REQUEST FOR COUNCIL ACTION

CITY COUNCIL MEETING DATE:

JUNE 3, 2014

CLERK OF COUNCIL USE ONLY:

TITLE:

BALLOT INITIATIVE REGARDING MEDICAL MARIJUANA COLLECTIVES/ COOPERATIVES

APPROVED

- ☐ As Recommended
- ☐ As Amended
- ☐ Ordinance on 1st Reading
- ☐ Ordinance on 2nd Reading
- ☐ Implementing Resolution
- ☐ Set Public Hearing For_____

CONTINUED TO _____

FILE NUMBER _____

CITY MANAGER

RECOMMENDED ACTION

Discuss options for an initiative on the November 2014 ballot regarding medical marijuana collectives/cooperatives, including a potential action to provide direction to staff.

DISCUSSION

On February 19, 2013 the City Council received the Certificate of Sufficiency indicating the proponents of the *Santa Ana Medical Cannabis Restriction and Limitation Initiative* obtained the necessary valid signatures to have the initiative placed on the ballot at the next general election in November, 2014. In March, 2013 staff presented a report to the City Council analyzing the proposed initiative to assist the Council in making a decision to either adopt the initiative as submitted or to submit it to the voters at the November 2014 general election.

At the March 18, 2013 meeting the City Council moved to receive and file the report, call for the election, and place the measure on the November 2014 ballot. The City Council also directed staff to explore placing a competing initiative on the November 2014 ballot to either affirm the City's ban on storefront medical marijuana collectives/cooperatives or an initiative to further regulate collectives/cooperatives beyond the proposed regulations provided in the collective-backed initiative.

BACKGROUND

State and Federal Law

In 1996, California voters approved Proposition 215, entitled "The Compassionate Use Act" (CUA), which provides seriously ill Californians "the right to obtain and use marijuana for medical purposes" once a physician has deemed the use beneficial to the patient's health. The CUA regulates several forms through which marijuana can be distributed, such as "a medical marijuana cooperative, collective, collective, operator, establishment, or provider that is authorized by law to possess, cultivate, or distribute medical marijuana and that has a storefront or mobile retail outlet which ordinarily requires a local business license." By its own terms, nothing in CUA prohibited cites from adopting policies further restricting the location or establishment of such operations.

In 2003, the State legislature enacted SB 420 to clarify the CUA's scope and to allow cities to adopt and enforce rules and regulations consistent with its provisions. SB 420, also known as the "Medical Marijuana Program Act" (MMPA), provides additional statutory guidance for those involved with medical marijuana use. The CUA and MMPA allow for the use and operation of collectives or cooperatives by qualified medical marijuana patients and primary caregivers, and provides narrow affirmative defenses for criminal prosecutions of persons for drug possession.

Notwithstanding the CUA and MMPA, the Federal Controlled Substance Act makes it unlawful to manufacture, process, distribute or dispense marijuana. In fact, the United States Supreme Court, in both 2001 and 2005, held that Federal law continues to apply in California despite the CUA and that no medical necessity exceptions exist.

After the initial passage of the CUA, some cities and counties across California began to experience a proliferation of storefront medical marijuana collectives claiming to be legal collectives or cooperatives. Aside from the fact that the use and distribution of marijuana in any form is illegal under federal law, the existence of storefront collectives is usually illegal under California law because it is nearly impossible to comply with the CUA and MMPA while catering to a large membership. Moreover, storefront collectives also create significant crime, health, and safety concerns for the surrounding areas. After studying these concerns, some municipalities chose to adopt comprehensive bans on storefront medical marijuana collectives and collectives, as Santa Ana did in 2007, based upon their knowledge of how these collectives operated at that time.

On May 6, 2013, in the case of *City of Riverside v. Inland Empire Patients Health and Wellness Center,* the California Supreme Court held that local governments can ban medical marijuana collectives because California's marijuana laws do not expressly or impliedly limit a local jurisdiction's land use authority, including the authority to prohibit facilities for the distribution of medical marijuana. In this opinion, the court ruled that the California Constitution grants cities and counties broad power to determine the permitted uses of land within their borders, that the CUA and MMPA do not restrict that power, and that a local ban on medical marijuana collectives does not conflict with these laws because they do no more than exempt certain activities from State criminal and nuisance laws.

