



# NORTH CAROLINA GENERAL ASSEMBLY

2023 Session

## Legislative Fiscal Note

**Short Title:** Hemp-Derived Consumables/Con Sub Changes.  
**Bill Number:** House Bill 563 (Sixth Edition)  
**Sponsor(s):** Rep. McNeely, Rep. Sasser, Rep. Cotham, and Rep. Fontenot

### SUMMARY TABLE

#### FISCAL IMPACT OF HB 563, V.6 (\$ in millions)

	<u>FY 2024-25</u>	<u>FY 2025-26</u>	<u>FY 2026-27</u>	<u>FY 2027-28</u>	<u>FY 2028-29</u>
<b>State Impact</b>					
General Fund Revenue					
<b>Dept. of Revenue (DOR)</b>					
Revenue		21.8	26.0	31.1	37.2
Less Expenditures	0.4	2.2	2.3	2.3	2.4
DOR Impact	(0.4)	19.6	23.7	28.8	34.8
<b>Alcohol Law Enforcement (ALE)</b>					
Revenue		7.4	8.5	9.8	11.2
Less Expenditures	1.9	3.1	2.4	2.4	2.4
<b>General Fund Impact</b>	<b>(1.9)</b>	<b>4.3</b>	<b>6.1</b>	<b>7.4</b>	<b>8.8</b>
<b>NET STATE IMPACT</b>	<b>(\$2.3)</b>	<b>\$23.9</b>	<b>\$29.8</b>	<b>\$36.2</b>	<b>\$43.6</b>
<b>ALE POSITIONS</b>	<b>10.00</b>	<b>20.00</b>	<b>20.00</b>	<b>20.00</b>	<b>20.00</b>
<b>DOR POSITIONS</b>	<b>0.00</b>	<b>22.00</b>	<b>22.00</b>	<b>22.00</b>	<b>22.00</b>

**TECHNICAL CONSIDERATIONS:** See Technical Considerations Section

### FISCAL IMPACT SUMMARY

The bill provides for regulation of the manufacture, distribution, sale, and taxation of hemp-derived consumable products (HDCPs) in the State. The estimated recurring costs to the Department of Revenue (Department) for regulating the HDCP industry is approximately \$2.1 million in the first year. The bill includes a one-time appropriation to the Department of \$375,000 in FY 2024-25 for implementation, which will remain available until spent. The bill also includes a non-reverting one-time appropriation to the Alcohol Law Enforcement Division (ALE) of \$2.0 million for implementation. All licensure fees collected by the Department are required to be remitted to ALE to cover the costs of enforcement. These fees are anticipated to sufficiently cover ALE's enforcement expenses of approximately \$2.4 million per year.

**Section 1.1.(a)** will increase General Fund revenue by imposing an excise tax of 10.5% on the retail sale of HDCPs. The tax is expected to generate \$116.1 million over the next 5 fiscal years. The tax is collected and administered by the Department of Revenue in a similar manner as the State sales and use tax, and is additional to that tax.

**FISCAL ANALYSIS**

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**Section 1**

Section 1 of the bill amends the General Statutes by adding a new Chapter 18D to regulate the manufacture, distribution, and sale of HDCPs in the State, to establish the Department as the regulating entity, and to authorize ALE to enforce the provisions of the new chapter.

Licensure

The bill requires affected businesses to obtain and annually renew a license from the Department based on the following licensure schedule:

**Table 1. HDCP Licensure Fees**

<b>Business Type</b>	<b>Fee Amount</b>
Manufacturers	\$15,000 \$1,000*
Distributors	\$2,500 \$750*
Retail sellers	\$250 per location/website <b>or</b> \$5,000 for more than 25 locations/websites

\*Reduced licensure fee for manufacturers and distributors with gross income of less than \$100,000 in the calendar year prior to application.

**Table 2. Annual HDCP Licensure Renewal Fees**

<b>Business Type</b>	<b>Fee Amount</b>
Manufacturers	\$5,000
Distributors	\$750
Retail sellers	Same as initial licensure fee

The initial licensure fee and the renewal licensure fee for businesses seeking to engage in a combination of manufacturing, distributing, and/or selling of HDCPs would pay a single fee, which would be the highest fee of those business types. For example, a business that manufactures and distributes HDCPs would have an initial fee of \$15,000 and a renewal fee of \$5,000.

All licensure fees collected by the Department are required to be remitted to ALE to cover the costs of enforcement.

