



CITY OF SALINAS

COUNCIL STAFF REPORT

DATE: AUGUST 15, 2017

DEPARTMENT: CITY MANAGER'S OFFICE
CITY ATTORNEY'S OFFICE

FROM: ANDREW MYRICK, ECONOMIC DEVELOPMENT MANAGER
CHRISTOPHER A. CALLIHAN, CITY ATTORNEY

TITLE: GOVERNANCE OF COMMERCIAL CANNABIS BUSINESSES

RECOMMENDED MOTION:

Staff Recommends that the City Council take the following actions:

- 1) Adopt the proposed Ordinance amending Chapter 16B of the Salinas Municipal Code;
- 2) Approve the proposed Resolution related to application procedures for the issuance of additional commercial cannabis permits; and
- 3) Approve the proposed Resolution to implement the provisions of Chapter 19A, relating to taxes on commercial cannabis businesses.

RECOMMENDATION:

Staff recommends that the Council adopt the attached Ordinance and approve the attached Resolutions, which will enable staff to begin the implementation of further activities associated with regulating the medicinal commercial cannabis industry.

EXECUTIVE SUMMARY:

Based on Council feedback at the Council Meeting of July 11, 2017, City staff has prepared the materials necessary to allow the City to be able to review permit applications in a manner that will reduce the time required while maintaining standards, implement procedures to monitor and provide reporting to the Council and the community regarding the commercial cannabis industry, and implement the City's taxation protocols in accordance with Measure L.

BACKGROUND:

History of Cannabis Regulations

For many years, the cannabis plant (also known as marijuana and/or hemp) has been (and remains) a controlled substance under the Federal Controlled Substances Act. However, in recent decades debate has arisen regarding the potentially beneficial impacts of using cannabis to treat certain medical conditions. As of the date of this Report, 29 states and the District of Columbia have

passed laws providing for the use of cannabis for medical purposes, and an additional 16 states have passed laws allowing for the use of certain extracts from the cannabis plant to be used medicinally in certain situations.

Furthermore, debate has also arisen regarding the question of whether cannabis should be allowed to be used for recreational purposes. The argument in favor of legality is based on the theory that cannabis, like tobacco/nicotine and alcohol, can be consumed responsibly by adults if properly regulated. As of this date, seven states, including California, and the District of Columbia have legalized cannabis for recreational use.

Although California has been gradually permitting the possession and use of medicinal cannabis since 1996, in 2015 the California legislature significantly changed the industry by passing the Medical Cannabis Regulation and Safety Act (MCRSA), which created a licensing structure to allow for the legal cultivation, manufacture, and sales of medicinal cannabis and medicinal cannabis product. In response to this bill, the City Council in January 2016 adopted Chapter 16B of the Municipal Code regulating commercial cannabis businesses. Chapter 16B stipulated a limited number of four types of businesses, and provided regulations for these businesses. Additionally, Chapter 16B explicitly excluded recreational cannabis.

Two significant changes impacting the commercial cannabis industry in Salinas were approved by voters during the November 2016 election. The first of these was Measure L, a tax on commercial cannabis businesses placed on the ballot by the City Council that passed with nearly 75% of the vote. This resulted in the addition of Chapter 19A to the Municipal Code, which provides tax rates for commercial cannabis businesses and specifies the methods of collection for these taxes.

The second significant change that occurred in the November 2016 election was the passage of Proposition 64 (aka the Adult Use of Marijuana Act, or AUMA), which provided a framework for the legalization of recreational cannabis in California, effective January 1, 2018. As a result of this, the California legislature repealed MCRSA and incorporated its provisions, with some modifications, into AUMA, creating the Medicinal and Adult-Use Cannabis Regulation and Safety Act (MAUCRSA). The MAUCRSA was signed into law by Governor Brown on June 27, 2017, and became effective immediately. Several bills that would make additional changes to these regulations are under review in the legislature. State regulations are currently under development.

Background of Current Ordinance and Resolutions

Pursuant to Chapter 16B and the MCRSA, the City of Salinas developed regulations relating to the acceptance and processing of permits for commercial cannabis businesses (which were approved by the City Council on May 17, 2016), and began accepting applications for medical commercial cannabis businesses in June 2016. The process for reviewing these applications ran from July 2016 through May 2017, and was conducted by a Selection Committee. This Committee originally consisted of four City employees with guidance and leadership provided by HdL Consultants; however, upon the retirement of one of the Committee members, HdL assumed the additional role of serving on the Committee. The process originally consisted of a three-phase application review, with each phase scored or reviewed separately. Business interviews were conducted in January 2017, and the selected businesses were announced in May 2017.

