

# Tier 1 Cultivator License Solutions

Provided for: Vermont Cannabis Control Board

Tuck School of Business at Dartmouth



# The Vermont CCB can make a sizable impact with \$900,000 in funding

## Current State of the Industry

- Tier 1 cultivators are struggling to build profitable business in current competitive market
- Average costs to operate in Vermont showcase the financial burden cultivators face today
- Three themes have surfaced that burden cultivators' longevity in the business

## Cultivator Feedback

- Key takeaways from survey and 1:1 interviews highlight common challenges amongst the Vermont cannabis industry
- Financial cost-analysis of operating a standard Tier 1 farm reveal the barriers to operate
- Administrative and operational inefficiencies deter business success

## Our Solution

- \$900,000 will solve widespread challenges for the Tier 1 cultivators, appealing to key pain points
- Cost analysis justifies \$900,000 when looking at long-term advantages for overall Tier 1 farmers
- An alternative 'a la carte' financing option will create customized solutions pending legislation's budget

# **Current State of Tier 1 Cultivators**



# Tier 1 cultivators are struggling to build profitable business in current competitive market

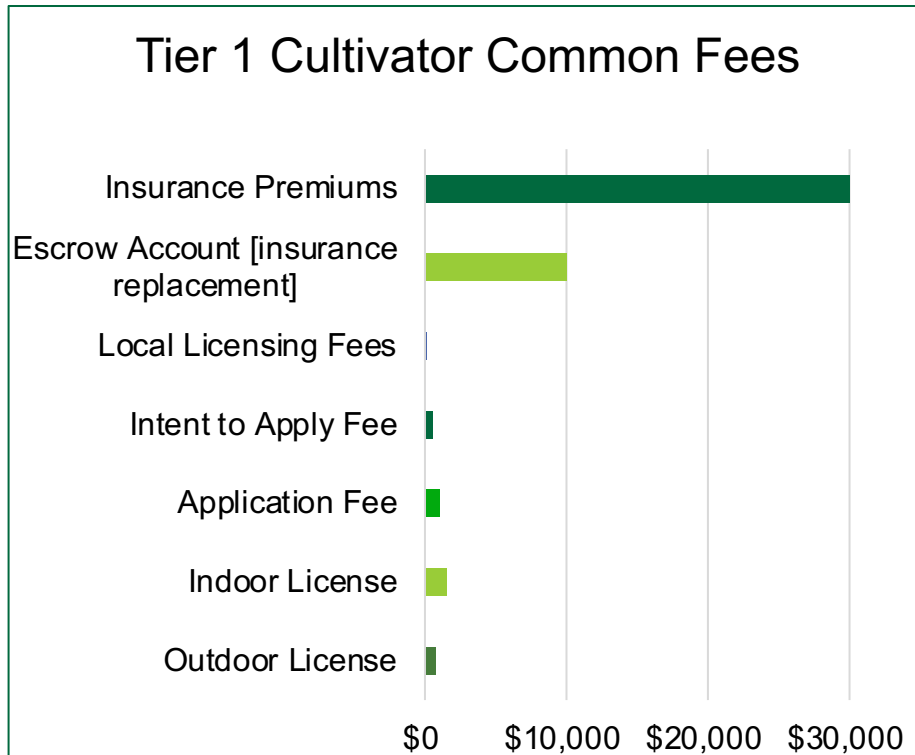
- Tier 1 cultivators face significant entry barriers; startup costs range from **\$250,000-\$1,000,000**
- Market entry is further complicated by limited funding options and lack of bankruptcy protection
- Lack of education surrounding business operations, tax requirements and profitability projections create negative business environment for growers

## **Federal Taxes** present the largest challenge for Tier 1 Cultivators

- **Income Taxable:** Cannabis businesses are required to pay federal income tax despite the federal illegality of cannabis.
- **No Deductions Under 280E:** They cannot deduct most ordinary business expenses due to IRC 280E restrictions.
- **Deductible COGS:** Cost of Goods Sold (COGS) can be deducted, reducing gross income for tax purposes.
- **Higher Tax Rates:** Effective tax rates can be higher as they're often taxed on gross income, not net income.
- **Cash Flow Impact:** Limited deductions affect profitability and cash flow, posing financial challenges.
- **Schedule I Classification:** Federal classification as Schedule I under the CSA influences tax obligations.
- **Compliance Importance:** Thorough record-keeping and working with tax professionals are crucial for compliance.
- **IRS Guidance:** The IRS provides resources and guidance for cannabis businesses on tax compliance.

