Excise Tax Survey Results

September 2023

“Taxes on cannabis will be kept low to support the objectives of its legalization: keeping it out of the hands of youth, and profits out of the hands of criminals.”

~ Federal-Provincial-Territorial Agreement on Cannabis Taxation

2017

2023 Excise Tax Survey

In 2022, C3 issued a report on *Economic Analysis of the Cannabis Excise Duties, Mark-Ups and Fees* to analyse the overall effects of regulation and taxation on the cannabis industry in Canada. The report assessed the impact of taxation and compliance costs on the legal industry's ability to compete effectively with unregulated and untaxed contraband products and thereby achieve the objectives of the Cannabis Act.

One year later, the industry is marred with closures and consolidation, with Licensed Cultivators and Processors widely reporting an inability to be generate profitability and positive cash flow.

In 2023, C3 surveyed Licensed Parties (LPs) of all sizes across the country to understand the financial health of cultivators and processors of cannabis today. The survey was conducted online, with responses provided anonymously.

122 survey responses were collected between August 15 and September 7, 2023.

Survey Highlights

LPs paid 20-35% excise tax
in 2022
(% of gross sales)

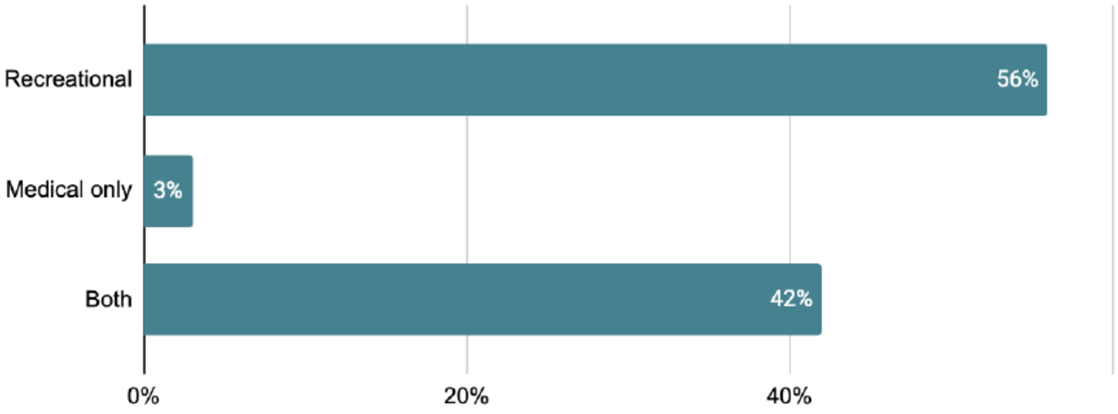
83% reported negative net income
in 2022

73% reported negative EBITDA
in 2022

71% reported increase in excise rate
in 2022 vs 2021
(% of gross sales)

