

CITY OF SANTA ROSA
CITY COUNCIL

TO: MAYOR AND CITY COUNCIL
FROM: DAVID GUHIN, DIRECTOR
PLANNING AND ECONOMIC DEVELOPMENT

SUBJECT: RESOLUTION OF THE COUNCIL OF THE CITY OF SANTA ROSA DECLARING A FISCAL EMERGENCY IN THE CITY AS A RESULT OF THE RECENT ENACTMENT OF THE MEDICAL CANNABIS REGULATION AND SAFETY ACT AND PASSAGE OF CALIFORNIA STATE PROPOSITION 64 (ADULT USE OF MARIJUANA ACT); AND

RESOLUTION OF THE COUNCIL OF THE CITY OF SANTA ROSA (1) ORDERING A SPECIAL ELECTION TO BE HELD ON TUESDAY, JUNE 6, 2017 FOR THE PURPOSE OF SUBMITTING TO SANTA ROSA VOTERS AN ORDINANCE OF THE CITY OF SANTA ROSA AMENDING CHAPTER 6-04 OF THE SANTA ROSA CITY CODE AND ADDING CHAPTER 6-10 OF THE SANTA ROSA CITY CODE TO AUTHORIZE THE CITY OF SANTA ROSA TO IMPOSE A BUSINESS TAX ON CANNABIS BUSINESSES, (2) APPROVING BALLOT LANGUAGE, (3) PERMITTING THE FILING OF BALLOT ARGUMENTS, (4) DIRECTING THE CITY ATTORNEY TO PROVIDE AN IMPARTIAL ANALYSIS, AND (5) SETTING INITIAL TAX RATES FOR A 2-YEAR TERM.

AGENDA ACTION: RESOLUTIONS

RECOMMENDATION

It is recommended by the Planning and Economic Development and Finance Departments that the Council adopt the following:

a. Resolution to declare a fiscal emergency as a result of the recent enactment of the Medical Cannabis Regulation and Safety Act and passage of Proposition 64 (the Adult Use of Marijuana Act); and

b. Resolution to (1) order a special election to be held on Tuesday, June 6, 2017 for the purpose of submitting to Santa Rosa voters an ordinance of the City of Santa Rosa amending Chapter 6-04 of the Santa Rosa City Code and adding Chapter 6-10 of the Santa Rosa City Code to authorize the City of Santa Rosa to impose a

ADOPTION OF AUTHORIZATION TO IMPOSE CANNABIS TAXATION
PAGE 2 OF 7

business tax on cannabis businesses, (2) approving ballot language, (3) permitting the filing of ballot arguments, (4) directing the City Attorney to provide an impartial analysis, and (5) setting initial tax rates for a 2-year term.

EXECUTIVE SUMMARY

On November 5, 1996, the California State election passed ballot measure Proposition 215, known as the “Compassionate Use Act,” legalizing medical use of cannabis. In September, 2015, the State enacted the Medical Cannabis Regulation and Safety Act (MCRSA), establishing a state licensing framework and authorizing local regulation of medical cannabis. The City has adopted interim regulations and is in the process of developing comprehensive medical cannabis policies.

On November 8, 2016, the California State election passed ballot measure Proposition 64, known as “the Adult Use of Marijuana Act.” Proposition 64 legalizes adult recreational use of cannabis, brings businesses that support adult recreational cannabis use into a regulated market, and allows the City of Santa Rosa to enact local regulations on such businesses in addition to the regulations that will be imposed by the state.

With the enactment of MCRSA, the passing of Proposition 64 and the City’s support and permitting of medical cannabis business through adopted interim measures and the anticipated comprehensive policies, the City has and will incur substantial costs to regulate newly-legalized cannabis businesses, including considering, adopting and enforcing regulations, administering associated business permits, providing for business inspections, supporting public safety, protecting the environment, providing economic development analysis and review to support policy decisions and education/outreach to the industry, and providing information and educational materials to the community. The City’s current business tax ordinance, which applies to all businesses operating in Santa Rosa, does not allow the City to impose a high enough tax on cannabis businesses to generate the necessary financial resources to support the unique needs of this emerging industry as described above. In light of the imminent financial burdens on the City caused by the evolving cannabis industry, the enactment of MCRSA and the passage of Proposition 64, Staff recommends the Council declare a fiscal emergency.

