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## Up in Smoke: How AB 374 Can Help Revive the Cannabis Industry

Zachary Byrne

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# Up in Smoke: How AB 374 Can Help Revive the Cannabis Industry

Zachary Byrne\*

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## I. INTRODUCTION

Johnny Casali, owner of Huckleberry Hill Farms in Humboldt County, experiences many of the same problems that other cannabis farms, retailers, and microbusinesses face.<sup>1</sup> Cannabis-related businesses are not making enough to cover their costs.<sup>2</sup> Casali moved to Humboldt County in 1968 with his mother and learned the value of appreciating the land they cultivated.<sup>3</sup> In 1992, at the age of twenty-four, federal agents arrested Casali for growing cannabis and he spent “eight years in federal prison, followed by five years of probation.”<sup>4</sup> Casali returned to his farm with promises of legalization and joined the regulated cannabis industry.<sup>5</sup> The county and state granted full permits to Huckleberry Hill Farms, making it the fourth legacy farm in Humboldt County.<sup>6</sup>

In 2022, Casali sold all of Huckleberry Hill’s product yet still suffered a total loss of \$50,000.<sup>7</sup> A main reason for Casali’s increased losses was a decrease in the price per pound of cannabis.<sup>8</sup> This decrease, farmers allege, is due to consumers choosing to purchase from the illegal market.<sup>9</sup> As a result, a significant supply and demand problem developed, with consumers refusing to purchase cannabis from the legal market.<sup>10</sup> Casali has already seen a strong demand for orders for the 2023 season and is hopeful for a turnaround while still aware of the issues restricting the industry.<sup>11</sup>

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<sup>1</sup> Will Yakowicz, *California’s Cannabis Sales Declined in 2022, The First Time Since Legalization*, FORBES (Feb. 28, 2023), <https://www.forbes.com/sites/willyakowicz/2023/02/28/californias-cannabis-sales-declined-in-2022-the-first-time-since-legalization/?sh=2b8ee1587af9> (on file with the *University of the Pacific Law Review*) (describing how high taxes, a limited number of dispensaries, and strict regulations are harming the cannabis industry); *License Types*, DEP’T OF CANNABIS CONTROL, <https://cannabis.ca.gov/applicants/license-types/#retail-licenses> (last visited May 28, 2023) (on file with the *University of the Pacific Law Review*) (defining microbusiness as a business that does at least three of the following at one location: cultivation, manufacturing, distribution, or retail).

<sup>2</sup> Yakowicz, *supra* note 1 (reporting a total of \$5.3 billion in legal sales across California in 2022, a decrease from \$5.77 billion in 2021); Susan Wood, *Survey: 37% of US Cannabis Operators Say They’re Not Profitable*, N. BAY BUS. J. (Mar. 14, 2022), <https://www.northbaybusinessjournal.com/article/industrynews/survey-37-of-us-cannabis-operators-say-theyre-not-profitable/> (on file with the *University of the Pacific Law Review*) (reporting that only twenty-six percent of responding California cannabis businesses were profitable).

<sup>3</sup> *Welcome to Huckleberry Hill Farms*, HUCKLEBERRY HILL FARMS, <https://pickhumboldt.com/> (last visited June 17, 2023) (on file with the *University of the Pacific Law Review*).

<sup>4</sup> *Id.*

<sup>5</sup> Tony Lange, *California Cannabis Operators in Peril as American Dream Turns to Nightmare*, CANNABIS BUS. TIMES (Mar. 17, 2023), <https://www.cannabisbusinesstimes.com/news/california-cannabis-peril-dream-nightmare-legalization/> (on file with the *University of the Pacific Law Review*) (describing that Casali returned to the cannabis industry because of the state’s promises of legalization).

<sup>6</sup> *Id.*; Jesse Duncan, *The Cannabis Conversation: Legacy Farms*, LOST COAST OUTPOST (Jan. 1, 2022), <https://lostcoastoutpost.com/2022/jan/1/cannabis-conversation-legacy-farmers/> (on file with the *University of the Pacific Law Review*) (defining a legacy farm as farmers that “have cultivated in historical producing regions for at least twenty years”).

<sup>7</sup> Yakowicz, *supra* note 1 (explaining the loss of profit because of low demand among consumers).

<sup>8</sup> *Id.* (reporting the price per pound of weed at \$665 a pound, a decrease of twenty-six percent year over year).

<sup>9</sup> *Id.* (“[T]he customer is tired of paying the exorbitant taxes and are now buying it from a friend of a friend or the guy on the corner.”).

<sup>10</sup> *Id.* (stating that the sparse number of legal dispensaries has resulted in California growing more legal cannabis than what consumers can legally consume).

<sup>11</sup> *Id.* (reporting Casali’s views for the 2023 season and problems that may continue including the impact of the illegal cannabis market).

In 2016, California legalized recreational cannabis use.<sup>12</sup> The California Legislature established the Department of Cannabis Control (DCC) in 2021 with the goal of facilitating and advancing the legal market in California and created regulations for cannabis businesses.<sup>13</sup> These regulations have made it difficult for many businesses to keep their doors open.<sup>14</sup> A daunting obstacle for cannabis retailers is the limited availability of socially attractive areas for consuming legally purchased cannabis.<sup>15</sup>

Currently, local jurisdictions must approve consumption areas on premises where cannabis is sold and approve the sale of cannabis through retailers or microbusinesses, creating additional obstacles for businesses.<sup>16</sup> The only other option is for people to consume at home.<sup>17</sup> Attractive social cannabis consumption areas allow consumers to socialize and encourage people to purchase cannabis from the legal market by being able to consume on the same premises.<sup>18</sup>

AB 374 attempts to solve this problem by allowing social consumption lounges to expand the types of activities that can occur on their premises.<sup>19</sup> The law allows consumption areas to prepare and sell food and beverages as well as host live musical performances, along with other events.<sup>20</sup> The bill mimics the successful framework of cannabis lounges seen in Amsterdam.<sup>21</sup> In Amsterdam, people may purchase and consume cannabis within the legal limits on business premises while enjoying food, drink, or performances.<sup>22</sup>

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<sup>12</sup> Katy Steinmetz, *What to Know About Marijuana Legalization in California*, TIME (Nov. 9, 2016), <https://time.com/4565438/california-marijuana-faq-rules-prop-64/> (on file with the *University of the Pacific Law Review*) (outlining the history of marijuana legalization in California).

<sup>13</sup> *California's Cannabis Laws*, DEP'T OF CANNABIS CONTROL, <https://cannabis.ca.gov/cannabis-laws/laws-and-regulations/> (last visited May 26, 2023) (on file with the *University of the Pacific Law Review*) (listing statutes, regulations, and ordinances that set rules for the cannabis industry); *The Department of Cannabis Control Is Established*, DEP'T OF CANNABIS CONTROL, <https://cannabis.ca.gov/2021/07/department-of-cannabis-control-established/> (combining the Bureau of Cannabis Control, CDFA's CalCannabis Cultivation Licensing Division, and CDPH's Manufactured Cannabis Safety Branch into the DCC); *About the Department of Cannabis Control*, DEP'T OF CANNABIS CONTROL, <https://cannabis.ca.gov/about-us/about-dcc/> (last visited Aug. 8, 2023) (on file with the *University of the Pacific Law Review*) (listing the DCC's mission and functions of the DCC).

<sup>14</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 3 (May 18, 2023).

<sup>15</sup> Alex Wigglesworth, *Q&A: Legal Weed in California: A Consumer's Guide*, L.A. TIMES (Apr. 20, 2018), <https://www.latimes.com/politics/la-pol-ca-cannabis-consumer-guide-20180420-htmllstory.html> (on file with the *University of the Pacific Law Review*) (stating that consumption of cannabis is legal on private property in areas that permit tobacco smoking).

<sup>16</sup> *Id.* (explaining that state law allows for local jurisdictions to authorize cannabis consumption on retailer's premises).

<sup>17</sup> *Id.* (clarifying that cannabis consumption can only be on private property that permits tobacco smoking).

<sup>18</sup> Geoffrey Lawrence, *California Considers Legislative Changes to its Legal Cannabis Market*, REASON F. (Apr. 9, 2023), <https://reason.org/commentary/california-considers-legislative-changes-to-its-legal-cannabis-market/> (on file with the *University of the Pacific Law Review*) (listing social opportunities as more attractive options of purchasing cannabis legally).

