



Legislative Fiscal Bureau

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Joint Committee on Finance

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Industrial Hemp Program Staff (Agriculture, Trade and Consumer Protection – Regulatory Programs)

[LFB 2021-23 Budget Summary: Page 67, #6]

CURRENT LAW

The federal Agricultural Act of 2014 legalized the cultivation of industrial hemp under certain circumstances, and cultivation was further expanded under the federal Agricultural Improvement Act of 2018. Under the federal authorization, Wisconsin established its own industrial hemp program under 2017 Wisconsin Act 100, and administrative code Chapter ATCP 22. Further changes were made to the program under 2019 Wisconsin Act 68. Under Wisconsin law, industrial hemp is defined as the plant *Cannabis sativa* that has a tetrahydrocannabinol (THC) concentration of less than 0.3% by weight. The Department is responsible for licensing and conducting a criminal background check on all growers and processors, and for sampling and testing cultivated hemp to ensure it complies with the THC limit.

The U.S. Department of Agriculture (USDA) is responsible for implementing federal regulation of hemp cultivation. As hemp cultivation has been incrementally legalized over time, USDA has promulgated successive rules to establish requirements for states operating hemp programs. Effective December 31, 2021, state hemp pilot programs (including Wisconsin's) authorized under the original 2014 law expire, and states must implement a new permanent hemp program, as approved by USDA, effective January 1, 2022.

Hemp growers must pay a license fee of \$150, or \$5 per acre up to \$1,000, whichever is greater. Once licensed, growers pay annual registration fees equal to \$350. DATCP charges growers for required testing at a rate of \$250 per sample collected, which is intended to cover the actual cost of sampling and testing. Each individual field and variety of hemp requires a separate sample, meaning growers may pay for several samples. Additionally, beginning in the 2021 growing season, growers may pay a fee of \$200 to retest a sample, or \$300 to resample and test a remediated field. Remediation is when a hemp field tested above the THC limit, but THC-

containing components of plants were destroyed, allowing a grower to salvage remaining portions of a plant. DATCP is also responsible for regulating hemp processors, who pay an initial license fee of \$150, and an annual registration fee of \$100.

DATCP first operated its hemp program during the 2018 growing season. In the first season, 180 growers registered with DATCP to plant approximately 1,900 acres. In 2019 and 2020, approximately 1,250 growers registered to plant 4,500 and 5,400 acres, respectively. For 2021 through May 5, 549 growers have registered with DATCP. It is expected most all growers for the 2021 season have already registered with DATCP, which represents a 56% decline relative to 2020. Annual processor registrations totaled 78, 562, 619, and 340, for 2018 through 2021 as of May 5, respectively.

DISCUSSION POINTS

Appropriation Condition

1. As seen in the table, the hemp program appropriation is anticipated to close with a negative balance of approximately -\$450,000 on June 30, 2021. As a result, the appropriation will be in overdraft and draw against the balance of the general fund until revenues are sufficient to recoup previous costs. The overdraft represents an imbalance in revenues and expenditures caused by a number of factors: (a) significantly lower participation during the 2021 growing season; (b) recurring costs related to program development; and (c) increasing staff and operations costs.

Hemp Regulation Appropriation Condition

	<u>2017-18</u>	<u>2018-19</u>	<u>2019-20</u>	<u>2020-21*</u>
Opening Balance	\$0	\$3,500	\$307,000	\$292,700
Revenues	114,700	775,900	1,171,800	695,800
Expenditures	<u>-111,200</u>	<u>-472,400</u>	<u>-1,186,100</u>	<u>-1,445,800</u>
Closing Balance	\$3,500	\$307,000	\$292,700	-\$457,300

