Alaska Marijuana News

‘No one’s having a ton of fun’: Many Alaska cannabis businesses are struggling and failing

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Five years ago, when Alaska’s first legal cannabis shops started opening, there was a lot of money to be made.

“We had three fabulous, great years,” said Sue Nowland, whose Alaska Fireweed was among the first cannabis stores to open its doors in Anchorage.

Those days are over.

Cannabis businesses across the state are confronting a daunting set of issues that owners and advocates say are making it nearly impossible to survive. Some Alaskans who poured their life savings or retirement accounts into starting companies are scrambling to find someone to buy them out. Operations are failing, others are in the red and behind on taxes owed to the state.

One measure of the industry’s problems is tax delinquency: according to an August memo from the Department of Revenue, by the end of June, 56 businesses owed $1,785,751 in back taxes. Nine of the delinquent businesses have closed, though collectively they still owe hundreds of thousands of dollars in unpaid taxes.

The most salient problems, according to people within the industry, are the flat excise tax structure placed on cultivators, an over-saturation of retailers and the rigidity to which licenses are tied to real estate.

Some say the industry’s current woes are normal growing pains to be expected as a new sector of the economy finds equilibrium. But others, including many business owners and the industry’s chief trade group, are debating potential reforms that could stave off looming business defaults as more license applications work their way through the pipeline.

“They got dug in a hole”

In October, the Marijuana Control Board did something novel: for the first time, the panel effectively closed a cannabis business because of the taxes it owed.

The company, Alaskan Blooms, runs a cultivation facility and retail shop in Fairbanks. It owes the state around $700,000 in back taxes.

“This is a hard one,” said Jana Weltzin, the company’s attorney.

She was speaking to the board members during a meeting at the end of October. She described the accumulated tax debt as the fault of a former business partner who has since been removed from the license. Almost $200,000 of the amount owed was from interest and penalties on the overdue balance.

“They got dug in a hole,” Weltzin told board members.

Her attorney asked the board to give the business until January to pay back 50% of the taxes owed.

“If this tax burden wasn’t in the picture, we would be profitable,” said Karen Lowry, one of the Alaskan Blooms owners.

“Everything is going to this tax bill,” Weltzin added.

One member was skeptical that the business would be able to catch up with all the money owed.

Weltzin told the board the cultivation business employed around 20 people. Lowry, she said, had made efforts to stay current with the taxes. Cannabis businesses can’t use banks, and even if Alaskan Blooms could find an entity to loan them money it would likely come at an exorbitant interest rate. And, Weltzin argued, if the board denied the license renewal, there might be no mechanism for the state to recover the money owed.

But the board was unswayed.

“This is an egregious violation,” said member Christopher Jaime.

Board members voted unanimously not to renew Alaskan Blooms’s cultivation license, though did opt to let the business keep its retail license. It was the first time the board denied a license renewal to a business because of an outstanding tax liability.

Lowry declined a request for an interview.

Alaska is unique in how it taxes cannabis relative to other states. Instead of charging at the point of sale, like a tax on groceries collected at the cash register, growers pay the state a flat rate of $800 per pound on cannabis buds. “Trim,” the plant leaves and byproduct manufactured into edible and concentrated products, is taxed at $240 a pound.

The problem with the flat-tax structure, growers say, is that unlike any other agricultural products, they are responsible for the same amount of money regardless of whether the crop turns out highly potent or ends up an impotent bust.

According to multiple owners, cannabis bud, or “flower,” remains the mostly popular product in retail shops, and accounts for the majority of the state’s tax revenues. To the consternation of growers and cannabis connoisseurs in Alaska, consumers have continued favoring high-THC flower strains, almost like beer-drinkers seeking out the most alcoholic IPA’s because they equate “stronger” with “better.” A brewer, on the other hand, might emphasize qualities like flavor, mouthfeel and complexity in quality determinations.

According to Lacy Wilcox, president of the Alaska Marijuana Industry Association, while high-THC crops could sell for around $4,000 a pound, the $3,000-range is more typical. But if a crop sample sent off for a potency test comes back from a lab with a THC level of, for example, 16% — “Which isn’t a high test,” Wilcox said — then the cultivator might only be able to get a $2,000 price for wholesale. After the state taxes are paid, that leaves the cultivator with $1,200 to cover the labor, rent, supplies, and energy costs that went into that crop.

“Which is not enough in Alaska,” Wilcox said.

The flat tax on weight, Wilcox said, means growers are constantly struggling to produce more potent flower because it is the only way for them to earn a profit on a crop.

But if buds turn out mild, cultivators face a choice of either selling them at a loss, or destroying them to avoid a tax liability.

“The amount of waste hurts my heart a little bit,” Wilcox said.