<sup>19</sup> *Id.*

<sup>20</sup> AB 374, 2023 Leg., 2023–2024 Sess. (Cal. 2023) (as amended on May 18, 2023, but not enacted).

<sup>21</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 1 (May 18, 2023) (describing cannabis “coffeeshops” in Amsterdam that serve as social hubs).

<sup>22</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 1 (May 18, 2023) (describing the framework of consumption lounges in Amsterdam); SENATE COMMITTEE ON BUSINESS, PROFESSIONS AND ECONOMIC DEVELOPMENT, COMMITTEE ANALYSIS OF AB 374, at 3 (June 26, 2023) (noting that the 700 cannabis lounges in Amsterdam generate 1.5 million visitors per year).

AB 374 is an encouraging first step in preserving the legal cannabis industry and eliminating an unnecessary ban on social occasions involving cannabis.<sup>23</sup> The bill incentivizes the legal purchase of cannabis by offering new experiences to consume cannabis in a social setting while also protecting cannabis businesses from shutting down.<sup>24</sup> To aid the struggling cannabis industry more effectively, AB 374 should be amended to include provisions that lower the state excise tax.<sup>25</sup> The fifteen percent excise tax on cannabis sales should be reduced for businesses that have social consumption lounges to further encourage consumers to purchase from the legal market.<sup>26</sup>

## II. LEGAL BACKGROUND

Cannabis use in the United States has a long and complex history, but legal recreational cannabis use is still fairly new in California.<sup>27</sup> With AB 374, California continues to be a national leader in cannabis policy.<sup>28</sup> In 1996, California became the first state to legalize medical cannabis use when it passed the Compassionate Use Act.<sup>29</sup> Twenty years later, the legalization of recreational use was intended partly to combat the illegal market and partly to encourage people to purchase cannabis legally.<sup>30</sup>

Despite efforts to limit the illegal market, high taxes and limited opportunities for businesses allow the black market to maintain a strong presence.<sup>31</sup> As a result, legal cannabis businesses are struggling.<sup>32</sup> Section A outlines how the history of cannabis-use laws in California has established the legal market today.<sup>33</sup> Section B discusses already existing social consumption lounges and the benefits

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<sup>23</sup> Lawrence, *supra* note 18 (stating that lifting the ban on social occasions may make lounges more attractive to consumers).

<sup>24</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 3 (May 18, 2023) (describing how preparing food and drink for sale would allow cannabis retailers to move away from the pharmacy-like dispensary model).

<sup>25</sup> See Paul Demko, *Why Weed Companies Can't Make Any Money*, POLITICO (Sept. 4, 2022), <https://www.politico.com/news/2022/09/04/weed-companies-cant-make-money-00054541> (on file with the *University of the Pacific Law Review*) (explaining how high taxes on cannabis prevent local businesses from making enough profit).

<sup>26</sup> *Tax Guide for Cannabis Businesses*, CAL. DEP'T OF TAX AND FEE ADMIN., <https://www.cdtfa.ca.gov/industry/cannabis.htm#Retailers> (last visited June 15, 2023) (on file with the *University of the Pacific Law Review*) (defining the cannabis excise tax as fifteen percent).

<sup>27</sup> *History of Cannabis*, UCLA CTR. FOR CANNABIS AND CANNABINOIDS, <https://cannabis.semel.ucla.edu/history-of-cannabis/> (last visited June 13, 2023) (on file with the *University of the Pacific Law Review*) (outlining the history of cannabis use).

<sup>28</sup> Mark Baldassare et al., *Californians' Attitudes Toward Marijuana Legalization*, PUB. POL'Y INST. OF CAL. (Apr. 2015), [https://www.ppic.org/wp-content/uploads/content/pubs/jtf/JTF\\_MarijuanaLegalizationJTF.pdf](https://www.ppic.org/wp-content/uploads/content/pubs/jtf/JTF_MarijuanaLegalizationJTF.pdf) (on file with the *University of the Pacific Law Review*) (detailing California's past marijuana policies).

<sup>29</sup> *California's Cannabis Laws*, *supra* note 13.

<sup>30</sup> Amanda Chicago Lewis, *California Legalized Weed Five Years Ago. Why Is the Illicit Market Still Thriving?*, GUARDIAN (Nov. 2, 2021), <https://www.theguardian.com/us-news/2021/nov/02/california-legal-weed-cannabis-industry-economy> (on file with the *University of the Pacific Law Review*) (reporting that California legalized recreational cannabis use in 2016 but that eighty to ninety percent of the cannabis market remains illegal).

<sup>31</sup> *Id.* (describing how high taxes and local control are hurting the cannabis industry).

<sup>32</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 3 (May 18, 2023).

<sup>33</sup> *Infra* Section II.A.

they provide.<sup>34</sup> Section C highlights why high taxes and the prominence of the illegal market prevent businesses from making large profits.<sup>35</sup>

### *A. California's History of Cannabis Use Laws*

Prior to recreational use, California legalized the medicinal use of cannabis.<sup>36</sup> As the industry began to expand through newly legalized recreational use, California passed statutes and regulations to oversee businesses.<sup>37</sup> Subsection 1 highlights important aspects about medicinal and recreational cannabis consumption in California.<sup>38</sup> Subsection 2 discusses the most relevant statute that governs cannabis business operations.<sup>39</sup>

#### *1. Revolution of Cannabis Use in California*

California voters passed the Compassionate Use Act in 1996 after supporters saw the pain-relieving benefits of cannabis.<sup>40</sup> The Act allowed doctors to recommend that patients grow their own cannabis for medical consumption.<sup>41</sup> However, cultivating cannabis was still illegal, creating a gray area for medicinal cannabis use.<sup>42</sup> Entrepreneurs began opening dispensaries and other illicit businesses to serve the medical cannabis need.<sup>43</sup> By 2010, Los Angeles had about 2,000 cannabis retailers illegally selling cannabis, causing the illegal market to take off.<sup>44</sup>

The next step forward in developing the cannabis industry was the legalization of recreational use.<sup>45</sup> In 2016, California passed Proposition 64 to provide new safety regulations involving cannabis consumption.<sup>46</sup> Public consumption remained illegal, but Proposition 64 gave local jurisdictions the

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<sup>34</sup> *Infra* Section II.B.

<sup>35</sup> *Infra* Section II.C.

<sup>36</sup> Chicago Lewis, *supra* note 30.

<sup>37</sup> *California's Cannabis Laws*, *supra* note 13 (listing statutes and regulations that cannabis businesses must follow).

<sup>38</sup> *Infra* Subsection II.A.1.

<sup>39</sup> *Infra* Subsection II.A.2.

<sup>40</sup> Chicago Lewis, *supra* note 30 (reporting AIDS activists' support of legalization in the Bay Area because of the pain-relieving and hunger stimulating aspects of cannabis consumption among friends living with AIDS); *Guidelines For The Security and Non-Diversion of Cannabis Grown For Medicinal Use*, CAL. DEP'T OF JUST., <https://oag.ca.gov/system/files/media/medicinal-cannabis-guidelines.pdf> (last visited Apr. 11, 2024) (on file with the *University of the Pacific Law Review*) (stating that California voters passed "Proposition 215, the Compassionate Use Act of 1996").

<sup>41</sup> Chicago Lewis, *supra* note 30 (describing the limitations of the Compassionate Use Act).

<sup>42</sup> *Id.* (providing details of how the illegal cannabis market grew due to cultivation still being illegal).

<sup>43</sup> *Id.*

<sup>44</sup> *Id.* (describing the growth of the illegal market after legalizing medical consumption of cannabis).

<sup>45</sup> Ben Adler, *Explaining Proposition 64: How California would Legalize Marijuana*, CAPRADIO (Oct. 20, 2016), <https://www.capradio.org/articles/2016/10/20/explaining-proposition-64-how-california-would-legalize-marijuana/> (on file with the *University of the Pacific Law Review*) (noting the details of Proposition 64).