In order to pay for the expected costs of authorizing and regulating cannabis businesses, staff also recommends that the Council submit an ordinance to the voters that would impose a local business tax on the cannabis industry and authorize the Council to set appropriate rates, subject to specified caps, sufficient to cover the costs to the City of allowing this emerging industry to operate in Santa Rosa. The proposed tax is not a sales tax and would not be imposed directly on cannabis users or consumers.

The declaration of a fiscal emergency requires a unanimous vote of all members of the City Council who are in attendance for this item. Doing so will allow the City to bring the

ADOPTION OF AUTHORIZATION TO IMPOSE CANNABIS TAXATION
PAGE 3 OF 7

proposed ballot measure to the voters at the June 6, 2017 election – when the City is also expected to submit an additional measure to the voters – as a general tax measure requiring approval by only a simple majority of the City’s voters. Without such a unanimous declaration of fiscal emergency, the City must wait until the next City General Election in November 2018 to submit a tax measure requiring approval of only a simple majority of voters.

On February 14, 2017, the Council approved appointment of an ad hoc subcommittee to draft a proposed argument in support of the tax measure, to be subject to full Council approval. That draft argument will be presented to the Council for approval on March 14th. The Council also authorized the ad hoc subcommittee to prepare and submit, without need for further Council approval, a rebuttal argument, if needed.

BACKGROUND

On November 5, 1996, the California State election passed ballot measure Proposition 215, known as the “Compassionate Use Act,” legalizing medical use of cannabis. In September, 2015, the State legislature enacted and the governor signed into law the Medical Cannabis Regulation and Safety Act (MCRSA), establishing a state licensing framework and authorizing local regulation of medical cannabis. Over the past year, the Council’s Medical Cannabis Policy Subcommittee has been working with staff and with cannabis industry stakeholders to develop comprehensive policies to regulate medical cannabis businesses within the city limits.

On November 8, 2016, the California State election passed ballot measure Proposition 64, known as “the Adult Use of Marijuana Act.” Proposition 64 legalized adult recreational use of cannabis and brings businesses that support that use into a regulated market. Proposition 64, like state laws regulating medical cannabis, allows the City of Santa Rosa to enact local regulations on the cannabis industry in addition to the regulations that will be imposed by the state.

With the passing of Proposition 64, the enactment of MCRSA and the City’s existing and anticipated cannabis regulations, the City of Santa Rosa anticipates incurring substantial costs associated with the newly-legalized cannabis industry. Expenditures are estimated to be a total of at least \$1,000,000 annually, including:

- \$250,000: Code Enforcement of City business regulations
- \$200,000: Policy development and administration
- \$150,000: Legal support and oversight
- \$150,000: Public Safety
- \$150,000: Non-recoverable permit, planning and inspection
- \$100,000: Education, Workshops, Outreach (for the industry and for the community)
- \$50,000: Economic impact research and studies

ADOPTION OF AUTHORIZATION TO IMPOSE CANNABIS TAXATION
PAGE 4 OF 7

The City cannot recover its full costs of allowing the cannabis industry to operate in Santa Rosa under the City's current general business tax provisions because the general business tax is capped at \$3,000 per year. Such a low business tax would not generate adequate resources to support the unique needs of the cannabis industry. A cannabis industry specific business tax is needed to ensure that general fund resources used for other critical City services will not be exhausted as a result of allowing this emerging industry to operate in Santa Rosa.

Staff recommends all Council members in attendance for this item vote unanimously to declare a fiscal state of emergency based on the passage of Proposition 64, the enactment of MCRSA and the emerging City regulations. By doing so, the Council may submit the proposed ballot measure to the voters at the June 6, 2017 election -- the same election the City is considering submitting an additional measure to the voters -- as a general tax measure requiring approval by only a simple majority of voters. Without such a unanimous declaration, the Council must wait until the next City General Election in November 2018 to submit a tax measure requiring approval of only a simple majority of voters.

The Planning and Economic Development and Finance Department staff also recommend that Council, by resolution, submit the proposed tax measure to the voters at the June 6, 2017 election. If adopted by the voters, the proposed ordinance would authorize the Council to implement a cannabis-specific tax, rather than the City's existing general business tax, on cannabis-related businesses -- including commercial cultivators, nurseries, distributors, manufacturers, and dispensaries.

