusion underlying the microbusiness approach by focusing the conversation on the relevant underlying licensed activities, and would grant cultivators the maximal amount of flexibility to obtain authorization for one, two, three or more licensed cannabis activities appropriate for their site. This approach would also resolve the confusing and unnecessary existing requirement for a distribution transport-only license to operate out of a separate premises, one of the primary barriers to transport-only licensure among small farmers.

5. Reassess and reduce licensing fees for small cultivators.

As discussed above, reduced licensing fees may be a reason for some cultivators to seek a microbusiness license rather than multiple licenses for separate activities. These benefits are uneven, however, and are likely to be more significant for larger and more urban businesses.

The benefits of reduced licensing fees for microbusinesses could be captured on a broader scale by simply reassessing, and reducing, the licensing fees applicable to small cultivators. Since state

[13] https://drive.google.com/file/d/1ZiRJcwrHVhdAFm5ZcVPcu0EGsmUr3VW_/view

regulators first adopted licensing fees for cultivators in 2017, wholesale prices per pound have dropped by ~66%, but fees have remained the same, making it difficult for many small operators to afford these fees.

The structure of state cultivation licensing fees could also be improved in several ways. Fees could be assessed more proportionally to square footage - for example, allowing a 7,000 square foot farmer to pay proportionally for 7,000 square feet, rather than obtaining a 10,000 square foot permit for a smaller cultivation area. This could mirror the process now created for Type 5 ("large") cultivation licenses, in which cultivators are charged a fixed amount for each additional 2,000 square feet.

Additionally, the fee structure established for Type 5 cultivation licenses beginning on January 1, 2023 has created inequities between fees assessed to smaller and larger cultivators. Currently, Type 5 outdoor licenses are charged $640 for each 2,000 square feet of additional cultivation area, or $3,200 for each 10,000 square feet of additional cultivation area. By contrast, a 10,000 square foot outdoor farmer is charged $4,820 for 10,000 square feet of cultivation area. These fees could be equalized so that small farmers pay the same as Type 5 licenses per square foot of permitted cultivation area.

6. Avoid policy reforms that provide exclusive benefits to microbusiness licensees.

As discussed in this report, microbusiness licenses are currently held overwhelmingly by larger and more urban operations, and this pattern reflects the underlying land use dynamics and capital constraints faced by small, rural cultivators.

For this reason, any policy reform which seeks to provide exclusive benefits to microbusiness license holders would be a severe error if the goal is to benefit small, rural cultivators. Given that most small farmers are not able to obtain this license type, any exclusive benefit granted to microbusinesses would ironically provide disproportionate benefit to larger operators.

Instead, policies that are designed to benefit small farmers should be broadly accessible to small farmers, regardless of whether they choose to vertically integrate; and opportunities for incremental vertical integration, such as obtaining an on-farm distribution license, should be encouraged regardless of whether they're associated with a microbusiness license.

Conclusion: A Path Forward for Craft Cannabis in California

As small operators face increasing challenges to operate successfully within the legal market, it's critical that attempts to improve policy are informed by an objective assessment of legal, regulatory, and market conditions.

Given the inherent and multi-faceted challenges associated with rural land use, we believe there is no silver bullet solution that will result in widespread adoption of microbusiness licenses on small, rural farms in the near future. For this reason, we recommend a longer-term and more measured approach that focuses on removing immediate DCC regulatory barriers to on-farm vertical integration at the state level, while working with county governments to incrementally address land use barriers at the local level.

At the same time, we recommend immediate state action to provide small producers with support that does not trigger the complexities associated with rural land use. AB 1111 is the policy that achieves these goals, and we urge the legislature and administration to prioritize signing this policy into law in 2024.

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