<sup>46</sup> *Local Government Reference Guide to Proposition 64*, CAL. STATE ASS'N OF CNTY., [https://www.counties.org/sites/main/files/file-attachments/local\\_government\\_reference\\_guide\\_to\\_prop\\_64\\_final\\_11-22-16.pdf](https://www.counties.org/sites/main/files/file-attachments/local_government_reference_guide_to_prop_64_final_11-22-16.pdf) (last visited Aug. 6, 2023) (on file with the *University of the Pacific Law Review*) (legalizing recreational cannabis consumption for individuals over the age of twenty-one).

ability to regulate cannabis businesses by requiring specific licenses and permits.<sup>47</sup> Local jurisdictions now had the power to regulate what was previously an illegal market, creating safer opportunities for consumers.<sup>48</sup>

## 2. *The Medical and Adult Use Cannabis Regulation and Safety Act*

The most prevalent statewide statute for cannabis businesses is the Medical and Adult Use Cannabis Regulation and Safety Act (MAUCRSA).<sup>49</sup> This establishes guidelines for licenses, oversight, and enforcement policies related to cannabis businesses.<sup>50</sup> MAUCRSA prohibits cannabis consumption in any public place, but Proposition 64 authorized local jurisdictions to approve consumption on a retailer or microbusinesses' premises.<sup>51</sup> Despite MAUCRSA permitting onsite consumption, it does not contain express language allowing businesses to sell food, drinks, or tickets to performances.<sup>52</sup>

This led the DCC to adopt Section 15407 of the California Code of Regulations (CCR)—prohibiting the sale of food and drink not infused with cannabis on retailer's premises.<sup>53</sup> Later in 2022, the DCC amended Section 15407 to allow businesses to sell prepackaged food and drinks.<sup>54</sup> This allowed consumers to have enough flexibility to receive food and drinks without requiring the DCC to maintain regulatory oversight of the preparation of food and drinks.<sup>55</sup> This made it clear that cannabis businesses were not permitted to prepare or sell fresh food and drinks.<sup>56</sup>

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<sup>47</sup> *Id.*

<sup>48</sup> *Id.* (noting that state authorities and local jurisdictions can regulate the industry through permits, licenses, and zoning laws).

<sup>49</sup> *California's Cannabis Laws*, *supra* note 13 (listing statutes and regulations that cannabis businesses must follow).

<sup>50</sup> *Id.* (describing MAUCRSA).

<sup>51</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 2 (May 18, 2023) (describing how the Amsterdam model would only partially be legal under California Law); Adler, *supra* note 45 (noting that businesses are required to obtain licenses for the on-site consumption of cannabis).

<sup>52</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 2 (May 18, 2023) (providing details of MAUCRSA).

<sup>53</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 2 (May 18, 2023) (providing details about how the DCC responded to MAUCRSA to prevent businesses from selling food and drinks and only allowing the sale of cannabis and cannabis products).

<sup>54</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 2 (May 18, 2023) (providing information about Section 15407 of regulations adopted by the DCC); DEP'T OF CANNABIS CONTROL, FINAL STATEMENT OF REASONS 180–81 (2022) (on file with the *University of the Pacific Law Review*) (explaining the DCC's rationale behind amending section 15407).

<sup>55</sup> DEP'T OF CANNABIS CONTROL, FINAL STATEMENT OF REASONS, *supra* note 54 (explaining the DCC's rationale behind amending section 15407).

<sup>56</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 2 (May 18, 2023) (allowing guests to bring food and drink from outside sources not related to the consumption lounge or purchasing prepackaged food and drink on the premises).

## B. Existing Social Cannabis Consumption Lounges

Consumption lounges are relatively new to California but have had a strong presence both domestically and abroad.<sup>57</sup> Retailers that have consumption lounges on their premises have seen the benefits that come with them.<sup>58</sup> Subsection 1 describes Amsterdam's approach to cannabis consumption lounges.<sup>59</sup> Subsection 2 provides examples of established consumption lounges in the United States.<sup>60</sup>

### 1. The Netherlands' Toleration Policy and the Establishment of Cannabis Coffee Shops

California is not the first place to experiment with legal social consumption lounges.<sup>61</sup> AB 374 is inspired by "coffeeshops", located in Amsterdam, where cannabis is sold and consumed.<sup>62</sup> In the 1970s, the Netherlands implemented a toleration policy regarding cannabis, attempting to separate hard and soft drug markets.<sup>63</sup> Consumption lounges provide a safe opportunity for consumers and were successful in separating the two markets in Amsterdam.<sup>64</sup>

In addition to separating the two markets, coffeeshops help disincentivize the illicit cannabis market as well.<sup>65</sup> Coffeeshops provide a social and welcoming atmosphere for consumers, one that is not available on the black market.<sup>66</sup> The Netherlands strictly regulates cannabis consumption lounges, and coffeeshops are

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<sup>57</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 1 (May 18, 2023) (describing Amsterdam's "coffeeshops"); 2 *New Marijuana Laws Go into Effect in Colorado in 2020*, CBS COLO. (Dec. 30, 2019), <https://www.cbsnews.com/colorado/news/new-marijuana-laws-colorado-2020/> (on file with the *University of the Pacific Law Review*) (describing cannabis consumption lounges in Colorado).

<sup>58</sup> Freddy Brewster, *Bill Allowing Amsterdam-Style Cannabis Cafés Passes California Assembly*, FOX KTVU2 (June 1, 2023), <https://www.ktvu.com/news/bill-allowing-amsterdam-style-cannabis-cafes-passes-california-assembly> (on file with the *University of the Pacific Law Review*) (stating that Amsterdam's 700 cannabis cafes generate an expected \$1 billion annually).

<sup>59</sup> *Infra* Subsection II.B.1.

<sup>60</sup> *Infra* Subsection II.B.2.

<sup>61</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 1 (May 18, 2023) (describing Amsterdam's "coffeeshops").

<sup>62</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 3 (May 18, 2023) (comparing the Amsterdam model to AB 374's model of consumption lounges).

<sup>63</sup> Elizabeth Schulze, *Why Amsterdam Is Jealous of America's Growing Weed Industry*, CNBC (Sept. 20, 2018), <https://www.cnbc.com/2018/09/20/why-amsterdam-is-jealous-of-americas-growing-weed-industry.html> (on file with the *University of the Pacific Law Review*) (stating the purpose of The Netherlands' tolerance policy); Ginni Correa, *Why the Netherlands Is Becoming a Narco State*, ADDICTION CTR. (Jan. 8, 2020), <https://www.addictioncenter.com/news/2020/01/netherlands-narco-state/> (on file with the *University of the Pacific Law Review*) (defining soft drugs as "drugs with a low risk of harm and/or addiction such as hash, marijuana, sleeping pills, and sedatives" and hard drugs as "substances...considered to have a higher risk of harm and addiction").

<sup>64</sup> Schulze, *supra* note 63 (stating that the policy succeeded in separating the markets but created a new illegal market for cannabis); JEAN-PAUL GRUND AND JOOST BREEKSEMA, COFFEE SHOPS AND COMPROMISE, SEPARATED ILLICIT DRUG MARKETS IN THE NETHERLANDS 29 (2013) (highlighting coffee shops as having an impact on separating the two markets due to the low number of people addicted to hard drugs when "compared to the rest of Europe").

<sup>65</sup> SENATE COMMITTEE ON BUSINESS, PROFESSIONS AND ECONOMIC DEVELOPMENT, COMMITTEE ANALYSIS OF AB 374, at 3 (June 26, 2023) (noting that coffeeshops offer an experience that the illicit market is unable to provide).

<sup>66</sup> SENATE COMMITTEE ON BUSINESS, PROFESSIONS AND ECONOMIC DEVELOPMENT, COMMITTEE ANALYSIS OF AB 374, at 3 (June 26, 2023) (detailing the benefits of coffeeshops in Amsterdam).



not allowed to serve alcohol.<sup>67</sup> Today, there are over 700 cannabis coffeeshops located throughout the Netherlands.<sup>68</sup>

## 2. Cannabis Consumption Lounges in The United States

Similar to Amsterdam, cities in the United States are also permitting consumption lounges.<sup>69</sup> Before recreational legalization, the city of West Hollywood in Los Angeles County began distributing permits for ten dispensaries and sixteen consumption lounges within the city.<sup>70</sup> In 2019, Lowell Farms: A Cannabis Café opened in West Hollywood.<sup>71</sup> Lowell's allowed guests to consume cannabis socially while enjoying food and drinks.<sup>72</sup> Lowell's was split into two separate businesses, a cannabis dispensary and a restaurant, in order to comply with state law.<sup>73</sup> This model created unnecessary obstacles Lowell's was forced to follow, restricting the business from maximizing profits.<sup>74</sup> Outside sources prepared and served limited food and beverage options to customers inside the lounge.<sup>75</sup> Online reservations for Lowell's first thirty days of business sold out within three hours of being available.<sup>76</sup> The COVID-19 pandemic forced Lowell's to close its doors permanently, but in 2022, West Hollywood opened two new consumption lounges.<sup>77</sup>

Colorado is another pioneer in cannabis policy.<sup>78</sup> In 2019, Colorado Governor Jared Polis signed House Bill 1230 into law—permitting on-site

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<sup>67</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 1 (May 18, 2023).