Given the clarity offered by this decision upholding a municipality's ability to ban medical marijuana collectives, several municipalities have chosen this course of action or have re-visited their existing bans. Further, this decision has opened the door for discussion of a municipality's ability to regulate medical marijuana collectives instead of banning them altogether.

Senate Bill 1262

Senate Bill 1262, introduced on February 21, 2014 is sponsored by the California Police Chiefs Association and co-sponsored by the League of California Cities. The policy underlying this bill is the need for reform of California's medical marijuana laws as defined by the CUA (Proposition 215) and MMPA (SB 420).

The Bill proposes to establish an improved regulatory structure to ensure that the CUA works as originally envisioned to assist patients with legitimate medical needs, in a manner that works for law enforcement, city and county governments, local community organizations, and medical professionals. The five essential principles of the bill are:

1) Protect local control by precluding an operator from obtaining a state license unless the operator has first secured all necessary local permits from a particular jurisdiction;

2) Uphold local governments' ability to ban collectives and all related facilities;

3) Impose tighter regulations on doctors who issue medical marijuana recommendations, including new training and record keeping requirements as well as fines, and a strict regimen for recommendations to minors;

4) Impose uniform quality assurance standards as well as health and safety standards to be administered by counties with oversight by the Department of Public Health;

5) Require a series of detailed security measures to prevent diversion and recreational use at all medical cannabis facilities.

Current City Regulation and Enforcement

Currently the City of Santa prohibits the establishment of medical marijuana collectives citywide under Article XIII of Chapter 18 of the Santa Ana Municipal Code. This section was added in 2007 following a two year moratorium on medical marijuana collectives.

Since the City's ban on the establishment of medical marijuana collectives in 2007, the Police Department, Community Preservation Division and City Attorney's Office have continued to experience challenges trying to close illegal collectives in the City. As of May 1, 2014, there were a confirmed 50 existing illegal medical marijuana collectives in the City. This number is up from a low of 16 in early 2013, but down from the high of 68 in 2012.

The City has successfully closed 177 collectives and fined illegal collectives for more than $138,000 since enforcement began in 2010. While these and other joint enforcement efforts with the Drug Enforcement Administration (DEA) have proven effective, the transitory nature of these businesses typically result in one closing down and one or more appearing in its place.

It is important to note that while the Santa Ana Municipal Code currently prohibits medical marijuana collectives, it specifically precludes State-licensed: clinics, health care facilities, residential care facilities for persons with chronic life-threatening illnesses, residential care facilities for the elderly and residential hospice or home health agencies from these regulations. These licensed medical establishments are permitted to prescribe medical marijuana to its patients under the CUA and MMPA while remaining in compliance with the Santa Ana Municipal Code.

***Analysis** of Collective-backed Initiative*

In February, 2013, the City Council directed the City Manager to prepare an analysis of the collective-backed Santa Ana Medical Cannabis Restriction and Limitation Initiative. This initiative, if approved, would repeal the City's current prohibition of medical marijuana collectives/cooperatives, and replace it with a ministerial process to authorize collectives/cooperatives to operate in the City. Staff has a number of concerns regarding the proposed regulations contained in this initiative, most notable among these are:

1. No regulations regarding the distribution and/or separation between collectives/ cooperatives.

2. No maximum on the number of collectives/cooperatives permitted (minimum of 22 required).

3. Definitions of collectives and cooperatives results in smaller operations (more than 1 but less than 5) being unregulated.

4. Collectives/cooperatives permitted in all commercial, industrial and professional zones including properties that may be directly adjacent to residential properties.

5. No separation (buffer) requirements from sensitive uses (parks, churches, child care facilities, liquor stores, adult entertainment, etc.).

6. Ministerial approval process requires no public noticing or public hearing.

7. Limited/vague guidance regarding the provision of on-site security.

8. Prohibits the Police Department and Code Enforcement from accepting Federal funding or participating in any task force that accepts Federal funding or revenue sharing, to investigate, cite, arrest, prosecute or seize property based on offenses which would be legal under California medical cannabis laws.

9. Proposed licensing/taxation method is substantially less than what other cities that regulate medical marijuana collectives/cooperatives require and does not consider taxation methods for registered non-profit collectives/cooperatives.

10. Proposed changes to the Business License Tax Code (Chapter 21) for medical marijuana collectives/cooperatives results in possibility of unintended consequences regarding the taxation rates for businesses other than medical marijuana collectives/cooperatives.

A complete analysis of the collective-backed initiative was provided in the Report to City Council on March 18, 2013.