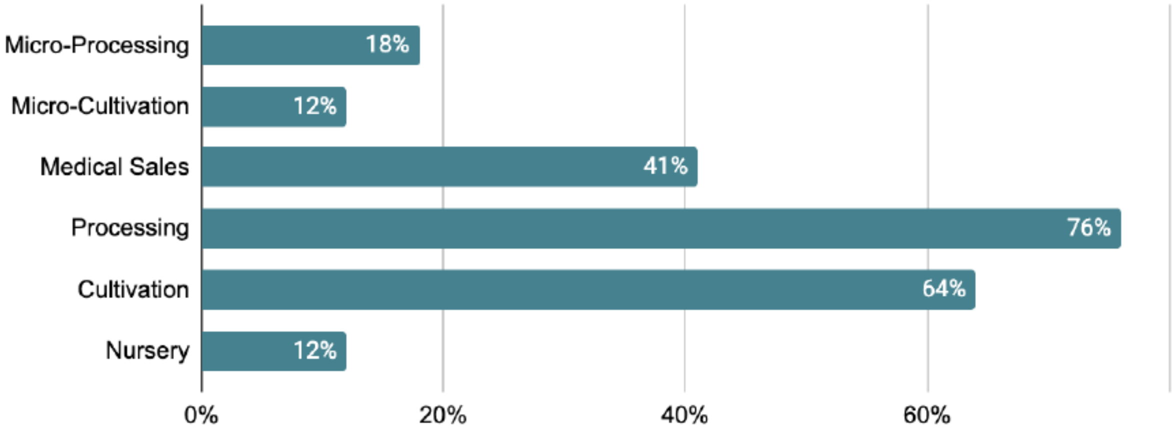
Respondent Profiles

Licence Type



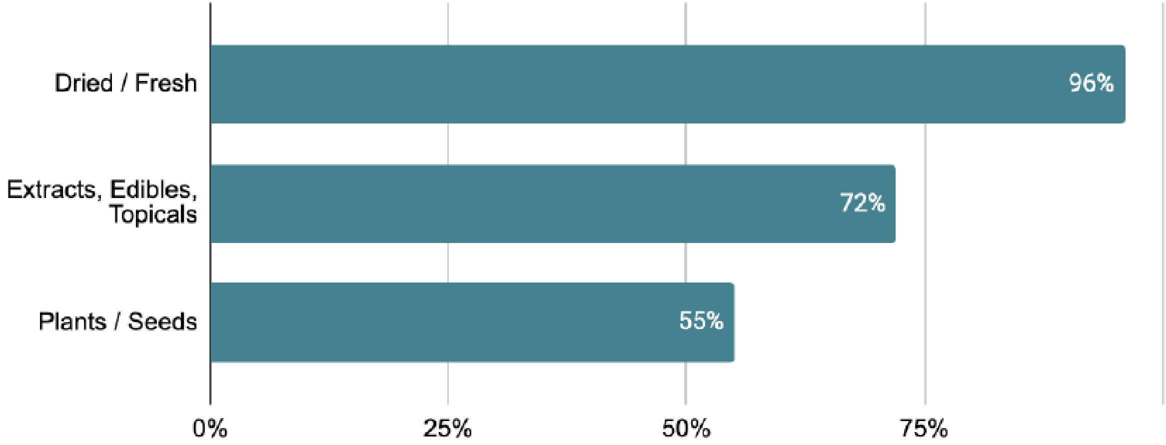
Respondent Profiles

Licence Category



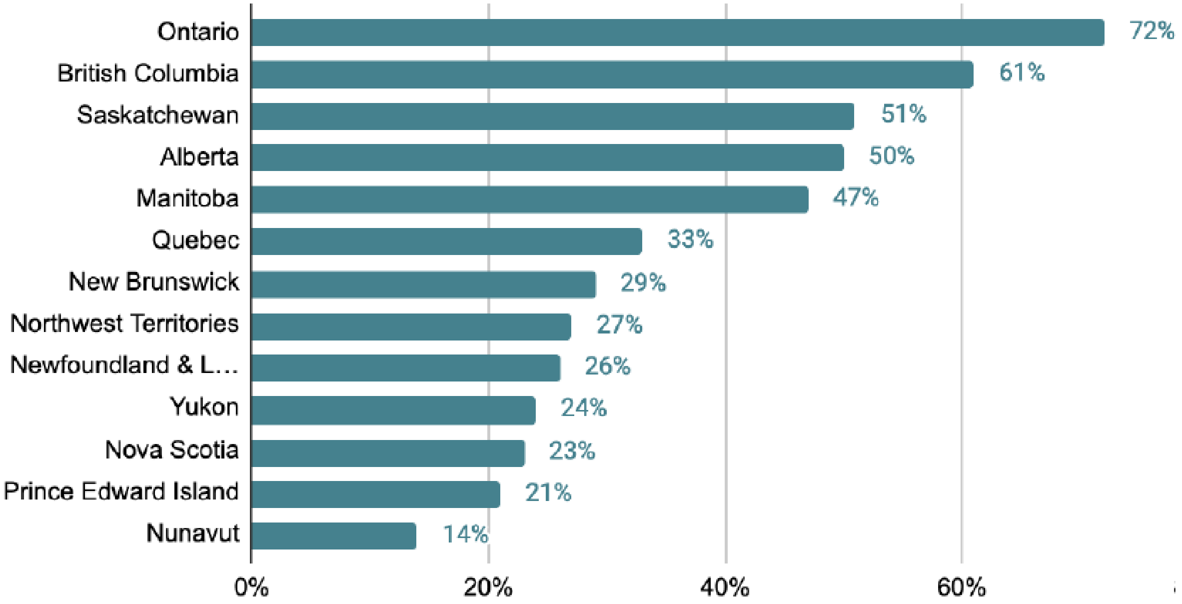
Respondent Profiles

Authorized to Sell



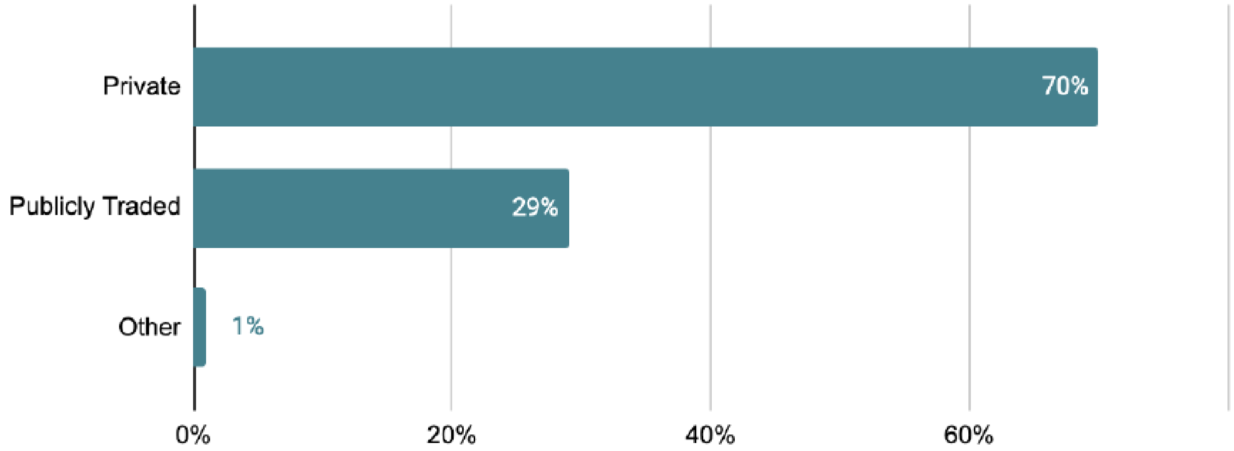
Respondent Profiles

Location of Operations



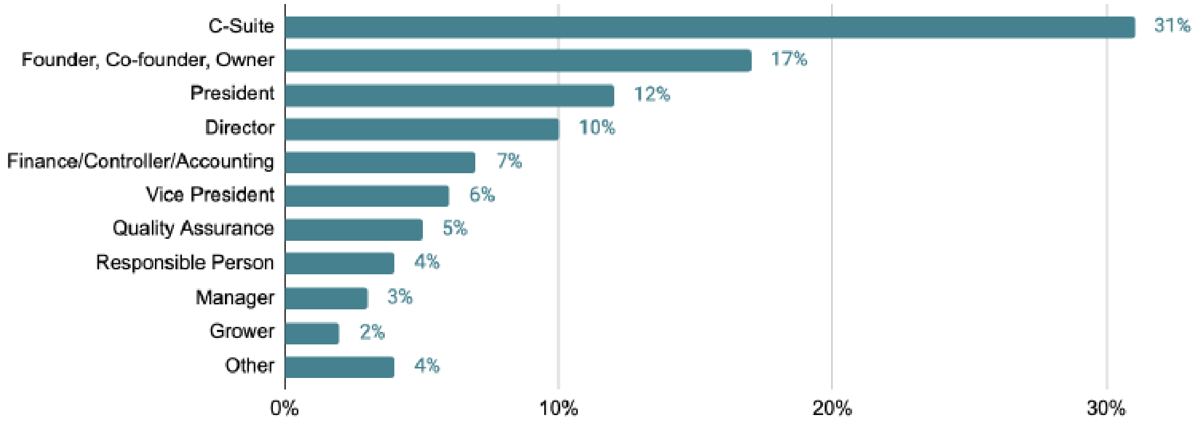
Respondent Profiles

Company Ownership



Respondent Profiles

Job Title



State of Excise

High taxation on a nascent sector battling an entrenched illicit market puts LPs in crisis.

96% of respondents view the current excise tax model as excessively punitive on their business.
(Average: 4.76/5)

Why?

Rate is too high
Disproportionate across products/provinces
Cash flow / profitability issues
Complexity of administration
Lack of government support
Inability to compete with illicit market

"Canada's tax policy for cannabis was built around an egregious miscalculation of long-term wholesale price. The excise formula was created by policymakers who expected wholesale prices for flower - the most