<sup>68</sup> SENATE COMMITTEE ON BUSINESS, PROFESSIONS AND ECONOMIC DEVELOPMENT, COMMITTEE ANALYSIS OF AB 374, at 3 (June 26, 2023).

<sup>69</sup> Baylen Linnekin, *New California Bill Proposes Legalizing Authentic Cannabis Cafes*, REASON (Feb. 11, 2023) <https://reason.com/2023/02/11/new-california-bill-proposes-legalizing-authentic-cannabis-cafes/> (on file with the *University of the Pacific Law Review*) (describing cities in Colorado and California).

<sup>70</sup> *Id.* (stating that West Hollywood already anticipated the legalization of recreational use).

<sup>71</sup> *Id.*

<sup>72</sup> *Id.* (describing the social opportunities that were available for guests at Lowell Farms: A Cannabis Café); Mona Holmes, *West Hollywood's Cannabis Consumption Lounges Are Making a Comeback*, EATER L.A. (Mar. 8, 2022), <https://la.eater.com/2022/3/8/22266524/west-hollywood-cannabis-consumption-lounges-update-2022> (on file with the *University of the Pacific Law Review*) (stating that Lowell's later changed its name to the Original Cannabis Café).

<sup>73</sup> Mona Holmes, *LA's First Cannabis Restaurant Had to Split into Two Businesses to Comply with State Law*, EATER L.A. (Sept. 11, 2019), <https://la.eater.com/2019/9/11/20853095/west-hollywood-cannabis-consumption-lounge-restaurant-state-regulations> (on file with the *University of the Pacific Law Review*) (describing how Lowell's worked around state law to prepare and serve food and drink).

<sup>74</sup> *Id.* (listing obstacles that Lowell's had to follow such as, zoning requirements, separating the main entrance of the restroom to comply with state and local regulations, and customers receiving two separate checks, one for food and drink and another for cannabis products).

<sup>75</sup> *Id.* (outlining how Lowell's operated as “three different sections located on a 20,000 square foot lot”).

<sup>76</sup> *Id.*

<sup>77</sup> Mona Holmes, *Another Cannabis Consumption Lounge Is Heading to Smoking-Hot WeHo*, EATER L.A. (June 26, 2023), <https://la.eater.com/2023/6/26/23769927/pleasure-med-west-hollywood-cannabis-consumption-lounge-opening-am-intel> (on file with the *University of the Pacific Law Review*) (noting that consumption lounge business slowed significantly during the COVID-19 pandemic, but in 2022, Artist Tree consumption lounge opened followed by Woody Harrelson opening The Woods later that year); Holmes, *supra* note 72 (stating that Lowell's was unable to follow social distancing requirements during the COVID-19 pandemic because “consuming cannabis on-site is an inherently social activity with airborne issues at play”).

<sup>78</sup> 2 *New Marijuana Laws Go into Effect in Colorado in 2020*, *supra* note 57.

cannabis consumption at “marijuana hospitality establishments.”<sup>79</sup> The law only allows for on-site consumption and not the sale of cannabis on the same premises.<sup>80</sup> Recently, Colorado’s cannabis industry has struggled as it faces many of the same problems that California’s industry experiences.<sup>81</sup> Colorado ranks second in the nation in terms of states that have seen the cannabis industry shrink, losing more than 10,000 jobs in the past year alone.<sup>82</sup>

### C. High Taxes and the Illegal Market

The legal cannabis industry faces several challenges that limit the success of retailers and microbusinesses.<sup>83</sup> Subsection 1 outlines the taxes imposed on cannabis retailers and microbusinesses.<sup>84</sup> Subsection 2 lists steps California has taken to relieve some of the tax burden imposed on the industry.<sup>85</sup> Subsection 3 explains the consistent presence of the black market in California.<sup>86</sup>

#### 1. California Taxes Imposed on Cannabis Retailers and Microbusinesses

Although California’s legal market has experienced a boom in the number of retailers over the past decade, high taxes are stifling the industry.<sup>87</sup> Retailers are responsible for collecting sales tax and a fifteen percent cannabis excise tax on cannabis products.<sup>88</sup> Excise taxes frequently target specific goods that “have a high social cost.”<sup>89</sup> Taxes like these are often implemented as a form of deterrence to encourage individuals not to purchase the goods.<sup>90</sup>

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<sup>79</sup> *Id.* (listing The Coffee Joint as an example in Denver that allows guests to bring their own cannabis or are given the opportunity to purchase products from a dispensary next store).

<sup>80</sup> *Id.* (stating that House Bill 1230 permits “tasting rooms” to sell cannabis products but prohibits the sale of cannabis products in “marijuana hospitality establishments”).

<sup>81</sup> Megan Ulu-Lani Boyanton, *Colorado’s Cannabis Industry Has Fallen on Hard Times. What Does the Future Hold?*, DENVER POST (May 21, 2023), <https://www.denverpost.com/2023/05/21/colorado-cannabis-marijuana-weed-dispensaries-downturn/> (on file with the *University of the Pacific Law Review*) (listing the illegal market, decreasing prices, and low demand with a high supply as problems plaguing Colorado’s cannabis industry).

<sup>82</sup> *Id.*

<sup>83</sup> Chicago Lewis, *supra* note 30 (listing high taxes and the prominent illegal market as harming the legal cannabis industry).

<sup>84</sup> *Infra* Subsection II.C.1.

<sup>85</sup> *Infra* Subsection II.C.2.

<sup>86</sup> *Infra* Subsection II.C.3.

<sup>87</sup> Suzanne Phan, *A Closer Look at the State of CA’s Cannabis Industry: Progress v. Ongoing Challenges*, ABC (Apr. 21, 2023), <https://abc7news.com/california-cannabis-industry-san-francisco-dispensary-420-weed/13162029/> (on file with the *University of the Pacific Law Review*) (describing how cannabis businesses are changing and San Francisco’s increase in the number of cannabis retailers).

<sup>88</sup> *Tax Guide for Cannabis Businesses*, *supra* note 26 (listing the taxes that are placed on cannabis businesses); *Tax Guide for Cigarettes and Tobacco Products*, CAL. DEP’T OF TAX AND FEE ADMIN., (last visited July 12, 2023) (on file with the *University of the Pacific Law Review*) (noting that the cigarette tax rate is \$0.1435 per cigarette or \$2.87 per pack); *Tax Guide for California Electronic Cigarette Excise Tax*, CAL. DEP’T OF TAX AND FEE ADMIN., (last visited July 12, 2023) (on file with the *University of the Pacific Law Review*) (noting that retailers are required to collect a 12.5% California Electronic Cigarette Excise Tax on the sales of electronic cigarettes containing nicotine).

<sup>89</sup> Julia Kagan, *Excise Tax: What It Is and How It Works, with Examples*, INVESTOPEDIA (Mar. 8, 2023), <https://www.investopedia.com/terms/e/excisetax.asp> (on file with the *University of the Pacific Law Review*) (defining sin taxes as a “form of excise tax on goods that have a high social cost”).

<sup>90</sup> *Id.* (listing an excise tax of \$4.35 on a pack of cigarettes in New York as an example of deterring consumers).