*Estimated

2. As noted previously, hemp grower participation dropped 56% in 2021 relative to 2020. No individual reason is identifiable for the decline in participation in 2021, although DATCP suggests the following may have affected participation: (a) operational challenges and uncertainty related to COVID-19; (b) increased production and oversupply of hemp products and cannabidiol (CBD) leading to lower prices and difficulty finding markets for products; (c) a maturing hemp market, driving higher cost and unprofitable producers out of business; and (d) an increase in corn and soybean prices, which decreased interest in diversifying production to hemp. DATCP is in the process of surveying hemp producers for feedback on its program. To date, 62 of 92 respondents report they lost money producing hemp in 2019, and 66 of 92 lost money in 2020. The decline in participation is not unique to Wisconsin, and DATCP reports that in a survey of 41 state hemp programs, 76% reported a decline in participation in 2021. It is unclear at this time if participation will continue to decrease, or is reflective of a one-time market adjustment.

Program Development Costs

3. DATCP reports it expects the hemp program deficit to continue to grow in future years. When the hemp program was created, fees were set at levels intended to cover costs associated with regulation of hemp producers, as is customary in many regulatory programs managed by the Department. However, DATCP notes that program development costs for implementation of unique regulatory requirements for a nascent industry have resulted in significant costs passed on to producers. Program development costs consist primarily of legal, policy, Secretary's office, and laboratory staff time dedicated to research and design of program structure, rulemaking, interpretation of and compliance with federal law requirements, establishing guidance and best practices for regulated entities, and development of laboratory testing standards.

4. Such program development costs could be considered one-time start-up costs, except that federal law requirements initially enacted in 2014 have continued to change under subsequent acts, and USDA guidance has similarly evolved to accommodate the unique context of hemp production. In response to these federal law requirements, Wisconsin has adopted legislation and several emergency rules to regulate hemp. DATCP estimates such program development costs have totaled perhaps \$650,000 from 2017-18 through 2020-21, and expects these costs to continue at perhaps \$265,000 for the next three years as it continues to pursue a permanent hemp rule and regulatory standards for hemp processing, product labeling, marketing, and quality.

Fee Increases

5. Even if program development costs were not supported by fees on producers, trends in revenues and expenditures would still result in a deficit in future years. DATCP suggests that it may be appropriate to increase fees on hemp growers to cover these increasing costs and resolve the program deficit. Fee structures vary by state, but Wisconsin generally has lower fees than its neighbors: (a) in Illinois, growers pay a fee of \$375, \$700, or \$1,000 for one, two, or three years; (b) in Iowa, growers pay an annual fee of \$500 for 0 to 5 acres, \$750 for 5 to 10 acres, and \$1,000 for 10 up to a maximum of 40 acres, plus an additional \$5 per acre; (c) in Michigan, growers pay an annual registration fee of \$1,250; and (d) in Minnesota, growers pay annual fees of \$150, plus \$250 per growing location. In addition to annual license fees, growers also typically pay sampling and testing fees.

6. DATCP estimates that doubling its hemp program fees could raise additional revenue of approximately \$300,000 each year. Under current law, DATCP has sufficient authority to raise annual registration fees through the administrative rule process. However, initial one-time license fees paid by hemp producers are set in statute, and DATCP would need additional authority to modify current one-time license fees, set at \$150, or \$5 per acre up to \$1,000, whichever is more.

General Fund Support

7. DATCP notes that fee increases could discourage participation in the program and have adverse effects on the growth of Wisconsin's hemp industry. If fees were increased, smaller or first-time growers may be discouraged from participating. Higher fees may make it cost-prohibitive to experiment with growing practices before scaling up an operation, which could discourage

prospective producers who might otherwise become long-term program participants. Further, based on current trends in revenues and expenditures, it is possible a fee increase totaling an additional \$300,000 each year would still be insufficient to bring expenditures and revenues into balance. Thus, DATCP contends that it would be appropriate to provide GPR support for hemp program operations.