City Options to Proceed

Given that the Santa Ana Medical Cannabis Restriction and Limitation Initiative has qualified for the November general election the City has three options to proceed.

Option #1 – Take no action (Not Recommended)

The first option available to the City is to not place a competing initiative on the ballot and accept the regulations and requirements of the qualified collective-backed initiative should it receive voter approval. This option is not recommended for several reasons. First, given the level of interest from the medical marijuana industry there is a high likelihood that, should the voter initiative fail in November; medical marijuana proponents would immediately begin to secure the necessary signatures to place another voter initiative on a future ballot.

Additionally, not placing a competing initiative on the ballot limits the voters' options. Should the voters wish to support medical marijuana collectives/cooperatives, the only regulations and requirements available to them would be those contained in the collective-backed initiative. Should the voters wish to confirm the City's ban on medical marijuana collectives, such an option would not be available. Lastly, by taking no action, it may inadvertently signal to the community that the City accepts the regulations proposed in the collective-backed initiative.

Option # 2 – City sponsored ballot initiative to ban medical marijuana collectives/cooperatives (Not Recommended)

The City Council retains authority under Elections Code Section 9222 to place a competing measure on the November 2014 ballot affirming the City's ban on medical marijuana collectives/cooperatives. A City initiative to prohibit medical marijuana collectives would effectively serve as the "No" alternative to the Santa Ana Medical Cannabis Restriction and Limitation Act Initiative.

Were a City initiative to ban medical marijuana collectives be approved by the voters it would serve to solidify the City's current position on storefront medical marijuana collectives/cooperatives and further support the City's existing enforcement strategies. In addition to prohibiting storefront medical marijuana collectives, this initiative would include language clarifying that the ban will also apply to mobile collectives which are addressed in the current regulations, but not explicitly prohibited, and cultivation, which is currently not addressed in current regulations.

Similar to the City's current enforcement, the initiative to ban medical marijuana collectives would not prohibit medical marijuana from being prescribed to patients by licensed physicians through State-licensed clinics, health care facilities, residential care facilities for the elderly or residential hospice or home health agencies and would address the issues regarding mobile marijuana collectives and cultivation.

Option # 3 – City sponsored ballot initiative to regulate medical marijuana collectives/ cooperatives (Recommended)

Another option available to the City is to place a competing measure on the November 2014 ballot that permits medical marijuana collectives, but with additional regulations not contained in the Santa Ana Medical Cannabis Restriction and Limitation Initiative. The regulations proposed in this option were derived from recommendations from the California Police Chiefs Association White Paper on Marijuana Collectives, a review of other cities' and counties' regulations regarding medical marijuana collectives, direct Code Enforcement experience regulating illegal medical marijuana collectives in the City over the last five years and a review of existing Municipal Code regulations regarding regulated uses. Regulations proposed as part of a City initiative to permit, but regulate medical marijuana collectives would generally include:

1. Limit to industrially zoned (M1, M2) properties only.

2. Set a maximum number of eight collectives permitted in the City.

3. Establish distance/separation requirements from sensitive uses (schools, parks and residentially zoned properties).

4. Establish a separation requirement from other medical marijuana collectives to prevent overconcentration.

5. Specify operational requirements including security guards, signage, ventilation, lighting, hours of operation, restricting minors, prohibiting on-site consumption, etc.

6. Update the Business License Tax Code (SAMC Chapter 21) to require a 5% gross receipts cannabis tax, which is commensurate with the other cities surveyed, as well as initial registration fees and annual regulatory fees to account for the costs associated with regulating these businesses.

Similar to the City's current enforcement and initiative to ban collectives, this initiative would not prohibit medical marijuana from being prescribed to patients by licensed physicians through State-licensed clinics, health care facilities, residential care facilities for the elderly or residential hospice or home health agencies and would address the issues regarding mobile marijuana collectives and cultivation.

Risk of regulation/permitting medical marijuana collectives

In *City of Riverside v. Inland Empire Patients Health and Wellness Center*, the California Supreme Court upheld the right of local governments to ban medical marijuana collectives, but the question of whether local governments can regulate these collectives was not directly before the court. However, in its holding, the Court opined "localities in California are left free to accommodate such [medical marijuana collective] conduct if they so choose, free of state interference." (*City of Riverside, supra*, 56 Cal. 4th at 762.) Thus, the Court clearly held that a

local government may ban medical marijuana collectives, but was less clear on the parameters, if any, for which a municipality can regulate them. Further, the decision in *City of Riverside* case does not specifically mention local regulation of the cultivation of marijuana. Where and how marijuana is grown may rightly be of great concern to local municipalities.