In addition to taxes required by state law, cannabis retailers may also be required to pay local business taxes—which further increase these already high prices.<sup>91</sup> Local taxes are another form of deterrence, implemented in an attempt to lower use.<sup>92</sup> Customers feel the brunt of this taxation as retailers increase their prices to make up for the revenue lost due to this excessive taxation.<sup>93</sup> Despite the industry suffering from high taxes and deterrence by the state, California has still been able to generate \$4.6 billion in total tax revenue since 2018.<sup>94</sup>

## 2. California's Attempts to Lower Cannabis Taxes

California has taken formidable steps to relieve the cannabis industry of high taxes.<sup>95</sup> For instance, cannabis growers previously faced burdensome cultivation taxes.<sup>96</sup> The cultivation tax established a fixed rate and does not change over time to reflect any changes in the market.<sup>97</sup> Despite the price per pound of cannabis decreasing, the cultivation tax remained the same.<sup>98</sup> Governor Newsom sought to bring much-needed relief to growers when he signed AB 195 in 2022.<sup>99</sup>

AB 195 eliminated the cultivation tax that forced growers to charge higher prices as a way of recovering lost profits.<sup>100</sup> Retailers and microbusinesses were forced to pay higher prices for products due to the cultivation tax—leading to higher prices for consumers.<sup>101</sup> AB 195 continues the fifteen percent excise tax for three years, with the option to later increase it.<sup>102</sup> Any future increase to the excise tax would be an attempt to regain lost revenue from eliminating the cultivation tax.<sup>103</sup>

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<sup>91</sup> *Everything You Need to Know About California Cannabis Tax*, LAJOLLA.COM, <https://lajolla.com/article/california-cannabis-tax/> (last visited June 17, 2023) (on file with the *University of the Pacific Law Review*) (listing taxes placed on the retail sale of cannabis); *Cannabis Business Operation Tax*, CITY OF SACRAMENTO, <https://www.cityofsacramento.org/Finance/Revenue/Business-Operation-Tax/Cannabis-Business-Tax> (last visited June 17, 2023) (providing that the City of Sacramento requires retailers to pay an additional four percent in business tax).

<sup>92</sup> *Cannabis Business Operation Tax*, *supra* note 91 (providing that the City of Sacramento requires retailers to pay an additional four percent in business tax).

<sup>93</sup> Andrew Sheeler, *California's Illicit Marijuana Market Thrives as Much of the State Continues to Restrict Sales*, SACRAMENTO BEE (Oct. 4, 2022), <https://www.sacbee.com/news/politics-government/capitol-alert/article266176661.html> (on file with the *University of the Pacific Law Review*) (explaining why retailer prices are higher than the illegal market).

<sup>94</sup> CALIFORNIA DEPARTMENT OF TAX AND FEE ADMINISTRATION REPORTS CANNABIS TAX REVENUES FOR THE FOURTH QUARTER OF 2022, CAL. DEP'T OF TAX AND FEE ADMIN., <https://www.cdta.ca.gov/news/23-02.htm> (last visited July 15, 2023) (on file with the *University of the Pacific Law Review*) (reporting California's total cannabis tax revenue since 2018).

<sup>95</sup> A.J. Herrington, *California Eliminates Cannabis Cultivation Tax*, FORBES (July 5, 2022), <https://www.forbes.com/sites/ajherrington/2022/07/05/california-eliminates-cannabis-cultivation-tax/?sh=4cd59a16de60> (on file with the *University of the Pacific Law Review*).

<sup>96</sup> *Id.* (defining the cultivation tax as \$161 per pound of cannabis flower).

<sup>97</sup> *Id.*

<sup>98</sup> *Id.* (stating that the cultivation tax amount was a flat rate and did not depend on the price of cannabis per pound).

<sup>99</sup> *Id.* (providing details of Assembly Bill 195); *Tax Guide for Cannabis Businesses*, *supra* note 26.

<sup>100</sup> *Tax Guide for Cannabis Businesses*, *supra* note 26 (stating that beginning on July 1, 2022, the state no longer requires cultivators to collect a cultivation tax on cannabis entering the legal market).

<sup>101</sup> Sheeler, *supra* note 93 (explaining why retailer prices are higher than the illegal market).

<sup>102</sup> Herrington, *supra* note 95 (describing why California may change the excise tax in the future).

<sup>103</sup> *Id.*

### 3. California's Cannabis Black Market

High taxes and inflated prices in the legal market have driven consumers towards the illegal market where prices are much lower.<sup>104</sup> Due to the gray area created by the Compassionate Use Act, the illegal market expanded rapidly.<sup>105</sup> The illegal market has maintained a strong presence in California, despite the legalization of recreational use.<sup>106</sup> Law enforcement operations indicate the alarming presence that the black market maintains.<sup>107</sup>

During the fourth quarter of 2022, the Unified Cannabis Enforcement Taskforce (UCETF) served thirty search warrants and seized over \$32 million worth of illegal cannabis products.<sup>108</sup> In the first quarter of 2023, the UCETF only served twenty-one search warrants but seized over \$52 million worth of illegal cannabis products.<sup>109</sup> These figures show that the illegal market is growing and consumers are choosing the illegal market over the more expensive, legal one.<sup>110</sup> Legalization proponents expected the legalization of recreational use to weaken the illegal market and help retailers, but retailers have not seen the benefits they were promised.<sup>111</sup>

### III. AB 374

Assembly Member Matt Haney introduced AB 374 to loosen the restrictions and regulations surrounding struggling cannabis businesses.<sup>112</sup> First, AB 374 amends Section 26200 of the Business and Professions Code, allowing licensed cannabis retailers or microbusinesses to permit cannabis consumption on their premises.<sup>113</sup> The bill allows smoking, vaping, and ingesting cannabis products on the premises of a retailer or microbusiness.<sup>114</sup>

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<sup>104</sup> Lester Black, 'Really Dire': California Pot Tax Revenue Falls for 7th Straight Quarter, KSBW 8 ACTION NEWS (June 13, 2023), <https://www.ksbw.com/article/really-dire-california-pot-tax-revenue-falls-for-7th-straight-quarter/44189410> (on file with the *University of the Pacific Law Review*) (reporting that tax revenue from the industry has decreased for seven quarters in a row).

<sup>105</sup> Chicago Lewis, *supra* note 30 (providing details of how the illegal cannabis market grew due to cultivation still being illegal).

<sup>106</sup> Sheeler, *supra* note 93 (stating that local restrictions and high taxes contribute to the illegal market's strong presence).

<sup>107</sup> *California's Statewide Cannabis Enforcement Taskforce Continues to Aggressively Combat Illegal Market by Seizing Over \$52M Worth of Unlicensed Cannabis Products in Q1 2023*, DEP'T OF CANNABIS CONTROL, <https://cannabis.ca.gov/2023/05/californias-statewide-cannabis-enforcement-taskforce-continues-to-aggressively-combat-illegal-market-by-seizing-over-52m-worth-of-unlicensed-cannabis-products-in-q1-2023/> (last visited June 17, 2023) (on file with the *University of the Pacific Law Review*) (reporting statistics for search warrants executed by the UCETF).

<sup>108</sup> *Id.*

<sup>109</sup> *Id.*

<sup>110</sup> Sheeler, *supra* note 93 (describing high taxes and local restrictions as reasons people choose the illegal market).

<sup>111</sup> *Id.* (stating that Proposition 64 should have weakened the illegal market, but it has not had the impact that legal businesses hoped for).

<sup>112</sup> Linnekin, *supra* note 69.

<sup>113</sup> AB 374, 2023 Leg., 2023–2024 Sess. (Cal. 2023) (as amended on May 18, 2023, but not enacted).

<sup>114</sup> *Id.* (clarifying that local jurisdictions must authorize the retailer or microbusiness to sell and consume cannabis).

Second, the bill allows cannabis retailers to prepare and sell food, as well as sell non-alcoholic and non-cannabis-based beverages pursuant to the California Retail Food Code and the Health and Safety Code.<sup>115</sup> The bill also permits prepackaged food and non-alcoholic beverages to be served in accordance with existing law.<sup>116</sup> Further, AB 374 allows businesses to host and sell tickets for live performances, where consumption is permitted.<sup>117</sup> The bill limits these activities to persons twenty-one years of age and older and prohibits the sale or consumption of alcohol or tobacco.<sup>118</sup> The consumption area must not be visible to the public as well.<sup>119</sup>

#### IV. ANALYSIS

AB 374 is a notable response to a struggling cannabis industry in California.<sup>120</sup> AB 374 is a strong start to saving the industry, but further improvements are necessary to help retailers and microbusinesses.<sup>121</sup> Section A discusses how AB 374 encourages consumers to return to the legal market and explores the ways retailers can improve their businesses.<sup>122</sup> Section B discusses why reducing the California Excise Tax will help cannabis retailers, microbusinesses, and the state itself.<sup>123</sup>

##### *A. Encouragement of the Legal Market and New Social Experiences*

AB 374 is designed to help businesses struggling in the legal cannabis industry by offering new experiences for consumers.<sup>124</sup> Subsection 1 explains how AB 374 offers new opportunities for consumers in the legal market.<sup>125</sup> Subsection 2 discusses how AB 374 improves the business model that retailers and microbusinesses must implement.<sup>126</sup> Subsection 3 highlights how non-consumers can contribute to the cannabis industry in a way that was not previously possible.<sup>127</sup>

##### *1. Encouraging Use of the Legal Market*

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<sup>115</sup> *Id.* (listing section 113700 of the Retail Food Code and Part 7 of Division 104 of the Health and Safety Code) (stating that prepared food and beverages must be nonalcoholic and noncannabis-infused).