# Average costs to operate in Vermont showcase the financial burden cultivators are facing

- Licensing fees range from **\$750-\$2,250**, with a \$1,000 one-time application fee and other associated costs.



- ### Other Variable Costs:
- Real Estate:** Cost depends on location and size of the operation.
  - Equipment and Supplies:** Includes lighting, irrigation, climate control, and growing supplies.
  - Compliance and Legal Fees:** Fees for legal advice on compliance and business structure.
  - Labor Costs:** Salaries for employees, depending on the scale of operations.
  - Insurance:** Coverage for crop failure, liability, and property damage.
  - Utilities:** Significant expenses in electricity and water, particularly for indoor growing.
  - Federal, State, and Local Taxes:** Various state and local taxes related to cannabis businesses, which can include sales tax, excise tax, and local business taxes.

# Administrative and operational inefficiencies deter business success

## Current Roads Funding

The existing allocation of **\$150,000** from the CCB Development Fund to Roads Consulting Group for technical assistance is a step towards addressing below challenges but is **not sufficient**.

### Complex Regulatory Environment

- Cultivators must navigate a complex landscape of frequently changing cannabis regulations
- The burden of compliance without sufficient guidance impedes operational efficiency

### Zoning & Development Challenges

- Zoning restrictions and development review board processes delay and deter business operations
- Need clearer guidelines and communication channels for cultivators in navigating local zoning laws

### Insufficient Specialized Support

- Shortage of industry-specialized service providers in areas such as legal and marketing
- Essential services like banking and insurance are costly, fraudulent and scarce due to federal status of cannabis

### Gaps in Technical and Marketing Support

- Cultivators can't market products like other agricultural industries and do not have other outlets to showcase products
- Cultivators need hands on support in areas like product quality control and post-harvest processes

### Business Scaling Challenges

- Challenges in scaling operations to market demands due to lack of strategic guidance
- Need for programs that assist cultivators with supply chain management and growth planning

### Legacy Market Access & Competition

- Tier 1 cultivators are competing with a legacy market that offers higher profits without the regulatory burden
- Need for incentives and streamlined regulations to make the legal market more attractive than the legacy market

# Financial cost-analysis of a standard Tier 1 farm reveal the barriers to operate

Key Components	Costs	Impact
<b>Operating &amp; Start-up</b>	<ul style="list-style-type: none"><li>• Initial start-up costs</li><li>• Licensing fees</li><li>• Product registration</li></ul>	<ul style="list-style-type: none"><li>• Changing regulations &amp; license renewal requires additional time expense</li><li>• Registration creates additional bottleneck</li><li>• Cultivators spend more time reviewing paperwork</li><li>• Product sits on shelf for longer, diminishing quality</li></ul>
<b>Banking &amp; Financial Services</b>	<ul style="list-style-type: none"><li>• Business bank account</li><li>• Insurance</li></ul>	<ul style="list-style-type: none"><li>• \$500 startup account fee</li><li>• \$50/month account fee</li><li>• \$2,000-\$5,000 insurance premium</li><li>• Additional burdens for cultivators</li></ul>
<b>Testing &amp; Compliance</b>	<ul style="list-style-type: none"><li>• Product testing fees</li><li>• Pathogens tested</li><li>• Employee ID cards</li></ul>	<ul style="list-style-type: none"><li>• Quarterly testing fees</li><li>• Testing bottleneck diminishes quality</li><li>• Loss of product if fail</li><li>• Creates inaccurate security blanket</li><li>• Craft product loses differentiation</li></ul>