During a meeting of the Council Finance Subcommittee on June 5, 2017, the members of the Subcommittee (Councilmembers Barrera, Davis, and Mayor Gunter) expressed concern regarding the permitting process (specifically regarding the length of time spent reviewing the applications) and with the limitations to the number of businesses provided in the Ordinance. The Subcommittee requested that staff bring a revised Ordinance to the July 11, 2017, City Council meeting in order to increase the number of permits available to Cultivation, Dispensary, and Manufacturing businesses from three to five per category, and creating a path forward for testing laboratories.

Upon receiving this feedback, staff conducted a thorough review of Chapter 16B with the Subcommittee's concerns in mind. While not all of the challenges associated with the permitting process were tied to the Ordinance, staff identified a number of changes, both major and minor, that could be modified to streamline application processing. In addition, staff identified additional business types (in addition to Cultivation, Manufacturing, Dispensaries, and Delivery) that had been effectively prohibited through the lack of a process for approval; procedures for approval for Testing Facilities and Distribution were added to the Ordinance.

On June 27, 2017, the MAUCRSA was signed into law, immediately changing the State's regulatory structure in significant ways. Staff promptly conducted a review of the MAUCRSA and made modifications to the proposed Ordinance – however, due to the July 4th holiday, staff was unable to conduct a comprehensive review prior to the hearing on July 11. Due to the upcoming Council break, staff made the decision to introduce the Ordinance on schedule, and to take the five-week break following the hearing as an opportunity for a more comprehensive examination.

At the City Council meeting of July 11, 2017, the Council requested clarification on a number of items, both regarding the proposed ordinance and relating to the implementation of Chapter 16B, regarding both the need expressed by Council to provide excellent customer service as well as to understand the impacts of that operation on City resources. The Ordinance, Resolutions, and additional information that are brought before the Council in this Report are intended to address many of these concerns.

ANALYSIS:

Ordinance

As discussed at the July 11 Council Meeting, the Ordinance presented makes a number of modifications to the permitting regime. The most significant modifications are:

- 1) Increase the number of permissible locations for Cultivation, Manufacturing, and Dispensaries from 3 to 5, and establishing a maximum of 5 Distribution permits;
- 2) Addition of an Administrative Permit for testing laboratories and Distribution locations under 500 square feet in size;
- 3) Allowed additional staff flexibility to review and approve applications located near certain sensitive receptors, particularly alcohol-related uses; and

- 4) Streamlined the application process by designating a Selection Committee to review Permits and moving some administrative functions to the City Manager's Office.

Since the Ordinance was introduced on July 11, staff has been able to more comprehensively review SB 94. A number of inconsistencies were identified between the City's existing law, which was developed under MCSRA, and the provisions of MAUCRSA. Changes have been made between the Ordinance provided on July 11 and the one before Council today for the purposes of making our Ordinance consistent with MAUCRSA. The City Attorney has opined that, because these changes are not significant and/or are designed to bring the Ordinance in compliance with another law, it is not necessary to reintroduce the Ordinance. These additional changes include:

- Correction of references to MCSRA to reference correct laws.
- Modification to definitions and other provisions to maintain consistency with MAUCRSA.
- Correction of Section references and/or drafting errors.
- Clarification regarding the counting of Delivery and Distribution Permits, based on the provisions of MAUCRSA.
- Clarify that applicants charged or convicted of a crime within the past ten years are ineligible to receive permits, except for cannabis-related crimes that were considered legal by the respective State at the time the crime occurred.

Resolution to Grant Staff Discretion in Developing Permit Review Processes

As noted above, one of the changes to the Ordinance is to empower staff, through the Selection Committee, to develop and implement review processes for applications for a commercial cannabis business. The current law requires all materials to be adopted by the City Council – while this method does have the positive advantage of being thoroughly vetted in a public setting, it also makes it much more difficult for staff to respond quickly to new information, and requires Council action for relatively minor changes. Under the new Ordinance, staff would continue to inform Council on a regular basis regarding the application process, as well as the industry generally, and Council would be able to provide feedback to staff. Applications guidelines would continue to be published and be available for the public, and staff would be available to respond to questions.

For example, Council has requested that staff examine the possibility of conducting some sort of closed review for applications that were not approved in the first round. Under current law, since Council has adopted a previous Resolution indicating the process to be followed, staff would need to prepare a new permitting process for Council approval, which could take several weeks. This process would need to be repeated for every round, with significant modifications requiring new Council action, potentially delaying processing of applications, depending on the issue. Under the proposed Resolution and Ordinance, staff could develop details around Council principles, and could make adjustments as necessary during the process.

