



# PROPOSITION 64 IN SOCAL

BY CHARLIE HARRIS '19

Photo Credit: Jennifer Martin | *Wikimedia Commons*

In 2016, California voters passed Proposition 64, The Adult Use of Marijuana Act or AUMA. Fifty-six percent of voters across the state, and majorities in Los Angeles, Orange, Riverside, and San Bernardino Counties, voted in favor of the ballot initiative. The widely publicized result of the measure was the legalization of recreational cannabis for adults over the age of 21. Californians demonstrated that they wanted to legalize and regulate marijuana, just like alcohol and tobacco. However, bringing the existing illegal marijuana industry into the light is no mean feat. This drug would need an entirely new regulatory structure to address business regulation and taxation of an entirely new product. At the state level, Proposition 64 gave California's Bureau of Cannabis Control authority to impose state regulations on the marijuana industry and established a 15% tax on retail sales, but it also gave local governments the power of final regulatory authority over the marijuana industry in their jurisdictions. That meant local governments across the state were free to determine exactly what they wanted to allow or

prohibit in their communities. Since then, cities across the state have been wrestling with how to approach this thorny public policy question. Recreational sale became legal on January 1, 2018, but many cities have yet to finalize, or even begin drafting, marijuana business regulations. This article will examine the regulatory structures of two cities in Southern California, Los Angeles and Moreno Valley, with an eye towards the broader applicability of their policies.

## Prop 64 Voting in Southern California

|                       | Yes   | No    |
|-----------------------|-------|-------|
| Los Angeles County    | 59.5% | 40.5% |
| Orange County         | 52.0% | 48.0% |
| San Bernardino County | 52.5% | 47.5% |
| Riverside County      | 52.9% | 47.1% |
| Statewide             | 57.1% | 42.9% |

Source: California Secretary of State, Statement of Vote, <https://www.sos.ca.gov/elections/prior-elections/statewide-election-results/general-election-november-8-2016/statement-vote/>

Each municipality will be facing a choice between regulating (and taxing) commercial activities related to marijuana or prohibiting them. Southern California, with over a hundred cities and four large counties, is a perfect place to observe and analyze the range of approaches local governments are taking to the task the AUMA sets out for them. Designing and implementing a new regulatory framework and taxation scheme is, however, a daunting task even for experienced policy makers. Many local governments do not have the wherewithal to undertake this project from scratch. Instead, they will be looking to sister municipalities that have taken the lead on this issue and are already implementing regulations.

The cities that do take on this task have a wide range of options for dealing with marijuana sales in their jurisdiction. The choices range from exceptionally permissive policies allowing for commercial cultivation, distribution, sales, and grows for personal consumption, to banning nearly every action permitted under state law. Proposition 64 was designed to allow for this wide range of permissiveness so that local communities could retain some control over cannabis in their communities. According to an analysis of marijuana ordinances conducted by the *Orange County Register*, nearly all of the 35 cities in Orange County have essentially banned cannabis businesses. The only portion of Prop 64 that they allow is indoor cultivation for personal use. The city of Santa Ana, however, has gone in a different direction than its neighbors and has allowed nearly all forms of cannabis business permitted by Proposition 64. Santa Ana joins Los Angeles, Moreno Valley, San Bernardino, and a few other Southern California cities, aggressively leaning in to this new industry. Examining the regulatory framework of these early adopters is helpful to see how cities are approaching this task.