# Feedback from Cultivators



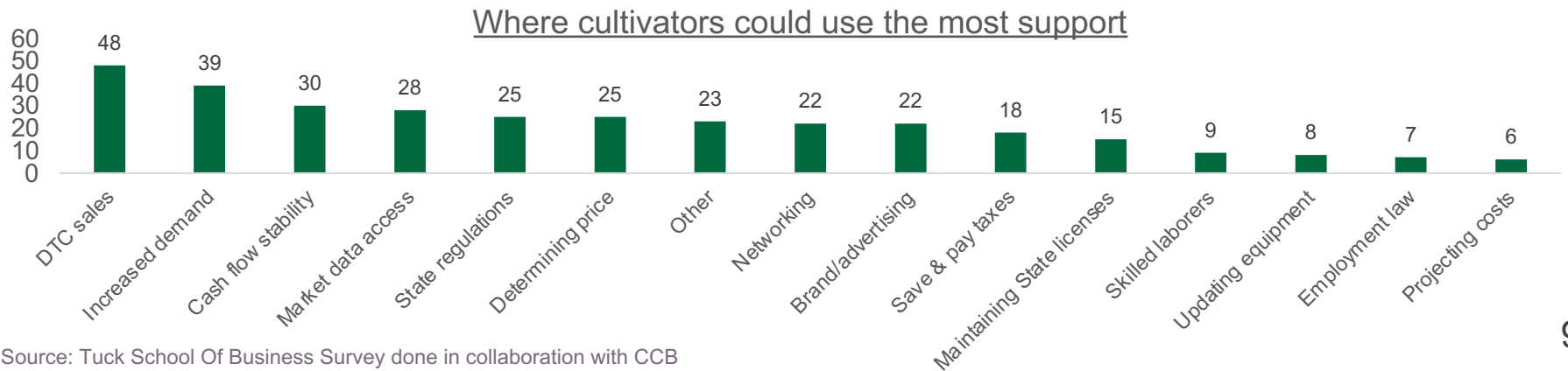
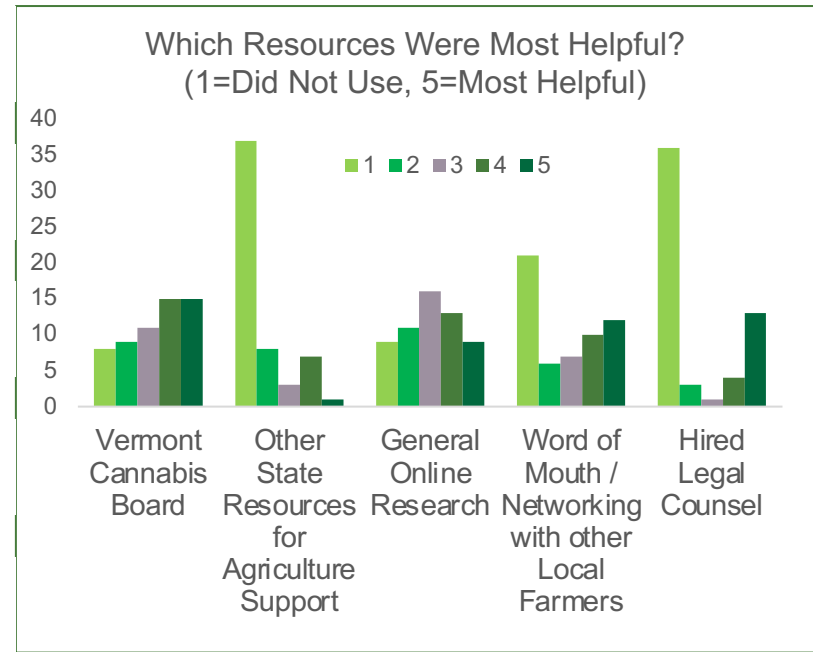