Licensure Revenue

The bill establishes specific licensure requirements for HDCP businesses that are currently registered to operate in the State as retailers that remit sales and use tax to the Department. Because the State currently does not identify HDCP businesses, and a central repository of the

number of impacted businesses does not exist, a complete projection of revenue collections for licensure under the bill is not possible. Instead, this analysis uses other business-related data from the Department to estimate the number of potential retail sale licensees.

The following assumptions were made in estimating licensure revenue:

- HDCPs are sold in most registered retail locations that sell tobacco and vape products. The Department estimates approximately 1,400 of these businesses were actively operating in the State at the end of FY 2022-23. To develop this estimate, the Department queried the State’s tax management information system for the number of active registrants using the following key terms: hemp, CBD, vapor, vape, smoke, tobacco, cigarette, delta, THC, and cannabis.
- HDCPs are sold in most retail locations registered as grocery stores, convenience stores, pharmacies, and related retailers. The Department estimates there were approximately 10,400 potential licensees in the State at the end of FY 2022-23.
- At least half of the current HDCP retail locations based in the State also operate as online sellers. Though the exact number is unknown, this analysis assumes that 50% of all retail locations, about 5,900, also sell the products online.

Based on the above assumptions, an estimated 11,800 retail locations and 5,900 websites were operating in the State at the end of FY 2022-23. Using historical data from the Department, the average annual growth rate of impacted businesses over the last five years was 13.1% for tobacco and vape retailers and 17.9% for grocery stores, convenience stores, pharmacies, and related retailers. Assuming growth will slow over time, a 10% annual growth rate was used to project licensure revenue collections over the first five fiscal years of implementation for tobacco and vape retailers and 15% for grocery stores, convenience stores, pharmacies, and related retailers. The results are presented in Table 3. Estimates are provided starting in FY 2025-26, when the licensing and enforcement of HDCP retailers would become effective.

**Table 3. Projected Revenue from Retail Licensure**

	<b>FY 2025-26</b>	<b>FY 2026-27</b>	<b>FY 2027-28</b>	<b>FY 2028-29</b>
Tobacco and Vape Retailers (10% Growth Rate)	1,900	2,100	2,300	2,500
Other Retail Locations (15% Growth Rate)	17,900	20,600	23,700	27,300
Retail Location Fees	\$4,950,000	\$5,675,000	\$6,500,000	\$7,450,000
Online Sellers (50% of All Retail Locations)	9,900	11,350	13,000	14,900
Online Seller Fees	\$2,475,000	\$2,837,500	\$3,250,000	\$3,725,000
<b>Total Number</b>	<b>29,700</b>	<b>34,050</b>	<b>39,000</b>	<b>44,700</b>
<b>Total Fees</b>	<b>\$7,425,000</b>	<b>\$8,512,500</b>	<b>\$9,750,000</b>	<b>\$11,175,000</b>

A complete projection of total revenue collections for licensure under the bill is not currently possible. There are many factors that complicate the accurate projection of total licensure revenue under the bill, such as:

- The Department was only able to capture active tobacco and vape shop registrants in its database query that matched the key terms searched. There are likely additional businesses that would be subject to licensure that fall outside of these search parameters.
- Not all businesses registered as grocery stores, convenience stores, pharmacies, and related retailers will sell HDCPs.
- Potential revenue that would be collected from licensed online retailers is unknown, as the bill does not require online sellers to be domiciled within the State and no data exists to estimate the total number of online sellers that would pursue licensure.
- The number of retail sellers with 25 or more locations and/or websites is unknown.
- Potential revenue that would be collected from licensed manufacturers and distributors is excluded from the analysis, as the number of these entities operating in the State is unknown.
- The number of entities engaging in a combination of manufacturing, distributing, and/or selling is unknown.

Civil Penalties

The bill authorizes the Department to impose the following civil penalties:

**Table 4: Civil Penalties for Violations of Chapter 18D**

<b>Violation</b>	<b>Retail Sales</b>	<b>Manufacturers and Distributors</b>
First	up to \$500	up to \$1,000
Second within three years	up to \$750	up to \$5,000
Third within three years of the first	up to \$1,000 and license suspension for one year	up to \$7,500
Fourth or subsequent within three years of the first	up to \$2,000 and revocation of the license	N/A

In addition to the penalties outlined in Table 4, the Department is authorized to suspend a license for up to three years, revoke a license, or impose conditions on the licensee’s operating hours. In lieu of these measures, the Department is authorized to accept an offer in compromise under certain conditions specified in the bill.