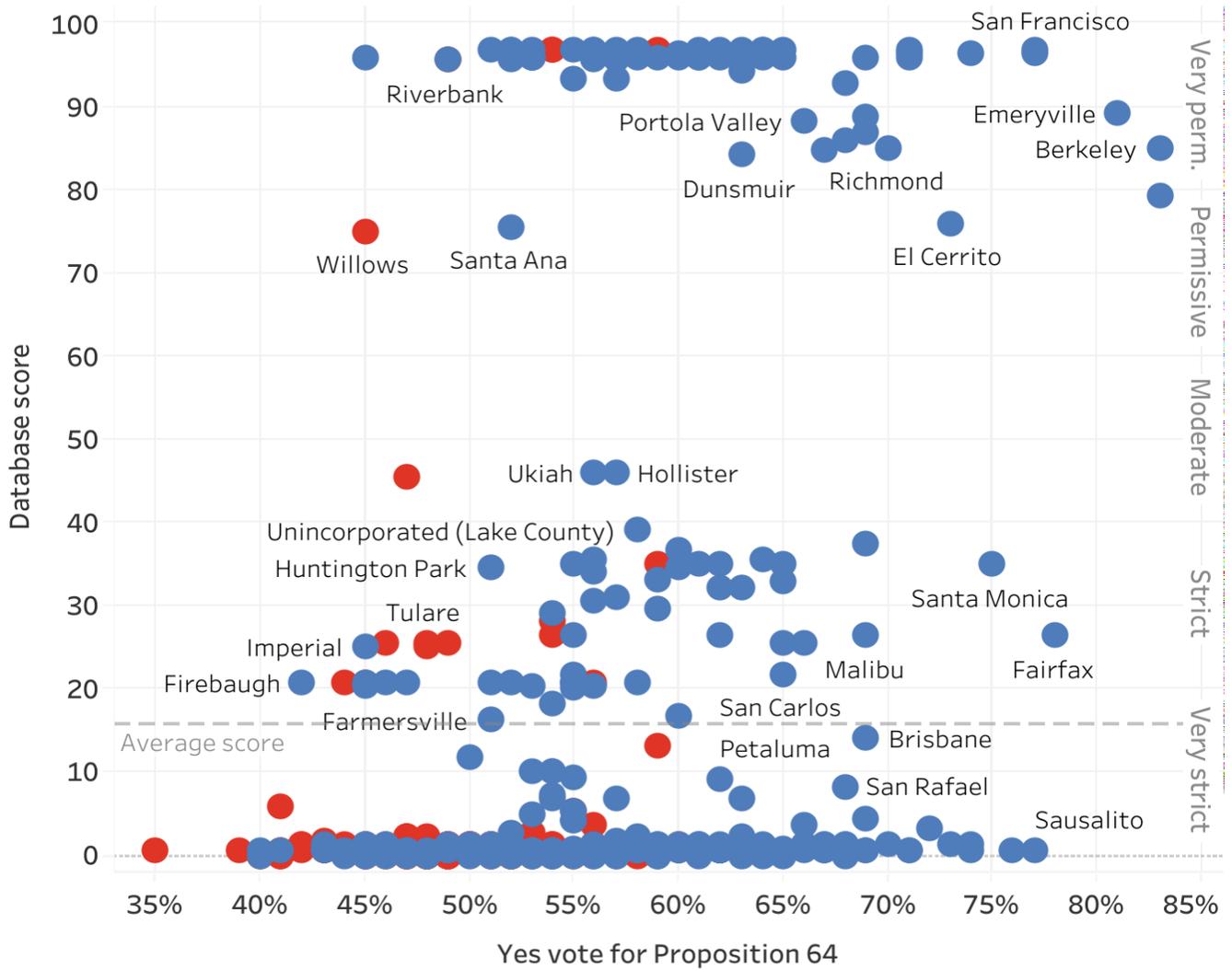
As the largest city in the state, Los Angeles has the resources and expertise to enact a complex new regulatory structure. Of course, the significant differences between LA and many other cities means that its policies are not the

easiest model to apply to other jurisdictions. Still, there are valuable takeaways from LA's approach. Sixty-five percent of voters in LA voted in favor of Proposition 64, handing city leaders a substantial mandate to permit and regulate cannabis business. However, the mayor and city council went back to the voters a few months later with a local initiative, Measure M, to affirm the voters' desire to permit, regulate, and tax cannabis within the city. Measure M passed with 80% support on March 7, 2017. Measure M levied a 10% gross receipts tax on the sale of recreational marijuana, a 5% gross receipts tax on medical marijuana, a 2% tax on gross receipts by cultivators, and a 1% gross receipts

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tax on delivery businesses. In addition to the taxes, Measure M granted LA the authority to create a Department of Cannabis Regulation (DCR) and an appointed Cannabis Commission. The Commission was intended to study other cannabis regulations and make recommendations to the city council about which policies to implement. The DCR is the agency charged with issuing licenses, inspecting licensed businesses, and enforcing the laws against violators. A key difference between LA and many other cities is that it has the resources and capability to form an entire commission and department to oversee these regulations. The scale of its operation is much larger, so it needs a correspondingly larger bureaucratic apparatus.