# Key takeaways from survey and 1:1 interviews highlight common challenges in the cannabis industry

Updated as of 05/15

**We collected 106 responses to the survey and conducted 12 interviews**

- 44%** Indicated that start-up costs >\$30,000
- 47%** Hired legal representation to assist in applying and maintaining the license which cost most between \$2,000-\$5,000
- 70%** Responded that it took more than 6 months to research, apply for a license and get the business up and running
- 45%** Said they only use 50-60% of their allocated plant canopy because they are understaffed, or it is not profitable
- 77%** Make a yearly profit of less than \$50,000



# Surveys and interviews of tier 1 cultivators show frustration but hope for the market in Vermont



“

I think we need way more support at the beginning of the process.

”



“

State laws seemed to change constantly. It made some things easier but was hard to keep up with the changes.

”



“

We would value logistical assistance with the application process, legal guidelines, testing requirements, costs and expectations.

”



“

Many of us may return to the legacy market. It's infuriating having people offering to buy my entire crop in the legacy market yet being unable to find buyers in the legal market.

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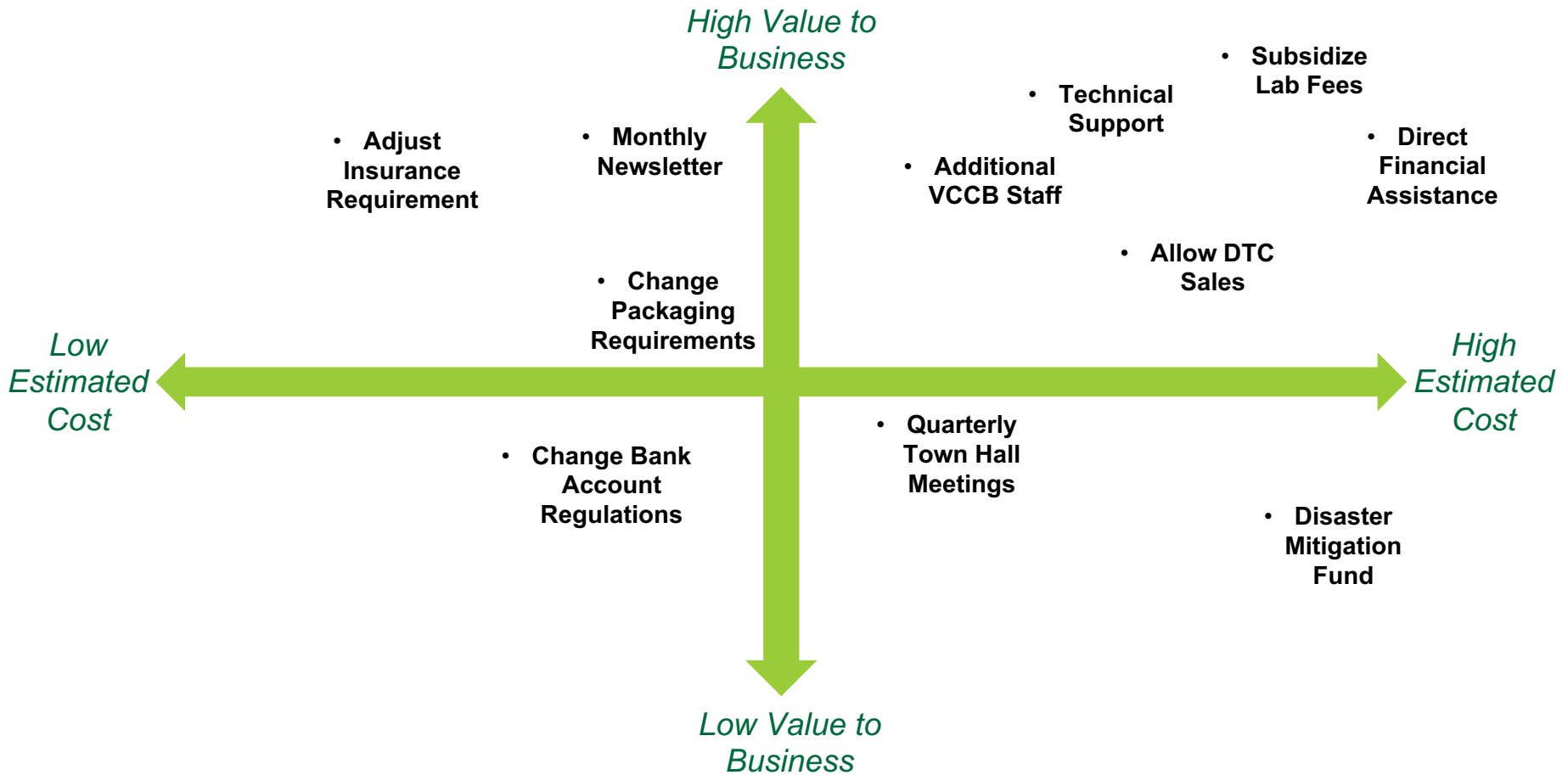
### 3 main pain points burden cultivators' longevity in the business