On balance, staff believes that the advantages gained from flexibility and responsiveness outweigh any potential disadvantages created by requiring that all rule changes go through the City Council, and recommends that Council support the Resolution. The Resolution does stipulate that the next round of review would include only those applications submitted in the first round; a proposed permitting process has been provided later in this Report.

Resolution Implementing the Tax Provisions included in Chapter 19A

In November 2016, Salinas voters approved Measure L, which added Chapter 19A to the Salinas Municipal Code. This Chapter defines taxes that are to be disbursed by commercial cannabis businesses to the City of Salinas (these taxes are in addition to taxes and fees associated with other business types). Taxes would initially be set at \$15/square foot of canopy space for cultivation, and 5% of gross receipts for Manufacturing, Delivery, and Dispensary businesses; in May 2019, these amounts would increase to \$25/square foot and 10% of gross receipts, respectively, with annual increases to the cultivation tax annually thereafter. Chapter 19A also provides collection procedures for the tax and interest rates and penalties for making late payments.

Chapter 19A-10.120 indicates that late payments shall be subject to a 25% penalty, plus an interest rate to be determined by the Council. This Resolution would set that interest rate at 1% per quarter.

NEXT STEPS:

Upon acceptance by the Council of the Ordinance and Resolutions included in this Report, staff intends to proceed with implementation as defined below. No action is being requested of Council regarding the information below; rather, it is being provided so that Council may provide feedback and input to staff.

Permit Round 1B

During the last Council meeting, Council requested that staff explore the possibility of awarding the additional permits created by the updated Ordinance to the applicants who applied for but did not receive a permit, or to conduct a new review in a “closed” round of applications. Upon review, staff proposes the following:

- Staff would conduct a follow-up, “closed” round for only those applicants that applied for permits but were not approved in Round 1 (Round 1B). A list of applicants in each category who would be eligible to participate in this round, including Round 1 final scores, is attached to this Report.
- The Selection Committee would include the same staff members (Andrew Myrick, Megan Hunter, and Matt Pressey) in order to maintain the institutional knowledge for these applications. The fourth member, formerly occupied by Hdl Consultants, would be filled by David Shaw from the Salinas Police Department.
- Prior to September 14 (the effective date of the Ordinance), the Selection Committee would meet with the applicants and provide detailed feedback regarding the rationale for awarding the scores that they were awarded. This would enable the applicants to make any needed corrections and develop updated materials. Staff would use the opportunity to develop a revised single-phase review process with an updated scoring rubric.
- On and around September 14, applicants would be allowed to indicate their continued interest in obtaining a permit from the City, and would be allowed to submit additional information to supplement their original application. There would be no application fee.
- The Selection Committee would review the materials, conduct interviews, and score the applications between September 18, 2017 and October 6, 2017. Given the limited number

of applicants and most Committee Member's familiarity with the applications, staff believes this timeframe is realistic.

- The Selection Committee would announce any additional permits to be awarded during the week of October 9, but no later than October 13, 2017.

Permit Round 2

If any permits remain unallocated after Round 1B, staff will explore the possibility of implementing a second, open permitting round. Depending on response and interest, staff may afterwards continue to open future Rounds, or may develop an "open application" process.

Administrative Permits

Staff will develop forms and procedures for the issuance of Administrative Permits. It is anticipated that these will be completed by the effective date of the Ordinance (September 14).

Work Permits

The Ordinance requires all potential employees for commercial cannabis businesses to obtain a Work Permit from the Police Department. The Police Department currently has procedures in place for conducting background checks on prospective card room employees. The Department feels that these procedures would be adequate and appropriate for screening potential employees of commercial cannabis businesses. Internal procedures require slightly more development, but it is expected that the Department will be prepared to begin the intake of applications in the near future.

Monitoring/Reporting

The City Manager's Office will provide support in maintaining a record of important dates and events, such as renewals, and in the collection of data at the time of renewal. Updates to the Council regarding the performance and the impact of commercial cannabis industry on both the economy and the municipal operations of City of Salinas will be provided at regular intervals as stipulated in the Ordinance.

Impact of City Operations/Establishment of Fee Structure

During the July 11 City Council meeting, Council requested information regarding the ongoing costs the City may incur in monitoring and regulating these types of businesses. As it is very difficult to estimate at this time what the City costs would be in a comprehensive fashion, staff has analyzed the likely impacts of individual actions on specific Departments. These impacts are summarized below:

City Attorney's Office

- Review and Interpretation of City Ordinances
 - o This is a standard service provided to the City. Staff will monitor time spent on this activity, and, if the amounts are excessive, will return to Council with a remedy at a later date.
- Assistance in the Review and Drafting of Commercial Cannabis Permit Applications
 - o The City will charge Permit Application Fees to offset these costs. These fees will be examined regularly.