# MARIJUANA PERMISSIVENESS COMPARED TO PROP 64 SUPPORT



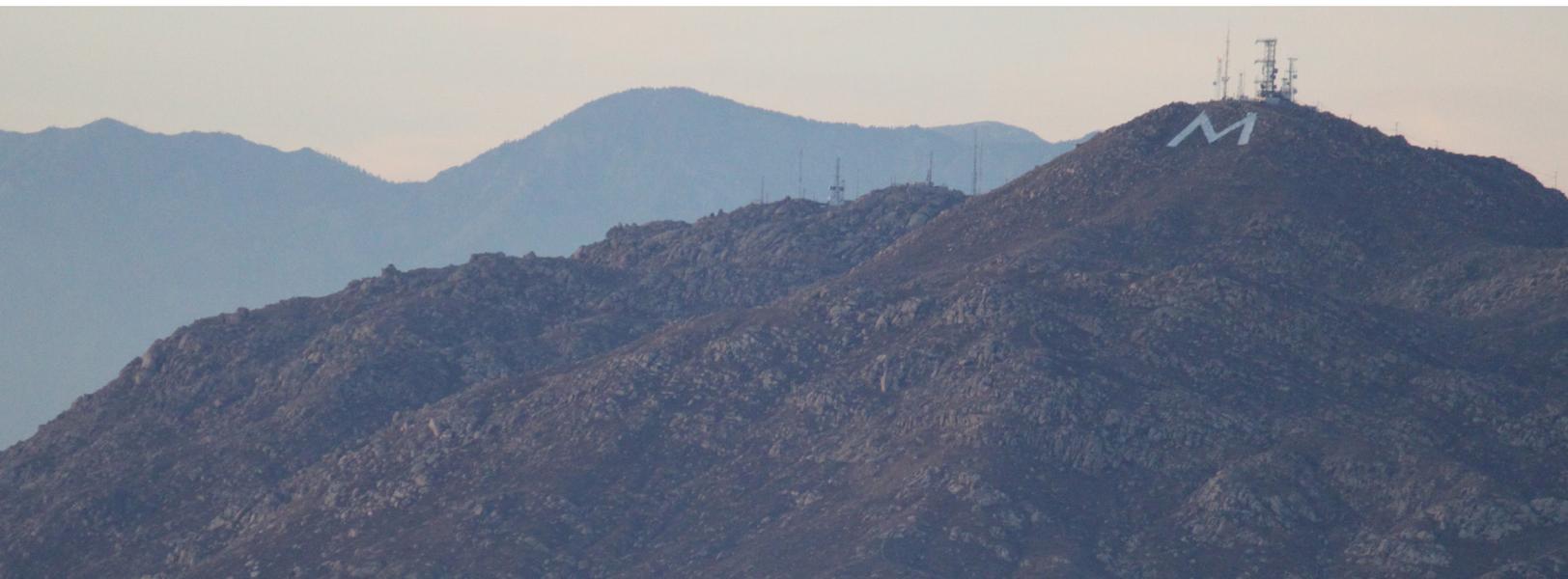
Where most voters are registered...