In Scope		Out of Scope
Financial Burden	Administrative & Operational Support	Price Chasing Environment
<ul style="list-style-type: none"><li>• <b>Regulatory Complexity:</b> Navigating business taxes, banking, and regulatory understanding is the most challenging aspect.</li><li>• <b>High Initial Costs:</b> Acquiring the right farming equipment, insurance, and banking services are the most significant expenses.</li><li>• <b>Funding Sources:</b> Nearly all respondents used personal savings, contributions from family and friends, or loans to finance their businesses.</li><li>• <b>Widespread Discrimination:</b> 90% of business owners report facing discrimination when seeking financial services due to the cannabis-related nature of their business.</li></ul>	<ul style="list-style-type: none"><li>• <b>Educational Gap:</b> Newcomers often dive into the industry without a full grasp of the agricultural and operational aspects</li><li>• <b>Complex Financial Landscape:</b> The financial aspects — from taxes to banking — and complex compliance reporting are the most daunting and time-consuming part of the process.</li><li>• <b>Bureaucratic Hurdles:</b> The process of licensing is laden with paperwork, often underestimated by applicants, leading to unexpected delays and frustrations.</li><li>• <b>Consultancy and Support Flaws:</b> Experiences with consultancy firms like Roads Consulting have sometimes been unsatisfactory, and there's a noted trend of not fully leveraging external support for licensing paperwork, resulting in lost opportunities and resources.</li></ul>	<ul style="list-style-type: none"><li>• <b>Competitive Market:</b> The recent surge in licenses has saturated the market, causing a drop in prices and challenging profitability.</li><li>• <b>Grower Hardship:</b> Economic pressure is mounting for growers, with many not drawing income for months.</li><li>• <b>Industry Risk:</b> The hemp industry's decline in Vermont raises concerns about a possible downturn in the cannabis sector.</li><li>• <b>Licensing Disparity:</b> The tiered licensing system is under scrutiny for potentially disadvantaging small businesses.</li><li>• <b>Marketing Hurdles:</b> Restrictions on marketing compound the difficulties facing cannabis businesses.</li></ul>

# **Solutions for the Vermont CCB**



# Cost-impact evaluation for cultivator support options



# There is opportunity for the CCB to leverage its lab testing requirements to improve the current cultivator market



## Market Longevity

- Vermont's history and reputation as an agriculture stronghold should be leveraged to bolster the cannabis industry
- The VCCB should aim to support the 'good players' and allow for natural attrition of weaker businesses an industry correction for well run businesses to prosper
- Local VT cheese and craft beer breweries can serve as models for the VCCB. The VCCB targets their budget towards improving organizational health, professional education, business support, and industry sustainability