<sup>116</sup> *Id.* (existing administrative law allows for licensed retailers or microbusinesses to sell prepackaged, noncannabis-infused, and nonalcoholic food and beverages on premises that permit cannabis consumption).

<sup>117</sup> *Id.*

<sup>118</sup> *Id.* (identifying limitations under section 26200 of the Business and Professions Code).

<sup>119</sup> *Id.* (identifying a limitation under section 26200 of the Business and Professions Code).

<sup>120</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 3 (May 18, 2023) (noting that the cannabis industry is currently struggling).

<sup>121</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 3 (May 18, 2023) (identifying that cannabis businesses are struggling to make enough profit).

<sup>122</sup> *Infra* Section IV.A.

<sup>123</sup> *Infra* Section IV.B.

<sup>124</sup> AB 374, 2023 Leg., 2023–2024 Sess. (Cal. 2023) (as amended on May 18, 2023, but not enacted).

<sup>125</sup> *Infra* Subsection IV.A.1.

<sup>126</sup> *Infra* Subsection IV.A.2.

<sup>127</sup> *Infra* Subsection IV.A.3.

AB 374 allows cannabis retailers to move away from the “pharmacy-like cannabis ‘dispensaries’” that current law allows.<sup>128</sup> Current regulations encourage guests to purchase cannabis and leave because there is no social atmosphere available.<sup>129</sup> Even for businesses that have prepackaged foods, guests are not inclined to stay for long periods of time because of the lack of a social experience.<sup>130</sup> This model limits the potential profit that businesses can generate.<sup>131</sup> AB 374 encourages guests to stay longer by creating a more social and engaging experience for patrons.<sup>132</sup> Visitors can socialize while enjoying food, drinks, and live performances.<sup>133</sup>

Further, AB 374 offers cannabis consumers an opportunity not available on the black market.<sup>134</sup> Only the legal market offers social consumption lounges.<sup>135</sup> Many people turn to the black market for lower prices.<sup>136</sup> AB 374 makes consumption lounges attractive enough for consumers to return to the legal market and purchase from retailers or microbusinesses despite the price differences.<sup>137</sup>

## 2. An Improved Business Model Under AB 374

Currently, regulations restrict the ways cannabis retailers make profits.<sup>138</sup> AB 374 allows businesses to bring in new revenue through the sale of fresh food and drinks, as well as tickets for performances.<sup>139</sup> Businesses can increase their revenue stream through multiple different methods, relieving them of the pressure of relying on a limited source of profit.<sup>140</sup> Increased revenue for retailers allows

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<sup>128</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 3 (May 18, 2023) (noting that early policies of medicinal marijuana led to cannabis businesses operating similar to how pharmacies operate).

<sup>129</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 3 (May 18, 2023).

<sup>130</sup> SENATE COMMITTEE ON BUSINESS, PROFESSIONS AND ECONOMIC DEVELOPMENT, COMMITTEE ANALYSIS OF AB 374, at 3–4 (June 26, 2023) (explaining that the state only allows consumption lounges to sell prepackaged food and drink, or guests can bring their own food).

<sup>131</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 3 (May 18, 2023) (providing that businesses operate similarly to pharmacies and retailers serve the most amount of people in the shortest amount of time to maximize profits).

<sup>132</sup> SENATE COMMITTEE ON BUSINESS, PROFESSIONS AND ECONOMIC DEVELOPMENT, COMMITTEE ANALYSIS OF AB 374, at 6–7 (June 26, 2023) (stating that AB 374 permits consumption lounges to prepare and sell food and drink, as well as sell tickets to and host live performances).

<sup>133</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 3 (May 18, 2023) (providing details of AB 374).

<sup>134</sup> SENATE COMMITTEE ON BUSINESS, PROFESSIONS AND ECONOMIC DEVELOPMENT, COMMITTEE ANALYSIS OF AB 374, at 4 (June 26, 2023) (stating that local jurisdictions must approve authorization of consumption lounges).

<sup>135</sup> SENATE COMMITTEE ON BUSINESS, PROFESSIONS AND ECONOMIC DEVELOPMENT, COMMITTEE ANALYSIS OF AB 374, at 3 (June 26, 2023).

<sup>136</sup> Demko, *supra* note 25 (noting that the legal cannabis market is subject to numerous different taxes that lead to increased prices).

<sup>137</sup> Brewster, *supra* note 58 (stating that Amsterdam’s 700 cannabis cafes generate an expected \$1 billion annually).

<sup>138</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 2 (May 18, 2023) (stating that retailers can sell cannabis products and prepackaged food and drinks).

<sup>139</sup> AB 374, 2023 Leg., 2023–2024 Sess. (Cal. 2023) (as amended on May 18, 2023, but not enacted).

<sup>140</sup> SENATE COMMITTEE ON BUSINESS, PROFESSIONS AND ECONOMIC DEVELOPMENT, COMMITTEE ANALYSIS OF AB 374, at 1 (June 26, 2023) (stating that AB 374 allows consumption lounges to prepare fresh food and drinks for sale as well as sell event tickets with local approval).

them to reinvest profits into their premises, making consumption lounges more attractive to consumers as well.<sup>141</sup>

AB 374 expands opportunities for businesses, while also simplifying the cannabis business model.<sup>142</sup> For instance, consumption lounges like Lowell's in West Hollywood must follow numerous regulations and often find loopholes to exploit while still following California law.<sup>143</sup> AB 374 no longer requires businesses to divide themselves to comply with regulations, but instead allows them to be one single business.<sup>144</sup> A single business is more profitable than one divided into multiple businesses.<sup>145</sup> The Colorado cannabis industry provides direct proof of this.<sup>146</sup>

The Colorado cannabis industry struggles with many of the same problems as the California industry.<sup>147</sup> The Colorado General Assembly attempted to aid the industry by passing House Bill 1230.<sup>148</sup> This did not have the impact many hoped for, as it forced the Colorado cannabis industry to eliminate over 10,000 jobs.<sup>149</sup> AB 374 will have a much stronger impact on the California industry by eliminating the limited and split business model that Colorado and California businesses must follow.<sup>150</sup>

By allowing retailers to combine consumption lounges, cannabis retail sales, and the sale of food or drink, AB 374 is a much more impactful piece of legislation than HB 1230.<sup>151</sup> The DCC already stated that guests in lounges should have access to food and drinks.<sup>152</sup> The DCC also recognizes the possibility of businesses operating a restaurant adjacent to the lounge.<sup>153</sup> Based on these statements, it appears as though even the DCC finds these current restrictions

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<sup>141</sup> SENATE COMMITTEE ON BUSINESS, PROFESSIONS AND ECONOMIC DEVELOPMENT, COMMITTEE ANALYSIS OF AB 374, at 1 (June 26, 2023) (stating that AB 374 allows consumption lounges to prepare fresh food and drinks for sale as well as sell event tickets with local approval).

<sup>142</sup> Holmes, *supra* note 73 (describing how Lowell's in West Hollywood works around state law to prepare and serve food and drink).

<sup>143</sup> *Id.* (describing how Lowell's in West Hollywood operates as an adjacent kitchen and consumption lounge but are separate businesses); Holmes, *supra* note 77 (noting that Artist Tree in West Hollywood opened a second story consumption lounge above a dispensary).

<sup>144</sup> Holmes, *supra* note 73 (describing how Lowell's in West Hollywood works around state law to prepare and serve food and drink).

<sup>145</sup> *Id.* (describing how Lowell's in West Hollywood operates as two separate businesses creating multiple investments for the owner).

<sup>146</sup> Ulu-Lani Boyanton, *supra* note 81 (stating that in the past year the Colorado Cannabis industry ranked as the second highest state in the country in job losses, eliminating over 10,000 jobs).

<sup>147</sup> *Id.* (listing the illegal market, decreasing prices, and low demand with a high supply as problems plaguing Colorado's cannabis industry).

<sup>148</sup> 2 *New Marijuana Laws Go into Effect in Colorado in 2020*, *supra* note 57 (highlighting that House Bill 1230 allows businesses to open consumption lounges, but guests cannot purchase cannabis on the same premises).