8. DATCP notes neighboring states use general fund revenues to support hemp program operations, including: (a) \$770,000 in 2018-19 and \$150,000 in 2019-20 in Michigan; and (b) \$175,000 each year in Minnesota, as well as an initial appropriation of \$300,000 each year during the first two years of the Minnesota program. GPR supplements to the hemp program could be provided to offset program development costs, which may be considered necessary costs to establish a hemp industry in Wisconsin that are not reasonably recoverable from program participants without similarly discouraging growth of the industry.

9. Prior to the decline in hemp production after World War II, Wisconsin was a leading state in hemp production. In USDA's 1939 Census of Agriculture, 87 Wisconsin farms reported 813 acres of hemp production, representing 84% of total reported hemp production that year. This represented a significant decline from Wisconsin's 3,300 acres across 113 farms reported in 1919, equal to 47% of U.S. production at that time. Prior to 1919, Kentucky produced most hemp, totaling as high as 23,500 acres (94% of U.S. production) in 1889, the oldest available acreage statistics. It may be that Wisconsin's history of hemp production leaves it favorably positioned given the nationwide resurgence of hemp production in recent years. Thus, it could be considered appropriate to provide general fund revenues to allow Wisconsin to continue to offer low fees as compared to other states, which may encourage new producers to experiment with hemp production and further growth in Wisconsin hemp production.

Staffing

10. During the 2019-21 biennium, DATCP is provided 4.60 PR positions under its hemp regulation appropriation, including 3.0 PR project positions expiring on June 30, 2021. Additionally, DATCP reports it bills staff time for other permanent positions dedicating a portion of their time related to hemp regulation duties, including supervisory work by the section chief and bureau director. However, the hemp regulation appropriation does not support staff costs for the division administrator, legal counsel, or Secretary's Office staff, which have been significant due to evolving USDA requirements and implementation costs. DATCP also regularly hires limited-term employees (LTEs) to support seasonal surges in staff need for licensing, sampling, and testing capacity.

11. Assembly Bill 68/Senate Bill 111 would reauthorize the expiring 3.0 PR project positions as permanent positions, and reallocate an additional 0.4 PR position from other program areas, for a total of 5.0 permanent PR positions. DATCP reports the 5.0 PR positions represent the minimum staffing sufficient to operate the Department's hemp program. The 3.0 expiring project positions consist of: (a) 1.0 plant pest and disease specialist, responsible for management, coordination, and training related to hemp sampling conducted by LTEs; (b) 1.0 licensing and permit program associate, responsible for managing the processing of hemp applicants, including recordkeeping, conducting background checks, managing reporting by licensees, and training LTE staff dedicated to application processing; and (c) 1.0 laboratory chemist, which tests hemp samples for THC content, manages development of testing standards, and manages and trains LTE laboratory

testing staff. DATCP contends all 3.0 expiring project positions are essential to core hemp program operations and cannot be replaced with limited-term staff because these permanent positions maintain programmatic expertise and continuity necessary to oversee and hire additional LTE staff for seasonal program needs. If these positions were not renewed, DATCP reports it would need to strongly consider relinquishing control of hemp regulation duties to USDA.

Relinquishment to USDA

12. As part of the certification process for delegation of hemp regulation to a state-operated program, DATCP must certify to USDA that Wisconsin has sufficient funding and staff capacity to operate its hemp program consistent with federal law requirements. If funding or staff were to become insufficient, DATCP would have to consider relinquishing its delegated regulatory authority to USDA. Under a USDA-regulated hemp program, producers would be licensed by USDA, which operates its hemp regulation program from its Washington, D.C. office. DATCP reports USDA is currently operating its federal regulatory program for the first time this year in Mississippi, New Hampshire, and Hawaii, as well as for several tribal nations.

13. Under the USDA program, growers must contract with private third parties for sampling and testing of hemp prior to harvest, and DATCP believes there is sufficient capacity in Wisconsin for private sampling and testing to occur. DATCP suggests that it is possible a USDA-operated hemp program would not provide the same level of customer service to regulated growers, and may provide limited outreach, best practices sharing, or support in response to grower inquiries. Thus, a USDA-operated program could be less accessible to first-time growers seeking to begin hemp farming. However, USDA does not impose fees on program participants, which could reduce costs for producers and outweigh any loss of services.