## Artificial Selection

- Current testing regulations allow cultivators to select the sample that will be evaluated. This creates the potential for a selection bias and compromises the quality of the testing.
- Testing requirements & product registration regulations have forced cultivators to scale back on plant genetic experimentation, limiting innovation of new strands in the market

## Lab Testing Solutions

- The VCCB should invest resources in a state-run lab to supplement the private labs
- There should be a focus on timely, reliable testing solutions by the state-run lab
- Cultivators experimenting with new strands of cannabis should be eligible for small grants to continue to grow the industry

# Strategic fund allocation to empower tier 1 cannabis cultivators

Type	Cost	Impact
Financial Lending and Assistance	\$550,000	<ul style="list-style-type: none"> <li>• Cannabis businesses face significant challenges with obtaining funding as there are very limited banking and lending services available due to Cannabis being a Schedule 1 controlled substance at the federal level                             <ul style="list-style-type: none"> <li>○ Most licensees are largely self-funded</li> </ul> </li> <li>• Financial support in the form of loans and grants via the Cannabis Business Development Fund has been limited to social equity applicants</li> <li>• Low-interest loans, grants, and subsidized testing fees made available to Tier 1 licensees will help cannabis businesses reduce expenses, cover operational costs, and offers a source of funding in lieu of traditional lending sources</li> </ul>
Technical Support	\$300,000	<ul style="list-style-type: none"> <li>• For small scale Tier 1 cultivators, achieving profitability remains a challenge, particularly since direct-to-consumer sales is not possible without a retail license</li> <li>• Through the Cannabis Business Development Fund, only eight social equity businesses received technical support in 2022 from the Roads Consulting Group in the following areas: marketing, bookkeeping, website development, financial management, and branding logo/design</li> <li>• Expanding this technical support to a greater number of licensees will assist them towards improving their business practices to enhance demand and reduce costs</li> </ul>
Training and Workshops	\$40,000	<ul style="list-style-type: none"> <li>• Many cultivators have cited maintaining state licenses and keeping up with state regulations as challenges</li> <li>• Training and workshops on regulatory changes and different facets of running a business will allow licensees to stay up to date on regulations and best business practices</li> </ul>
Networking Events and Townhalls	\$10,000	<ul style="list-style-type: none"> <li>• Many cultivators also cited need for more networking opportunities with other licensees</li> <li>• Networking events and townhalls provides licensees an opportunity to share concerns with the CCB and connect with other cultivators to learn best industry practices</li> </ul>

**Total**    **\$900,000**

# Additional information on the implementation of CCB initiatives

- Tier 1 cultivators are taking on significant risk to enter Vermont's legal cannabis market as most licensees are completely self-funded, using their 401ks or taking out a mortgage
- Cultivators are facing increasing competition in a highly saturated market due to the rising number of licensees
- It has also become a challenging environment for small cannabis businesses to compete with larger Tier 3-5 cultivators who have greater access to external funding
- Additional support is required for Tier 1 cultivators to ensure they don't return to the legacy market where they were able to charge lower prices and earn higher margins by avoiding taxation as well as testing, product registration, and licensing fees

## Financial Assistance

Low interest loans for Tier 1 cultivators provide a sustainable source of lending

Grants to provide the financial support necessary for small businesses to overcome initial start-up costs

Subsidized laboratory fees for Tier 1 cultivators gives them greater opportunity to compete with larger cultivators

## Technical Support / Training

Financial Management – Accounts reconciliation, preparation and analysis of P&L statements, balance sheets, expense reports, and aging reports

Brand Management – Logo design, promotion and advertising

Digital Marketing – Web development and design, social media

Legal and Regulatory Assistance

## Networking and Townhalls

Townhalls present an opportunity for cultivators to share feedback face-to-face with the CCB

Networking events helps unify the growing industry and creates a channel for information sharing

To create a “craft cannabis” culture in the state, an integrated approach to cultivation, sales, and regulation is necessary in the long-term.