<sup>149</sup> Ulu-Lani Boyanton, *supra* note 81 (reporting that in March of 2023 legal retail sales of cannabis were \$17 million less than sales in March of 2022 in Colorado).

<sup>150</sup> 2 *New Marijuana Laws Go into Effect in Colorado in 2020*, *supra* note 57 (providing details of House Bill 1230 that only "tasting rooms" can sell cannabis products, but "marijuana hospitality establishments" are not permitted to sell cannabis on the same premises where it is consumed).

<sup>151</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 3 (May 18, 2023).

<sup>152</sup> DEP'T OF CANNABIS CONTROL, FINAL STATEMENT OF REASONS, *supra* note 54 (stating that the DCC currently believes there is enough "flexible access to food and beverages at the consumption lounge").

<sup>153</sup> *Id.* (stating that "nothing prohibits a licensee from operating a restaurant or other establishment adjacent to the licensed premises").

unreasonable.<sup>154</sup> It is clear that something must be done.<sup>155</sup> Therefore, AB 374 is the next logical step in allowing businesses and the industry to benefit from consumers.<sup>156</sup>

### 3. Non-consumers Supporting the Cannabis Industry

Another benefit of AB 374 is that it enables cannabis retailers to earn revenue from both consumers and non-consumers.<sup>157</sup> Previously, non-consumers of cannabis had little reason to visit a cannabis retailer or attend a consumption lounge.<sup>158</sup> Now, AB 374 provides non-consumers an opportunity to contribute to the cannabis industry by attending performances and buying food and drinks.<sup>159</sup> Retailers are able to expand the market they serve and are no longer restricted to only individuals who consume cannabis.<sup>160</sup>

It may be unlikely that retailers see a large number of non-consumers attend performances, but even a small number of new guests will help the industry.<sup>161</sup> Consumers are most likely to choose the illegal market over legal retailers because of the price difference; for non-consumers this is not an issue.<sup>162</sup> Non-consumers would be attracted to the possibility of food, drinks, and performances, and not care for the cannabis price retailers establish.<sup>163</sup> AB 374 opens the doors for retailers to benefit from non-consumers who are not discouraged by the industry's biggest problem—higher prices due to burdensome taxation.<sup>164</sup>

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<sup>154</sup> *Id.* (stating that consumers should have flexibility in the access to food and drink and that “[n]othing prohibits a licensee from operating a restaurant or other establishment adjacent to the licensed premises”).

<sup>155</sup> *Id.*

<sup>156</sup> SENATE COMMITTEE ON BUSINESS, PROFESSIONS AND ECONOMIC DEVELOPMENT, COMMITTEE ANALYSIS OF AB 374, at 3 (June 26, 2023) (stating current law allows only for the sale of prepackaged food and drink if the retailer has obtained local approval).

<sup>157</sup> SENATE COMMITTEE ON BUSINESS, PROFESSIONS AND ECONOMIC DEVELOPMENT, COMMITTEE ANALYSIS OF AB 374, at 1 (June 26, 2023) (stating that AB 374 allows consumption lounges to prepare fresh food and drinks for sale as well as sell event tickets with local approval).

<sup>158</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 2 (May 18, 2023) (stating that current California law restricts retailers to the sale of cannabis and cannabis products).

<sup>159</sup> Brewster, *supra* note 58 (describing how consumption lounges provide communities with new opportunities to experience arts and entertainment in new settings).

<sup>160</sup> *Id.* (describing how consumption lounges provide communities with new opportunities to experience arts and entertainment in new settings).

<sup>161</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 3 (May 18, 2023) (detailing how AB 374 supports cannabis retailers and microbusinesses).

<sup>162</sup> Yakowicz, *supra* note 1 (“[T]he customer is tired of paying the exorbitant taxes and are now buying it from a friend of a friend or the guy on the corner.”).

<sup>163</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 3 (May 18, 2023) (detailing how AB 374 supports cannabis retailers and microbusinesses by offering new experiences).

<sup>164</sup> Chicago Lewis, *supra* note 30 (describing how high taxes and local control are hurting the cannabis industry).



*B. Benefits of Reducing the California Cannabis Excise Tax*

While AB 374 will provide a much-needed revenue inflow for retailers and microbusinesses in the cannabis industry, there are still steps that can be taken to further support businesses.<sup>165</sup> The Revenue and Taxation Code must be reformed to bolster the industry even further.<sup>166</sup> Subsection 1 explains why the state should lower the excise tax.<sup>167</sup> Subsection 2 highlights the expected benefits of lowering the excise tax and the impact it will have on the industry.<sup>168</sup>

*1. Lowering the Excise Tax*

Ideally, for the benefit of businesses the cannabis excise tax would be completely eliminated, as was the cultivation tax.<sup>169</sup> Unfortunately, this is unrealistic, as the state, which faced a massive budget deficit in 2023, needs to continue maintaining the current figures of already-generated tax revenue.<sup>170</sup> However, the current fifteen percent excise tax on the cannabis industry is unsustainable in California.<sup>171</sup> The excise tax deters consumers from the legal market, instead pushing them to the illegal one, where the prices are much lower.<sup>172</sup> Deterring consumers from a legal market is poor public policy because it encourages consumers to participate in the dangerous, unregulated market.<sup>173</sup> This is tantamount to encouraging people to drink water over soda, yet covering the well.<sup>174</sup>

Based on the success of other states, California should change its excise tax rate to ten percent for retailers that establish consumption lounges and serve food and drinks.<sup>175</sup> States with a ten percent excise tax rate have been able to increase cannabis tax revenue, while California has seen a decrease.<sup>176</sup> In the

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<sup>165</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 3 (May 18, 2023) (detailing how AB 374 supports cannabis retailers and microbusinesses).

<sup>166</sup> Black, *supra* note 104 (reporting that tax revenue from the cannabis industry has decreased for seven quarters in a row starting in 2021).

<sup>167</sup> *Infra* Subsection IV.B.1.

<sup>168</sup> *Infra* Subsection IV.B.2.

<sup>169</sup> CALIFORNIA DEPARTMENT OF TAX AND FEE ADMINISTRATION REPORTS CANNABIS TAX REVENUES FOR THE FOURTH QUARTER OF 2022, *supra* note 94 (noting that beginning in July of 2022 Ab 195 eliminated the cultivation tax).

<sup>170</sup> *Id.* (reporting that California has generated \$4.6 billion in total cannabis tax revenue since 2018).

<sup>171</sup> Black, *supra* note 104 (reporting that tax revenue from the cannabis industry has decreased for seven quarters in a row starting in 2021).

<sup>172</sup> *Id.* (reporting that tax revenue from the cannabis industry has decreased for seven quarters in a row starting in 2021).

<sup>173</sup> Andrew Kline, *The Illicit Cannabis Market Puts Consumers At-Risk and Is an Existential Threat to the State-Legal Cannabis Industry*, NAT'L CANNABIS INDUS. ASS'N (Mar. 9, 2020), <https://thecannabisindustry.org/the-illicit-cannabis-market-puts-consumers-at-risk-and-is-an-existential-threat-to-the-state-legal-cannabis-industry/> (on file with the *University of the Pacific Law Review*) (stating products from the illegal market may contain “additives that are not intended for inhalation”).

<sup>174</sup> *Id.* (stating that the products from the illegal market may contain “additives that are not intended for inhalation”).

<sup>175</sup> Phan, *supra* note 87 (describing that the current fifteen percent excise tax is harming the cannabis industry).

<sup>176</sup> *Cannabis Tax Revenues*, CAL. DEP'T OF TAX AND FEE ADMIN., <https://www.cdtfa.ca.gov/dataportal/dataset.htm?url=CannabisTaxRevenues> (last visited July 15, 2023) (on file

second quarter of 2021, the excise tax generated over \$180 million in tax revenue—the most ever for a quarter.<sup>177</sup> Since then, tax revenue has decreased for seven straight quarters and only generated approximately \$104 million during the first quarter of 2023.<sup>178</sup> Colorado also imposes a fifteen percent excise tax and, unsurprisingly, has experienced a similar decrease in tax revenue.<sup>179</sup>

Unlike California and Colorado, other states with lower excise tax rates, have seen an increase in tax revenue during the same time period.<sup>180</sup> Michigan exercises a ten percent excise tax on cannabis and saw an increase in excise tax revenue from 2021 to 2022.<sup>181</sup> Similarly, Massachusetts imposes a 10.75% excise tax and also saw an increase in tax revenue from 2021 to 2022.<sup>182</sup> In these states, consumers have accepted the excise tax as a reasonable rate and are willing to pay higher prices as a result of the tax.<sup>183</sup> Lowering the excise tax will further encourage people to support the legal market by decreasing prices of cannabis, while also creating new opportunities for consumers at consumption lounges.<sup>184</sup>

## 2. Expected Impact of Lowering the Excise Tax

By decreasing the excise tax, California can expect an increase in tax revenue in the future.<sup>185</sup> Currently, consumers have grown tired of paying such high prices as a result of the excise tax.<sup>186</sup> Lowering the excise tax will buck this trend.<sup>187</sup> An initial drop in tax revenue is likely after lowering the excise tax;

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with the *University of the Pacific Law Review*) (reporting a decrease in excise tax revenue from the third quarter of 2021 to the first quarter of 2023).