Local governments cannot "permit" or "authorize" any activity that violates federal or state law; in fact, federal and state law pre-empts any such attempt. Accordingly, should a municipality decide to regulate, and not ban, medical marijuana collectives, at least one appellate court (whose opinion has since been de-published due to the City of Long Beach amending its regulations) held in 2011 that a municipality's regulation sanctioning the issuance of "permits" for medical marijuana collectives was not allowed because the scheme crossed the line by authorizing an illegal activity. *See Pack v. Superior Court* (Cal. App. 2d Dist. 2011) 199 Cal. App. 4th 1070 [de-published]). In other words, a court could find that the City is pre-empted by federal law from regulating medical marijuana collectives because the City cannot "permit" or "authorize" a medical marijuana business and marijuana related activities, which activities are prohibited by federal law (i.e. the Federal Controlled Substance Act). To get around this pre-emption issue, the State of California has merely de-criminalized certain State penalties, but has not, and cannot, permit or authorize any right in violation of federal law. Thus, the law is not clear on the ability of a local government to regulate medical marijuana collectives. Not only will any such regulation need to be crafted in a way so as to avoid any Federal pre-emption issues, it would also require the City to expend resources to ensure that medical marijuana collectives are not operating in violation of the City's regulations and to defend any legal challenges to any such City regulation.

Notwithstanding this lack of clarity on whether a municipality can regulate medical marijuana collectives or, if they can, the scope of such power, some local jurisdictions within California have passed such regulations. One example is the City of Los Angeles. Originally, Los Angeles attempted to regulate medical marijuana collectives. However, in 2012 after years of defending numerous lawsuits over the legality of these regulations, the City of Los Angeles repealed its regulations in light of the *Pack* decision (the City of Long Beach's medical marijuana collective regulations were based on the then-existing regulations from the City of Los Angeles) and instead banned medical marijuana collectives altogether. In doing so, the City of Los Angeles cited the several threats of litigation brought by marijuana advocates should the City of Los Angeles adopt registration provisions for medical marijuana collectives and to the December 2011 opinion of the California Attorney General Kamala Harris that several laws concerning the regulation of medical marijuana were "unclear," particularly the rules for medical marijuana collective operation.

Fiscal implications of medical marijuana collectives

There are a number of issues regarding the licensing and taxation of medical marijuana collectives/cooperatives that would need to be addressed as part of any ballot initiative proposing to permit, but regulate this type of business. The method proposed as part of the Santa Ana Medical Cannabis Restriction and Limitation Act is to charge collectives a 5-to-6% gross receipts

Cannabis Business License Tax and provide quarterly installment payments of the tax, as well as any applicable sales tax. Based on the City's experience with current illegal collectives and relevant research regarding the costs associated with regulating these uses, the tax rate and regulatory fees proposed in the collective-backed initiative are not sufficient to cover the costs to regulate these types of uses.

Nothing in Proposition 215 or the MMPA (SB 420) authorizes collectives, cooperatives, or individuals to profit from the sale or distribution of marijuana. Generally, medical marijuana collectives/cooperatives are organized as non-profits. Under Article XIII, Section 26 of the California Constitution, certain non-profit organizations that meet the requirements of Chapter 4 (commencing with Section 23701) of Part 11 of Division 2 of the Revenue and Taxation Code or Subchapter F (commencing with Section 501) of Chapter 1 of Subtitle A of the Internal Revenue Code of 1986 are exempt from local taxes measured by gross receipts or income.

Given the taxation issues created by the collective-backed initiative, should the City elect to propose a competing initiative to regulate medical marijuana collectives/cooperatives, the following components would be addressed in an amendment to Chapter 21 (Business License Tax code) of the Santa Ana Municipal Code:

1. Include sufficient definitions to address the multitude of medical marijuana business operations that may wish to open in the city including registered non-profit organizations, limited liability corporations and for-profit organizations.

2. Include a definition and taxation rate for cultivation even though the regulatory component of the proposed ordinance would not allow for cultivation. This will allow the city to impose a tax obligation on any illegal cultivation sites in addition to the regulatory penalties. Including this definition in the tax code will also provide greater flexibility should the State supersede any City regulations regarding cultivation in the future.