# Leveraging practices used across dairy and craft beer industries, the Vermont brand has opportunity to prop up the cannabis market factors

Vermont's strong reputation is based off its high-quality, organic, and often artisanal products. The state uses this as a differentiator for the products it produces, establishing a market around key products such as dairy (cheese) and craft beer.

## Marketing & Brand:

- **Tourism Campaigns:** Vermont includes its breweries and cheesemakers in tourism advertisements, attracting visitors who are interested in food and drink experiences.
- **Events and Festivals:** The state supports and publicizes events such as beer festivals and cheese tasting events, which serve to highlight local producers and their products.
- **Digital and Social Media Marketing:** Through digital marketing and social media, Vermont promotes its cheese and beer industries to a broader audience, emphasizing the quality and uniqueness of its products.

## Tourism and Agritourism:

- **Authenticated Partnerships:** Partnerships promote tourism and agritourism, attracting visitors to its picturesque farms, breweries, and creameries
- **Local and Organic Food Movements:** Vermont is known for its strong local and organic food movements. This ethos encourages the production and consumption of locally-sourced and organic ingredients. The demand for organic products in turn supports higher price points and market differentiation.

## Community Oriented Culture:

- **Collaboration Among Producers:** For example: breweries and cheese makers might collaborate on events or pairing that showcase how well their products compliment each other. This unique Vermont experience appeals to connoisseurs and casual customers alike, while creating innovation in the products.
- **Collaboration Among Local Businesses:** Vermont encourages local businesses to collaborate in promotions and marketing efforts, which often include cross-promotions involving both cheese and beers

The screenshot shows a news article on the 'Better News' website. The article is titled 'How a craft beer collaboration helped Vermont Public Radio grow audience and revenue' and is categorized under 'DIVERSIFYING REVENUE'. The author is Angela Evancie, and the article was published in March 2022. The article text begins with 'Here's an idea to steal and adapt: What does your target audience like...to drink? When the Vermont brewery Lawson's Finest Liquids approached Vermont Public Radio about a craft beer in honor of the station's award-winning narrative podcast, VPR saw an opportunity to reach new'.

# Appendix



# Works Cited

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(Lab testing and Inventory tracking guidance – lab testing can be costly for some, we are happy to connect you with one of the labs to discuss pricing, or it could be a question to add to your list when talking with licenses).

[https://ccb.vermont.gov/sites/ccb/files/2022-12/Inventory.Tracking.Labs\\_Guidance\\_FINAL.pdf](https://ccb.vermont.gov/sites/ccb/files/2022-12/Inventory.Tracking.Labs_Guidance_FINAL.pdf)

(Tax Compliance Guidance)

<https://tax.vermont.gov/business/cannabis-excise-tax>

(Insurance FAQ)

[https://ccb.vermont.gov/sites/ccb/files/2024-03/CCB%20Cannabis%20Insurance%20FAQ\\_3.13.24.pdf](https://ccb.vermont.gov/sites/ccb/files/2024-03/CCB%20Cannabis%20Insurance%20FAQ_3.13.24.pdf)

(Fee Guidance)

[https://ccb.vermont.gov/sites/ccb/files/2023-11/Fee.Schedule.Guidance\\_FINAL\\_0.pdf](https://ccb.vermont.gov/sites/ccb/files/2023-11/Fee.Schedule.Guidance_FINAL_0.pdf)

(Fee Structure Report)

[https://ccb.vermont.gov/sites/ccb/files/2021-11/Vermont\\_CCB\\_Report\\_Oct\\_15\\_2021-1.pdf](https://ccb.vermont.gov/sites/ccb/files/2021-11/Vermont_CCB_Report_Oct_15_2021-1.pdf)

(Summary of Continuing Barriers to entry for Social Equity, License App Data, Number of Loans and Grants)

[https://ccb.vermont.gov/sites/ccb/files/2023-09/1.15.23\\_CCB.SE\\_Report.pdf](https://ccb.vermont.gov/sites/ccb/files/2023-09/1.15.23_CCB.SE_Report.pdf)