popular consumer segment - to be at least $10 per gram. Instead, actual prices are less than $1 per gram in some cases, leaving almost no margin for licensed producers. The original estimation of $10 per gram wholesale price has never been close to reality, and LPs are buckling under the weight of a tax burden that often extracts 30% of top-line revenue."

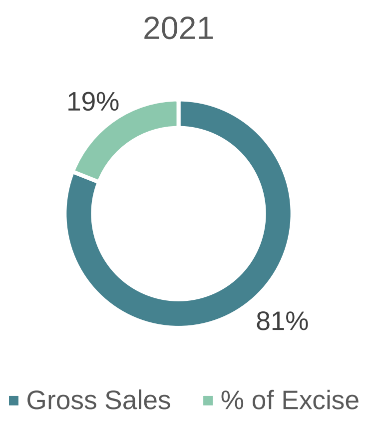
"At the current rate of tax our business is non-viable"

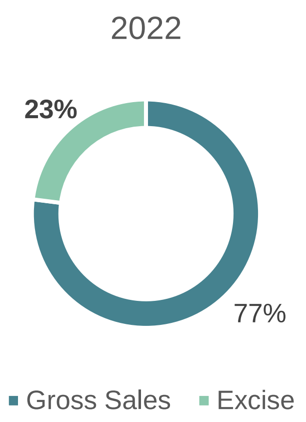
State of Excise

Excise continues to represent a higher percentage of LP's gross sales year over year.

71% of respondents saw an increase in the rate of excise they paid in 2022 from 2021, moving from an average of $5.6M to $8.4M in 2022.

Respondents produced and sold similar KGs of flower in 2022 as in 2021. (13% more in 2022 on average)





"In fiscal 2020, excise tax was 16% of revenue. In fiscal 2023, it is 30%. In Q4 2023, it is expected to be 35%. This is unsustainable (not to mention illogical as it's based on a $/g formula, and prices have been steadily compressing)"

"The tax structure does not scale with consumer pricing or preference. If price goes up, absolute excise dollars should go up. If price goes down, Absolute excise dollars should go down! If consumers shift their preferences to extracts, then the tax structure should adapt."

Financial Viability

LPs are working hard to reduce costs and improve cash flow but continue to remain unprofitable.

83% of respondents reported negative net income in 2022, decreasing by 5% from 2021.

Respondents reported an average net income of -$21.6M in 2022, decreasing slightly from 2021 at -$24.3M.

62% of respondents reported negative cash flow in 2022, increasing by 12% from 2021.

Respondents reported an average cash flow of $0.60M in 2022, showing a great improvement from 2021 at -$89.1M.

73% of respondents reported negative EBITDA in 2022, increasing by 16% from 2021.

Respondents reported an average EBIDTA of -$2.0M in 2022, declining significantly from 2021 at $0.66M.

State of Excise

LPs can't afford not to keep the majority from any potential excise tax reform.