- Democrats
- Republicans
- No party preference

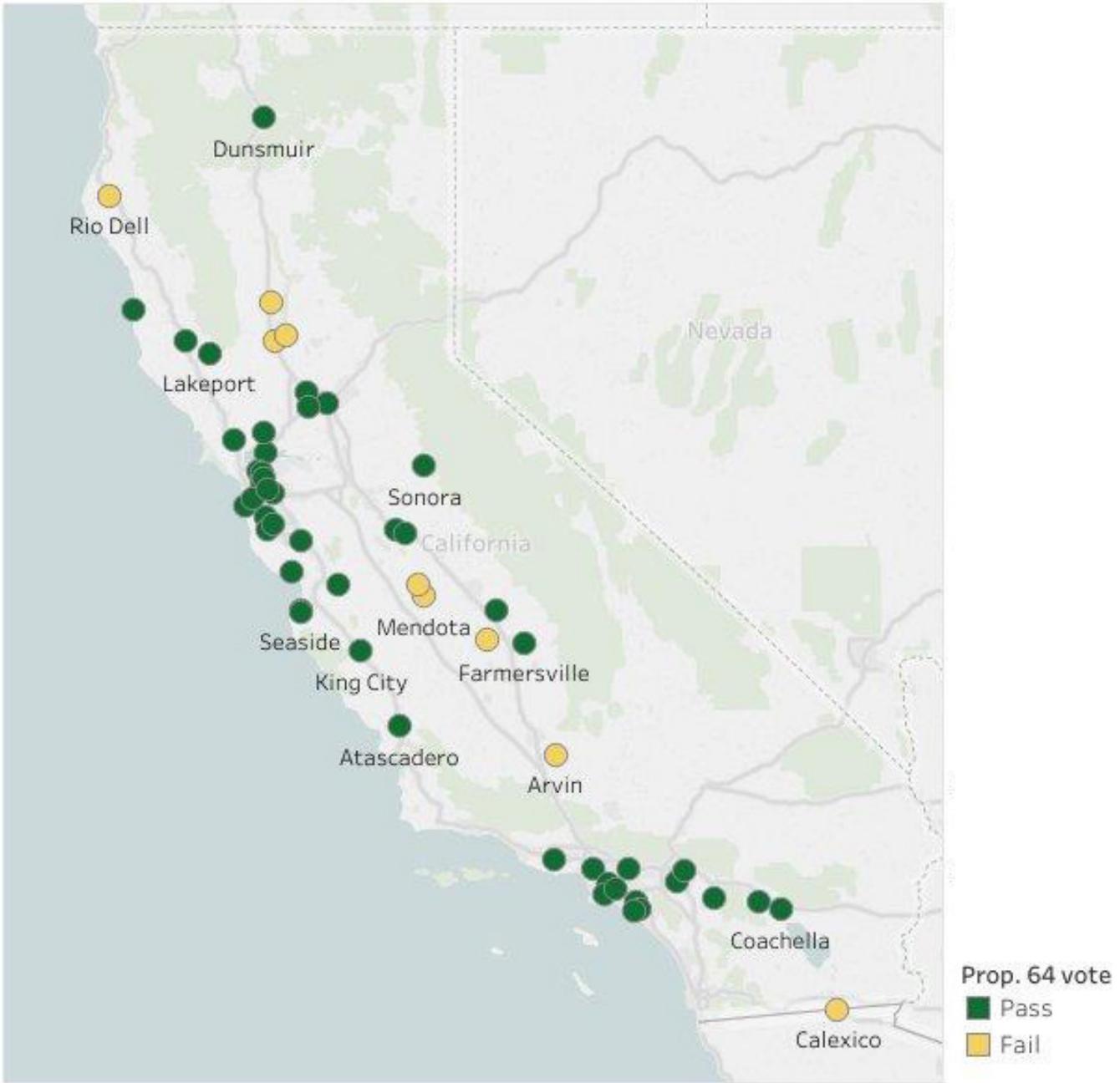
Source: Orange County Register, Scores based on Southern California News Group database, as of April 2, 2018 (Ian Wheeler, SCNG).

After the creation of the DCR and Cannabis Commission, regulators in LA drafted a final set of rules that was passed by the city council in December of 2017. The final rules outlined the requirements for getting a business license and established an online portal for filing applications. Applicants are required to submit standard information like a business plan and proof of ownership for their premises. In addition, there are a few requirements that are unique to marijuana businesses. Retail locations are required to be licensed businesses and are required to have video surveillance equipment that monitors all entrances, exits, and any other interior area where marijuana would be handled. They also need to hire or contract security personnel to guard the premises. Licensees also need to designate a “neighborhood liaison” whose contact information will be posted publicly and who can address issues raised by community members 24 hours a day. Businesses will also be inspected for compliance with all regulations by DCR employees before receiving final approval for a license and thereafter on a regular basis established by the DCR. To date, Los Angeles has licensed 167 commercial cannabis businesses, with more to come.

Of particular note in LA’s regulations is the inclusion of a social equity program. This program is intended to use the new legalized marijuana businesses to help offset historical negative effects of cannabis related criminal convictions. The social equity program gives priority licensing to two groups of people, low income individuals with previous cannabis related criminal convictions prior to the passage of the AUMA and low-income individuals who are residents of communities disproportionately impacted by cannabis arrests. LA is mandating that two-thirds of new licenses for retail stores and half of all other businesses receive a social equity license. Non-social equity business owners can still qualify for a social equity license if they pay additional fees to the city that will go towards assisting the social equity owners. Social equity licensees receive expedited processing and renewal of their licenses, assistance with regulatory compliance, and potential access to an “Industry Investment Fund.” That industry fund will be comprised of the fees paid by non-qualifying owners who still wish to receive a license under the social equity quotas. The goal of this program is to use the legal cannabis industry to benefit communities who have been disproportionately impacted by the War on Drugs. To that end, the city is doing what it can to redirect some of the capital flowing into