<sup>177</sup> *Id.*

<sup>178</sup> *Id.*

<sup>179</sup> *Marijuana Tax Reports*, COLO. DEP'T OF REVENUE, <https://cdor.colorado.gov/data-and-reports/marijuana-data/marijuana-tax-reports> (last visited July 15, 2023) (on file with the *University of the Pacific Law Review*) (reporting that Colorado generated over \$423 million in total cannabis tax revenue in 2021, but revenue decreased in 2022 to \$325 million).

<sup>180</sup> Katjusa Cisar, *Illinois and Michigan Again Earned Hundreds of Millions from Weed Taxes in 2022, Even More Than Previous Year*, BADGER PROJECT (Mar. 6, 2023), <https://thebadgerproject.org/2023/03/06/illinois-and-michigan-again-earned-hundreds-of-millions-from-taxes-on-weed-sales-in-2022-even-more-than-the-previous-year/> (on file with the *University of the Pacific Law Review*) (stating that Michigan imposes a ten percent cannabis excise tax); Christian M. Wade, *Pot Tax Revenue Getting Higher; Up 27%*, GLOUCESTER DAILY TIMES (Oct. 31, 2022), [https://www.gloUCESTERtimes.com/news/pot-tax-revenue-getting-higher-up-27/article\\_abff002c-57c8-11ed-b383-4352c98cd916.html](https://www.gloUCESTERtimes.com/news/pot-tax-revenue-getting-higher-up-27/article_abff002c-57c8-11ed-b383-4352c98cd916.html) (on file with the *University of the Pacific Law Review*) (stating that Massachusetts imposes a 10.75% cannabis excise tax).

<sup>181</sup> Cisar, *supra* note 180 (reporting that Michigan generated roughly \$325 million in tax revenue in 2022, a thirty percent increase from 2021's total).

<sup>182</sup> Wade, *supra* note 180 (reporting that Massachusetts generated \$225 million in cannabis tax in 2022, a twenty-seven percent increase from the previous year).

<sup>183</sup> Cisar, *supra* note 180 (reporting an increase in tax revenue generated); Wade, *supra* note 180 (reporting a year to year increase in tax revenue generated).

<sup>184</sup> Yakowicz, *supra* note 1 (“[T]he customer is tired of paying the exorbitant taxes and are now buying it from a friend of a friend or the guy on the corner.”).

<sup>185</sup> Cisar, *supra* note 180 (reporting an increase in tax revenue generated); Wade, *supra* note 180 (reporting a year to year increase in tax revenue generated).

<sup>186</sup> *Cannabis Tax Revenues*, *supra* note 176 (showing that the excise tax revenue has decreased since the second quarter of 2021); Yakowicz, *supra* note 1 (“[T]he customer is tired of paying the exorbitant taxes and are now buying it from a friend of a friend or the guy on the corner.”).

<sup>187</sup> Cisar, *supra* note 180 (showing that Michigan has able to increase tax revenue with a lower excise tax); Wade, *supra* note 180 (showing that Massachusetts has been able to increase tax revenue with a lower excise tax).

however, over time, it is more likely that tax revenue will begin to increase again.<sup>188</sup> With lower prices due to decreased taxes, more consumers will be inclined to purchase cannabis from the legal market instead of the illegal one.<sup>189</sup> Regulations require retailers to collect the excise tax directly from customers, so lowering this tax results in lower customer prices.<sup>190</sup> Combining these lower prices with the opportunity to serve food and drinks and host performances will further increase the strength of the industry and tax revenue.<sup>191</sup>

Lowering the excise tax for retailers that have consumption lounges also incentivizes businesses to establish lounges.<sup>192</sup> Businesses would experience all of the benefits that AB 374 proposes, as well as receiving a tax break.<sup>193</sup> Not only would it incentivize businesses to obtain the proper permits, but it would also incentivize local jurisdictions to grant them.<sup>194</sup> With local approval of consumption lounges, jurisdictions could receive the tax revenue benefits that come with it.<sup>195</sup> Retailers increasing their sales while maintaining optional local taxes would lead to an increase in local tax revenue.<sup>196</sup>

## V. CONCLUSION

AB 374 is a strong start to supporting struggling cannabis retailers and microbusinesses.<sup>197</sup> Although AB 374 does not contain excise tax reform that would significantly aid businesses, it still provides new opportunities for the industry.<sup>198</sup> California has been a leader in cannabis policy, and AB 374 continues the trend by modeling thriving cannabis industries.<sup>199</sup> Currently, businesses across the state are struggling and need support to keep their doors open.<sup>200</sup>

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<sup>188</sup> *Cannabis Tax Revenues*, *supra* note 176 (recording that the excise tax revenue increased from 2018 until the second quarter of 2021, then began to decrease).

<sup>189</sup> *Tax Guide for Cannabis Businesses*, *supra* note 26 (explaining that cannabis retailers and microbusinesses are responsible for collecting the excise tax from customers); Sheeler, *supra* note 93 (stating that local restrictions and high taxes contribute to the illegal market's strong presence).

<sup>190</sup> *Tax Guide for Cannabis Businesses*, *supra* note 26 (explaining that cannabis retailers and microbusinesses are responsible for collecting the excise tax from customers).

<sup>191</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 3 (May 18, 2023) (identifying the benefits of AB 374) (stating that AB 374 “allow[s] small cannabis retailers to diversify their business” increasing business revenue and as a result, tax revenue).

<sup>192</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 2 (May 18, 2023) (noting that retailers need local approval to establish consumption lounges).

<sup>193</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 3 (May 18, 2023) (listing the option to prepare food and drinks, as well as sell event tickets as benefits for businesses).

<sup>194</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 2 (May 18, 2023) (noting that retailers need local approval to establish consumption lounges).

<sup>195</sup> *Cannabis Business Operation Tax*, *supra* note 91 (providing that the City of Sacramento requires retailers to pay an additional four percent in business tax).

<sup>196</sup> *Id.* (providing that the City of Sacramento requires retailers to pay an additional four percent in business tax).

<sup>197</sup> See ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 3 (May 18, 2023) (identifying that cannabis businesses in California are struggling).

<sup>198</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 1 (May 18, 2023) (providing details of AB 374).

<sup>199</sup> Baldassare et al., *supra* note 28 (detailing California's past marijuana policies).

<sup>200</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 3 (May 18, 2023) (identifying that cannabis businesses in California are struggling).

At a minimum, AB 374 is a realization that cannabis businesses are failing, as well as the industry.<sup>201</sup> Allowing retailers to prepare and serve fresh food and drink, as well as sell performance tickets, is an effective start to turning the industry around.<sup>202</sup> Retailers and microbusinesses can improve upon their business model with new experiences for consumers.<sup>203</sup> Without AB 374 and further aid from the California Legislature, cannabis businesses will fail to see many of the benefits they were promised by California when the legal industry was established.<sup>204</sup>

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<sup>201</sup> Yakowicz, *supra* note 1 (detailing the reality of struggling cannabis businesses in California).

<sup>202</sup> ASSEMBLY FLOOR, FLOOR ANALYSIS OF AB 374, at 3 (May 18, 2023) (providing details of AB 374).

<sup>203</sup> SENATE COMMITTEE ON BUSINESS, PROFESSIONS AND ECONOMIC DEVELOPMENT, COMMITTEE ANALYSIS OF AB 374, at 1 (June 26, 2023) (listing details of AB 374 and how it benefits cannabis retailers and microbusinesses).

<sup>204</sup> See Sheeler, *supra* note 93 (noting that Proposition 64 was intended to “generate massive revenue, while decreasing illicit cannabis,” but businesses have not seen these benefits).

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