City Manager's Office

- Review of Administrative Permits
 - o Minor costs for time and application development, to be offset by fees collected.
- Coordination of Selection Committee
 - o Inconsistent but significant time investment selecting and managing Selection Committee. Costs to be offset by permit application fees.
- Reporting and Departmental Coordination
 - o Coordination of efforts between Departments, and collection of data from multiple sources to provide periodic reports to Council and Community. Potentially significant time investment, offset by monitoring fee.
- Tracking of Significant Dates (ie expiration dates)
 - o Moderate costs to be made up from collection of monitoring fee.

Community Development Department

- Review of Land Use Permit Applications
 - o Unknown staff time investment, a significant portion of which would be offset through Permit application fees.
- Code Enforcement Activity
 - o Unknown costs ranging from negligible to very significant, depending on the number and validity of complaints. Costs to be offset through cost recovery fees and citation payments.

Fire Department

- Compliance Inspections
 - o Fire Inspectors are required to conduct annual inspections of all businesses. Costs are offset through fees.
- Review of Permits and Hazardous Materials Plans
 - o Minor to Moderate costs of staff time, offset through the collection of permit application fees.
- Emergency Response
 - o Response to 911 calls or as otherwise needed, as with all businesses. Unknown whether incidence of these responses will exceed normal baseline levels. Cost recovery may be possible depending on the individual circumstances.

Police Department

- Emergency Response
 - o Response to 911 calls or as otherwise needed. Unknown whether incidence of these responses will exceed normal baseline levels. Cost recovery may be possible depending on the individual circumstances.
- Tracking of Incidents
 - o Minor to significant (depending on frequency and type of calls made) costs, potentially offset through monitoring fees.
- Review of Permits and Site Security Plans
 - o Minor to Moderate Costs of Staff time, to be offset through permit application fees.
- Review and processing of Work Permits/ Issue Cannabis ID Cards
 - o Significant staff time for permit intake and processing, to be offset through permit application fees.

As noted, in several instances the activities mentioned include activities pursued as a normal part of business, and fees are already in place to cover the City's costs of implementation. There are additional fees which will need to be established or modified to cover some of these costs – however staff is still analyzing the appropriate fee amounts. Staff will present a Resolution establishing any necessary fees to the Council prior to the effective date of the Ordinance.

Recreational Use

Recreational (or Adult) use is not addressed here. Staff anticipates bringing an updated Ordinance and/or Resolution, as deemed appropriate, prior to the effective date for the legalization of recreational cannabis businesses (January 1, 2018).

CEQA CONSIDERATION:

The City Council's approval of the proposed Ordinance and/or Resolutions is exempt from environmental review under the California Environmental Quality Act (CEQA) because it can be seen with certainty that there is no possibility that the activity in question may have a significant effect on the environment. [CEQA Guidelines Section 15061(b)(3)]

STRATEGIC PLAN INITIATIVE:

The City Council's approval of the proposed Ordinance and/or Resolutions is not among the City Council's current goals and objectives as identified in the City Council's current Strategic Plan.

FISCAL AND SUSTAINABILITY IMPACT:

The various items are expected to have the following financial impacts:

- 1) The proposed Ordinance would most likely generate unknown but significant additional revenues for the City relative to existing law. This would primarily be accomplished by the proposed increases in the number of available permits, which would in turn provide an

increase in revenues. Although increasing the number of permits could also result in an increase in City costs associated with permitting, monitoring, and enforcement, it is expected, although not assured, that revenues generated would be significantly greater than costs incurred.

- 2) The proposed Resolution providing additional staff discretion in structuring the permitting process would result in minor reductions to staff time and costs due to modifications in procedures.
- 3) The proposed Resolution establishing procedures to implement Chapter 19A would establish the interest rate for late payments and allow staff to begin collection of the appropriate taxes, which would likely result in additional revenues being brought in to the City of Salinas. The exact amount will vary depending on the number of businesses and their commercial success, but it is expected to be significant. The use of these funds would be unrestricted and could be used for general governmental purposes.

It should be noted that these projections are based only on existing law and the proposed Ordinance. A review of the potential impacts of permitting or not permitting recreational cannabis will be provided at a later date.

ATTACHMENTS:

Proposed Ordinance Amending Chapter 16B of the Salinas Municipal Code
Proposed Resolution Granting Discretion to Staff in Developing Permit Application Procedures
Proposed Resolution Establishing the Interest Rate for Unpaid Cannabis Tax
Round 1B Eligible Applicants and Round 1 Scores