# CITIES THAT ALLOW AT LEAST ONE TYPE OF RECREATIONAL MARIJUANA



Source: Orange County Register, Scores based on Southern California News Group database, as of April 2, 2018 (Ian Wheeler, SCNG).

this growing industry towards developing business to support the disadvantaged communities. Los Angeles is the only city in Southern California whose marijuana regulations include a social equity program. However, in September of 2018 Governor Jerry Brown signed legislation sponsored by Steven Bradford (D-Gardena) to provide technical and financial support to local governments wishing to implement their own cannabis social equity programs. SB 1294 would require the California Bureau of Cannabis Control to draft a model ordinance by July of 2019 for local governments to use.

While Los Angeles is at the forefront of this regulatory task, small and mid-size cities have different needs than those of a metropolis. The city of Moreno Valley, 60 miles to the east, has also moved quickly to establish commercial marijuana regulations. With a population of 205,000 people, Moreno Valley is easier to compare with the average city in Southern California. Its regulatory regime is comparatively much simpler than LA's. Moreno Valley passed its final regulations in April of 2018, and the city council placed a measure on the November 2018 ballot asking for authority to levy a tax on recreational marijuana sales. The ordinance allows for a maximum of 27 cannabis businesses in the city, including eight dispensaries, two testing facilities, eight indoor cultivation facilities, five manufacturing facilities, two distribution centers, and two microbusinesses. Moreno Valley is allowing all forms of cannabis businesses authorized under the AUMA. The land use ordinance requires a buffer zone of at least 600 feet between any cannabis business and a school or day care center.

Moreno Valley adopted a fee structure which intends to recoup the costs of licensing and regulating the businesses, which it estimates will be about \$58,000 a year for each business. These fees are simply a break even point, and voters must approve the previously mentioned ballot measure before taxes can be levied on recreational cannabis sales. Moreno Valley also hired a government consulting firm, HDL Consultants, to help design

and implement its marijuana program. Consulting firms like HDL supply specific technical expertise that smaller cities often lack. They also charge correspondingly high rates. Moreno Valley is paying HDL \$161,500 for the first year and then \$281,000 annually for the next five years. While the advice such firms offer is often necessary, costs like that can eat into the tax revenue cities hope to raise.

ONLY ONE IN SEVEN CALIFORNIA CITIES HAS DECIDED TO ALLOW RECREATIONAL CANNABIS DISPENSARIES AND ONLY ONE IN THREE ALLOWS ANY TYPE OF CANNABIS BUSINESS AT ALL.

The cannabis tax measure on the ballot in Moreno Valley would grant the city council authority to levy a tax of up to 8% on recreational sales. However, city officials have stated that they intended to aim for a tax of around 5% to undercut the rates of neighboring jurisdictions like Perris and San Jacinto. The *Press Enterprise* reported that at that lower rate, the city expects to raise \$2.2 million a year according to Chief Financial Officer Marshall Eyerman. The scale of Moreno Valley's program is considerably smaller than Los Angeles, with its hundreds of businesses and 10% tax on gross receipts, but that model may be more in line with the capacities of most local governments in California. Even with the support of an outside consulting firm, Moreno Valley is only looking to allow eight dispensaries.

A study (as of April 2018) by the Southern California News Group found that only one in seven cities allows recreational cannabis dispensaries, and only one in three allows any type of cannabis business at all. Since fewer cities than expected have implemented commercial licensing regulations, statewide marijuana revenue has come in lower than expected for this year. Policymakers at the state and local level have incentives to continue expanding the reach of recreational marijuana so that they can continue to expand this new revenue stream. Local governments that were hesitant to be the first to implement commercial cannabis can now look to cities like Los Angeles and Moreno Valley to get a sense of what an effective

regulatory program looks like. Other cities, like those in Orange County, can continue to ban all commercial activity. Local control was the central component of the commercial side of Proposition 64. Local governments in California are exercising their authority to establish rules that fit their own communities. With many examples of the various paths cities can take, the commercial marijuana industry should continue to develop across the state as more local governments decide how to approach this regulatory challenge.

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