The $1.8 million in unpaid taxes is a small share of the total money cultivators pay the state. In fiscal year 2021, the State of Alaska collected just under $29 million. Of that, $19 million was brought into state coffers from 11.8 tons of flower, an amount that works out to a little more than half an ounce per Alaskan. And that is not counting trim.

Wilcox called tax delinquency in the industry “probably topic number one,” in part because there is still a lingering stigma around cannabis.

“We don’t want to look bad as an industry,” Wilcox said. “Taxes are a part of that.”

“Nobody’s getting rich”

Even though there is a consensus in the industry that the current tax structure is a problem, there is no clear policy fix at hand.

“The current tax is not sustainable, so there’s agreement there,” Wilcox said.

A more vexing problem, though, is whether or not there should be a cap on licenses. Unlike some other states, Alaska has no limit on the number of cannabis licenses it will issue, provided applicants meet the qualifications. As more and more people have jumped into the industry, it has led to what many call an over-saturated market, especially among retail operations. In October, Politco reported that Alaska has more licensed cannabis stores per resident than any of the other western states that have legal sales.

Feedback to the MCB on the issue of license caps tends to be evenly split between those for and against.

“We need to do something to protect our industry in the state,” said Lisa Coates, an owner of Herban Extracts in Kenai, at the October meeting.

“I strongly oppose license caps,” Anchorage resident Chelsea Foster testified, saying a cap would create a barrier to entry for newcomers to the industry, with the potential to bring out-of-state investors to eventually buy up licenses.

Wilcox’s group sent out a survey earlier this year to 349 license-holders. She said about a third of them responded, and among those who did, 70% supported a cap. AMIA is officially neutral on the issue of caps, and is considering asking an outside group for an economic analysis of the potential impacts.

“Maybe even the state will help us do a better analysis of how the market is doing,” Wilcox said.

The issue of over-saturation is most acute in Anchorage. In certain neighborhoods, it seems like there every other block has a pot shop on it.

This is because of zoning.

After Alaskans voted to legalize recreational cannabis in 2014, it was left to local jurisdictions to develop their own rules for how the new industry would be implemented at the very nuts-and-bolts level of zoning regulations. The Anchorage Assembly adopted relatively strict rules for cannabis businesses, effectively relegating them to just a handful of neighborhoods.

“The municipality put them all in a couple different pockets,” Wilcox said.

That’s been convenient for consumers who, if they don’t like the prices or inventory at one shop, can walk a few doors down or drive one strip mall over and potentially pay a little less. But for retailers its meant constantly shaving down prices in the hopes of whittling out a profit.

“They’re feeling the competition of having so many neighbors,” Wilcox said.

If there were to be a cap on licenses, it could take different shapes, according to Wilcox. Maybe its a temporary moratorium on new licenses. Maybe a mechanism for local control, allowing communities to decide for themselves how many businesses to permit. Maybe its a cap just inside Anchorage.

“Nobody’s getting rich, and no one’s having a ton of fun,” Wilcox said.

“We’re eating the young”

“I’m one of the victims of an oversaturated market in downtown Anchorage,” Susan Nowland told the MCB.

When she opened Alaska Fireweed in 2016, the prominent space on Fourth Avenue was expensive, and Nowland said she and her partners had been “immature in negotiating leases.” For the first few years, though, the business was making enough money they could afford the spendy rent.

But the combination of more competition in the area and COVID-19 driving much of their customer base away from downtown gobbled mightily into profits. When it came time to renew the lease, Nowland said she couldn’t come to a workable new rate with the landlord, which meant the end of the store.

“Your license basically has no value unless you have a lease or own your building,” Nowland said. “And so the property owner has basically complete control over you.”

Because cannabis licenses are bound to properties, owners cannot transfer them to different locations, even if rent is suddenly increased or a bank calls in the note on a building.

“If you don’t structure a good lease, the landlords think they have a gold mine. Which they do,” Nowland said.

At first, Nowland looked around Anchorage for a new location to set up a retail store. But with all the other shops that have opened in the city, the costs of setting up a new operation and all the zoning hurdles to jump through with the municipality, she said she couldn’t make the math pencil out.

The companies that are doing well, Nowland said, are the handful of vertically integrated businesses that are able to exercise more control over their inventories, pricing, and taxation. Newcomers face an uphill slog to survive.

“We’re eating the young. And the verticals are going to be able to control the pricing, and it’s going to be really hard for the independents to keep up with that,” Nowland said

In 2019, she opened Denali Grass Company in Healy. Though the customer base is much smaller, and the summer tourism season in the area less reliable during the pandemic, the business is doing well.

“It’s just so much easier and more cost-effective to set up anywhere outside of the municipality,” she said.

Nowland was sad to close her first store, but sounded relieved to be done watching a moneymaking venture slide gradually further into unprofitability.

“My motto is, if you’re not making any money, get out of it,” she said.

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