3. Include a 5-to-6% gross receipts tax rate applicable to medical marijuana collectives/ cooperatives which do not meet the requirements for exemption from local taxes measured by gross receipts or income with provisions to allow the City Council by ordinance to increase this rate as needed up to a maximum rate of 10% to offset the costs associated with the secondary and tertiary effects of medical marijuana businesses.

4. Include an alternate tax of up to one hundred dollars ($100) per square foot on all improvements owned, rented, leased or otherwise occupied or used by medical marijuana collectives/cooperatives that meet the requirements for exemption from local taxes measured by gross receipts. The tax shall initially be set at a rate of fifteen dollars ($15) per square foot with provisions to allow the City Council by ordinance to increase this rate as needed up to a maximum rate of one hundred dollars ($100) per square foot to offset the costs associated with the secondary and tertiary effects of medical marijuana businesses.

5. Apply the alternate tax of up to one hundred dollars ($100) per square foot on all improvements owned, rented, leased or otherwise occupied or used by medical marijuana collectives/cooperatives engaged in the cultivation/growing of marijuana on such improvements whether for retail sale or whether to supply another marijuana business. The tax shall initially be set at a rate of fifteen dollars ($15) per square foot with provisions to allow the City Council by ordinance to increase this rate as needed up to a maximum rate of one hundred dollars ($100) per square foot to offset the costs associated with the secondary and tertiary effects of medical marijuana businesses.

6. Provide that the "initial gross receipts tax rate" and both the "initial square foot tax rate" and "maximum square foot tax rate" be subject to annual CPI adjustment in the same manner as all other regular business license tax rates and charges under the City's Business License Tax Code to mediate the costs associated with the secondary and tertiary effects of medical marijuana businesses.

7. Add provisions requiring a monthly remittance of business tax rather than quarterly. Medical marijuana collectives/cooperatives typically operate as entirely cash-based enterprises because banks will not offer accounts out of fear of violating federal laws. Accordingly, auditing such operations may prove to be extremely difficult. Requiring a monthly remittance will protect the City from losing out on tax revenue if a collective/cooperative goes out of business prior to the remittance period. This method will also allow the city to more closely monitor the revenues generated by these businesses which may indicate illegal transactions.

Each of the recommendations above are consistent with the definitions, rates and taxing methods utilized by other cities in California that currently regulate medical marijuana collectives/ cooperatives. Based on the above taxing assumptions as well as the regulatory assumptions outlined in Option #3, the projected annual revenue from medical marijuana collectives/ cooperatives could be approximately $1,000,000 per year (Exhibit 1).

Summary and Recommendation

Since enacting an ordinance prohibiting medical marijuana collectives/cooperatives in 2007 the Police Department, Community Preservation Division and City Attorney's Office have faced a constant challenge in both tracking new collectives/cooperatives and working through the necessary legal steps to closing them down. Partnerships with Federal agencies and nearby cities on enforcement have proven successful for short periods of time, but have not been shown to be a viable long-term solution.

A City-sponsored competing initiative to permit, but regulate and tax medical marijuana collectives/cooperatives will provide an opportunity for a limited number of medical marijuana businesses to responsibly operate within specified areas of the city. Further, it will allow the City to enforce strict operational standards and to collect both a regulatory fee and business tax to offset the costs associated with enforcement while providing qualified patients with safe access to medicinal marijuana.

FISCAL IMPACT

There is no fiscal impact associated with this action. Council will discuss options and may provide direction to staff.

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MF:rb
MF:RFCA - Medical Marijuana Initiative Analysis 2014

Exhibit 1: Projected Revenues Calculation Methodology

Medical Marijuana - General Fund Revenue Analysis

Planning Annual Compliance Inspection	Planning Permit Fee (CUP)	Business License Tax Registration & State Fee	Business License Tax Minimum Basic Tax Amount	Local State Sales Tax @ 1%*	Total Fixed Revenue
$2,000	$10,000	$33	$2,000	$15,000	$29,033

Gross Receipts Tax Revenue*		
1%	$15,000	
2%	$30,000	
3%	$45,000	
4%	$60,000	
5%	**$75,000**	**$75,000**
6%	$90,000	
7%	$105,000	
8%	$120,000	
9%	$135,000	
10%	$150,000	

Subtotal Per Dispensary	**$104,033**
x 8 Dispensaries	
Total	**$832,264**

*Based on estimated annual gross sales of $1.5 million

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Exhibit 1