Civil Penalty Revenue

The clear proceeds of any civil penalties collected by the Department under the bill would be remitted to the Civil Penalty and Forfeiture Fund (CPFF) pursuant to G.S. 115C-457.2. Since HDCP businesses are not currently subject to State regulation, the number of violations of the new civil penalties established in the bill and the amount to be remitted to the CPFF is indeterminable.

HDCP Testing

The bill establishes product testing standards, requires manufacturers to test their products, and requires the Department to adopt rules regarding the HDCP manufacturer testing requirements

under the Chapter. The Department must also develop an application process for determining qualified testing laboratories and post a qualified testing laboratories registry on its website.

Impact on the Department

The bill requires the Department to administer Chapters 18D, which includes processing initial applications and annual renewals for licensing the manufacture, distribution, and sale of HDCPs, adjudicating cases involving civil penalties and license revocations, and determining which test laboratories are qualified for testing products. The Department will also need to publish guidance and provide general customer service regarding the new requirements.

The following staffing estimate is based on similar functions performed by the Excise Tax Division (ETD) in administering the motor carrier tax. Utilizing the current ETD staffing ratio of one position to approximately 600 licensees, approximately 22 positions would be needed to comply with Chapter 18D.

Fifteen positions would be needed to administer the licensure requirements. Two positions would perform duties related to adjudicating penalties, determining qualified testing laboratories, and administrative rulemaking. The final five positions would perform duties related to the process and collecting penalties, as well as performing compliance checks and audits.

The total projected costs to the Department in FY 2025-26 for administrative activities related to the bill are approximately \$2.2 million. The bill provides a one-time appropriation of \$375,000 in FY 2024-25 to the Department for implementation, which will remain available until spent. The bill does not provide for recurring funds to support positions in the Department needed to administer the licensure and civil penalties portion of the bill.

Table 5 provides an estimate of the fiscal impact to the Department for administering licensure for a portion of the businesses that could be identified in this analysis. Estimates are provided starting in FY 2025-26, when the licensing and enforcement of HDCP retailers would become effective.

**Table 5: Department of Revenue Licensure and Administrative Staffing Needs**

	<b>FY 2025-26</b>	<b>FY 2026-27</b>	<b>FY 2027-28</b>	<b>FY 2028-29</b>
Administrative Specialists (14 Positions)	\$1,113,309	\$1,156,169	\$1,197,047	\$1,239,444
Revenue Tax Technicians (1 Positions)	\$81,520	\$84,667	\$87,669	\$90,782
Revenue Administrative Officers (2 Positions)	\$286,191	\$297,763	\$308,801	\$320,248
Revenue Officers (3 Positions)	\$260,576	\$270,704	\$280,363	\$290,381
Revenue Field Auditor (2 Positions)	\$257,711	\$268,063	\$277,936	\$288,176
Staff Operating Costs	\$195,263	\$195,004	\$197,789	\$200,633
<b>Total</b>	<b>\$2,194,571</b>	<b>\$2,272,370</b>	<b>\$2,349,605</b>	<b>\$2,429,664</b>

## Enforcement

The bill places ALE in charge of enforcement. ALE estimates that it will require approximately 20 FTE positions to provide enforcement across the State, including 16 agents (2 per agency district) and 4 Assistant Special Agents in Charge (ASACs; ALE's supervisory position). These positions will carry a **recurring cost of approximately \$2.4 million** for salary, benefits, and operational costs, and first-year **nonrecurring cost of approximately \$1.4 million** for equipment and other start-up expenses.

The bill provides \$2 million in nonrecurring funds in the first year for initial start-up costs at ALE, with future years' expenses to be covered by fee revenue. While this initial appropriation may be insufficient for a full year's worth of expenses once enforcement operations are fully implemented, hiring staff and spinning up new operations will take time and it is unlikely that ALE would incur all of these expenses in the first year. As shown above in Table 3, **Fiscal Research projects that the licensure fees required in this bill will likely produce sufficient revenue** to cover these personnel costs for ALE.

As part of their enforcement duties, ALE is required to inspect licensees and test HDCP products, although the bill does not specify a minimum number of inspections per year or tests per inspection. Existing ALE agents already inspect existing Alcoholic Beverage Control (ABC) Commission permittees, and those agents are expected to also participate in the inspections of the new HDCP permittees. If ALE were fully staffed with 16 new field agents each conducting 5 inspections per week on average, the agency would be able to conduct an additional 4,000 inspections per year. (Please note that ASACs may also conduct inspections as part of their duties and as such the capacity for new inspections could be higher.) When combined with existing ALE capacity, this would likely be sufficient for the projected number of retailers.