14. DATCP reports that a decision on relinquishment to USDA would need to be made by July 1, 2021, in order to allow sufficient time to transfer regulatory duties to USDA by January 1, 2022, in time for the next growing season. Relinquishment of DATCP's hemp program to USDA would prevent further growth in the hemp program deficit, although the Department would still be responsible for any 2020-21 closing deficit. Further, USDA does not regulate hemp processors or hemp products for safety, quality, or product labeling, and DATCP would retain responsibility for those activities.

Alternatives

15. 2020-21 represents the first year the hemp regulation program is in deficit. Significant uncertainty remains with respect to future participation in Wisconsin's hemp program, the short-term impacts of the COVID-19 pandemic, market trends for hemp products, and any potential impacts of a USDA-administered Wisconsin hemp program. Given the recency of the current program deficit and uncertainty associated with future program trends, it could be considered appropriate to allow for the Department to continue operating its hemp program under the current fee schedule.

16. Given existing uncertainty, the Committee could direct DATCP to further study options for resolving the hemp program deficit and require DATCP to report to the Committee by September 30, 2022, on its recommendations [Alternative 6]. To continue current hemp program operations, the

Committee could consider reauthorizing the expiring 3.0 PR positions in the Department's hemp regulation appropriation for an additional two years [Alternative 1b] or on an ongoing basis [Alternative 1a].

17. Given the ongoing program development costs associated with compliance with evolving federal law requirements, rulemaking, research and development, and outreach to hemp growers, the Committee could consider providing a GPR supplement to support hemp program operations. Such a supplement could be a one-time transfer equal to program development costs to date, which total approximately \$650,000 [Alternative 4], or an ongoing appropriation equal to estimated current program development costs of \$265,000 annually [Alternative 5]. If a GPR supplement were provided, any DATCP fee increase would be expected to be smaller. If no supplemental funding were provided, it is likely the hemp program deficit would continue to grow while DATCP considered other funding options for the program.

18. The Committee could also consider increasing program fees to alleviate the program deficit. It could direct DATCP to use existing rulemaking authority to increase annual registration fees for growers [Alternative 2], and/or modify current law to allow DATCP to increase its initial licensing fee for new growers if a higher fee is necessary to cover hemp regulation costs [Alternative 3].

19. The Committee could also consider taking no action, and the hemp program would be provided 2.0 PR permanent positions during the 2021-23 biennium [Alternative 7]. It is likely that if new positions were not authorized, DATCP would relinquish its regulatory authority to USDA.

ALTERNATIVES

1. Provide 3.0 PR positions with \$146,600 PR in 2021-22 and \$195,700 PR in 2022-23 to support the industrial hemp program. Specify positions be:

- a. Permanent; or
- b. Two-year project positions.

ALT 1	Change to Base Funding	Positions
PR	\$342,300	3.00

2. Direct DATCP to increase annual hemp grower registration fees using existing rulemaking authority.

3. Modify current law to allow DATCP to increase the initial license fee for new hemp growers through rulemaking as is necessary to recover costs of hemp regulation.

4. Provide an additional \$650,000 GPR in 2021-22 to the Division of Agricultural

Resource Management's general program operations appropriation, and specify funding be transferred to the hemp regulation appropriation.

ALT 4	Change to Base
GPR	\$650,000

5. Create an annual GPR appropriation and provide \$265,000 GPR annually for hemp regulation.

ALT 5	Change to Base
GPR	\$530,000

6. Require DATCP to study options for resolving the hemp program deficit, including modifying fees, relinquishing operations to USDA, or restructuring program operations. Require DATCP to report to the Committee by September 30, 2022, on its recommendations for resolving the hemp program deficit.

7. Take no action.

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