Respondents said they would keep an average of 82% of the difference if the government decreased excise tax, with 11% flowing through to reduce the amount consumers pay at retail.

57% of respondents said they would keep all or almost all of the decrease. 23% would keep 50-90%

They would use any extra funds for:

- Personnel and hiring
- Debt repayment
- Research and development
- Capital improvements and equipment
- Working capital and overhead costs

"About 50% of savings would simply allow us to become more profitable, generate more cash flow to operate with fewer financial constraints, we would use some for purchasing bulk & raw materials (to have more safety stocks), some equipment purchases for operations efficiencies"

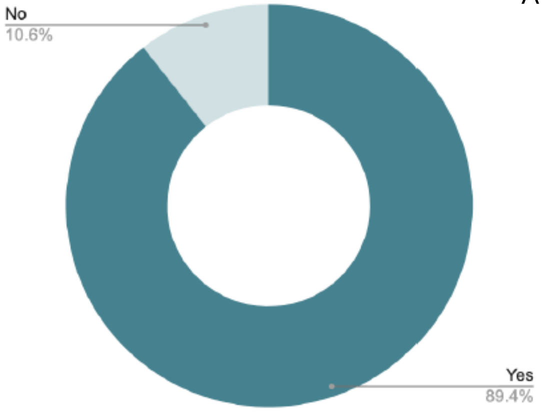
"We had to abandon our status as a living wage employer this year because we can't afford to pay our staff enough. Our senior leaders took a massive pay cut to try and keep the company afloat. All of the funds would be reinvested in retaining talent and paying down debt. We'd also be able to stay current with excise if it was within the realm of reasonable (e.g. 10% or less of topline sales)"

Stamp Operations

Excise stamps are overly complex and expensive to administer.

89% of respondents say the current excise stamp model is expensive to operationalize

Why? Additional resources required for staff, administration, tracking, reporting
Specific issues around different stamps for each province, delays in ordering
Inventory management difficulties
A single stamp would streamline operations



"Stamping labor and overhead costs us approximately $0.17/stamp, which is on top of the $0.07 cost per stamp. Given the inefficiency of being required to have physical stamps, there is significant labor needed in order to ensure proper application of the stamps to comply with regulations. If we moved to a laser printed stamp there would be significant labor savings and less room for error."

"We struggle with inventory and moving quickly if one province changes their POs and demands shift"

"Let us buy more than 3 months' worth of stamps so we stop running out (e.g., even 6 months would help smooth ordering and avoid gaps in stamp availability)" "We could hold less inventory and be faster with sales"

"Reduced complexity of preparing shipments if a single stamp can be used for each province."

"Lower error rates."

Addendum: Excise Tax Webinar Survey Results

40 LPs reviewed early results from the Excise Tax Survey and were polled on a number of additional issues.

95% of LP respondents say government has not achieved the objectives of legalization.

Keeping cannabis out of the hands of youth, and profits out of the hands of criminals.

Only 31% of LPs anticipate being profitable in 2023.

64% of LPs say excise tax reform would make the largest positive impact on their business.

National excise stamp:	36%
Regulatory fee:	31%
Provincial markups:	26%
Labelling restrictions:	15%
Standardized testing:	15%
Administrative burden:	13%
Enhanced distribution:	10%
Other:	3%

84% say moving to one national excise stamp would reduce costs and complexity for their business.

With 16% saying it might.

“The industry is attempting to offer safe, world-class cannabis products to the market. With this offer comes expensive inputs, operating costs, and costs of capital. On top of that, there is an additional cost on producers to maintain compliant operations and there are very restrictive marketing landscapes, making for a difficult path to profitability for any cannabis producer. As one of the first countries to legalize cannabis, the Canadian government needs to nurture the industry players that are working hard everyday to offer safe, world-class cannabis products to the market. With the high-cost expenses listed above, venturing producers are at-risk of financial failure, therefore, a high excise duty tax critically impedes the nurturing and growth of Canada's new industry potential.”

~Anonymouse LP respondent