ALE anticipates that testing would be done on an intelligence-informed basis rather than at random or upon every inspection of a given establishment. Currently, ALE utilizes an outside laboratory for this testing, a practice the agency expects to continue should this bill become law. The current cost for testing an HDCP product is \$220 per sample. ALE anticipates collecting 5-10 samples from each inspection. Annual testing costs will vary depending on the number of samples, the number of permitted establishments, and the number of inspections performed annually. If, for example, ALE were to take 5 samples from 9,900 locations in a given year (approximately half of the likely number of retailers), this would represent 49,500 tests at a cost of \$10.9 million. However, the bill also requires that the retailer must cover the cost of testing for any samples that are found to be in violation of the legal limits for active ingredients. ALE reports that for their testing activity for HDCPs in Spring 2024, 80% of tested samples were above the legal limit for Delta 9. If these rates continue, most if not all testing costs will be covered by retailers rather than by the State.

## Excise Tax

Section 1.1.(a) will increase State General Fund revenue by imposing an excise tax of 10.5% on the retail sale of HDCPs.

Consumable products containing any phytocannabinoid found in hemp, or any synthetic cannabinoid derived from hemp, are subject to tax under this section. Products containing

cannabidiol (“CBD”) are the primary products expected to be taxed under this section. The 2022 MJBiz Factbook (“Factbook”), a cannabis industry publication, emphasizes that CBD is the dominant product among those subject to the tax, stating that “[n]ovel cannabinoids still account for a very small portion of hemp-product sales overall.”

Chart 6.01 of the Factbook includes estimates of hemp-derived CBD retail sales for the United States, projecting \$6.9 billion in sales in calendar year 2025 and a 19.6% average growth rate for 2021-2026. This fiscal estimate is developed based on those figures, multiplying North Carolina’s share of United States gross domestic product (2.8%) to estimate State retail sales. Since the tax is effective July 1, 2025, revenue is increased beginning in FY 2025-26. Table 6 below shows General Fund revenue estimates for the excise tax.

**Table 6: Hemp-Derived Consumable Products Excise Tax Estimates**

FY 2024-25	FY 2025-26	FY 2026-27	FY 2027-28	FY 2028-29
\$0	\$21,800,000	\$26,000,000	\$31,100,000	\$37,200,000

Since this is a new excise tax, estimates of revenue are uncertain. The Department of Revenue does not have product-level data on hemp-derived consumable products, requiring the use of a national source.

This analysis anticipates DOR can absorb any associated costs of collecting the tax on HDCPs with existing staff resources within the Excise Tax Division.

**Section 3**

Section 3 appropriates \$2.0 million nonrecurring in FY 2024-25 to ALE to hire 20 full-time Special Agents to implement the provisions of the bill, and an additional \$125,000 nonrecurring to be used for any other costs incurred by ALE. It also appropriates \$375,000 nonrecurring in FY 2024-25 to the Department to be used for other implementation costs. The funds appropriated in this section do not revert and will remain available until expended.

**Section 4**

Section 4 requires public school units to adopt policies prohibiting the use of HDCPs, provide notice of the policies, post signs, and enforce these policies. Costs for these measures would be negligible and can be absorbed within existing school unit budgets.

**Section 5**

Section 5 directs the Department to establish guidance and adopt rules to implement Chapter 18D and to accept and issue licenses. The bill states that no licenses shall become effective prior to July 1, 2025. The costs to the Department of doing so are included in the estimate in Table 5. Section 5 also directs DPS to adopt any rules required to implement the bill.

**TECHNICAL CONSIDERATIONS**

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The Department of Revenue states that it anticipates 22 positions are needed to administer the licensure and civil penalties portion of the bill, at an estimated cost of \$2.2 million in the first fiscal year. The bill does not appropriate funds for any additional positions at the Department. Thus, this could present an implementation issue should the Department not be able to cover these required duties with existing staff resources.

## **DATA SOURCES**

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Department of Revenue; Department of Public Safety, Alcohol Law Enforcement Division; MJBizDaily; Moody's Analytics.

## **LEGISLATIVE FISCAL NOTE – PURPOSE AND LIMITATIONS**

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This document is an official fiscal analysis prepared pursuant to Chapter 120 of the General Statutes and rules adopted by the Senate and House of Representatives. The estimates in this analysis are based on the data, assumptions, and methodology described in the Fiscal Analysis section of this document. This document only addresses sections of the bill that have projected direct fiscal impacts on State or local governments and does not address sections that have no projected fiscal impacts.

## **CONTACT INFORMATION**

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June 19, 2024



**Signed copy located in the NCGA Principal Clerk's Offices**