The proposed measure will be printed on the ballot as follows:

“Shall an ordinance be adopted authorizing a cannabis business tax in the City of Santa Rosa on cultivation businesses up to \$25 per square foot of cultivation area (annually adjusted by CPI) or 8% of gross receipts, and on cannabis manufacturing, distribution and dispensary businesses up to 8% of gross receipts, to maintain general funds for City services and to address cannabis industry impacts, with all funds subject to audits and staying local, generating undetermined revenue until repealed?”

If adopted by the voters, the proposed ordinance would authorize the City Council to implement a business tax on commercial cannabis cultivators of either up to a maximum of rate \$25 per square foot of cultivation space, adjusted annually by the most recent change in the annual Consumer Price Index, or up to 8% of gross receipts, as the Council may choose. The proposed ordinance would also authorize the Council to implement a business tax on cannabis manufacturing, distribution and dispensary businesses of up to 8% of gross receipts.

However, the City recognizes the volatility of the newly-legalized cannabis market, and both staff and the City Council Medical Cannabis Policy Subcommittee recommend adoption of limited initial tax rates to balance the financial need of the City to support

ADOPTION OF AUTHORIZATION TO IMPOSE CANNABIS TAXATION
PAGE 5 OF 7

this industry and the viability of the industry itself. With the uncertainty of the evolving industry both at the local and state level, it is recommended that Council retain flexibility to ensure a sustainable and responsible approach to management of cannabis in our community. Under the proposed ballot measure, the Council will have the authority to adjust tax rates every two years, but never to exceed the maximum rates authorized by the voters. Setting a rate for multiple years provides greater certainty to the industry and will allow for collection of data and information to inform the Council for any potential rate changes in the future.

The initial rates, to be set by resolution, will go into effect if the ballot measure passes on June 6, 2017. The initial rates proposed are as follows: Cultivation 2% of gross receipts; Manufacturing 1% of gross receipts and Dispensaries (recreational only) 3% of gross receipts. It is anticipated that commercial recreational sales will not occur until after 2018, until the state begins issuing permits and the Santa Rosa City Council determines whether to authorize commercial recreational cannabis operations within the city limits.

In light of concerns that the local tax could overburden the emerging industry, it is proposed that the ordinance require a super majority vote of the City Council if the tax rate imposed by the Council, either for cultivation or for other cannabis businesses, is to exceed 5%. In addition, to address the issue of compounding taxation across multiple business types in the cannabis supply chain, it is being recommended that ordinance limit the taxation points to cultivation (including nurseries), manufacturing, distribution and dispensaries, and to exclude transportation, testing and other support services.

The proposed ordinance to be submitted to the voters also amends the General Business Tax chapter of the Santa Rosa City Code to make clear that cannabis businesses subject to the cannabis industry tax will need not also pay the city's general business tax. Conversely, those business not required to pay the cannabis business tax, as discussed above, will be required to pay the city's standard business tax.

Under the proposed measure, Council would have the authority to adjust tax rates in two year terms by resolution. The proposed measure permits Council the discretion to set different tax rates for businesses supporting medical cannabis use than the rates set for businesses supporting adult recreational cannabis use, in addition to setting a tax rate for some business types and not others. The City will continue to work with industry stakeholders and residents to review and develop a successful financial and policy framework for setting and adjusting the cannabis business tax rate within the limits set by the voters.

The City recognizes that businesses will be bearing many initial costs as they adjust to the new legal environment and adhere to State of California regulations. As such, imposed tax rates are intended to secure funding for the needs of the community, while not overburdening the market. Staff will continue to monitor the economic impact of the industry and its effect on overall business climate in the city to evaluate and report to the Council. In coming years, tracking and tracing industry trends will provide crucial

ADOPTION OF AUTHORIZATION TO IMPOSE CANNABIS TAXATION
PAGE 6 OF 7

data on gross revenues generated at various points in the supply chain, thereby enabling the Council to better confirm what taxation rates are the most appropriate.

Finally, to give the Council the ability to make future adjustments to the implementation and enforcement provisions of its business tax provisions, and to respond to changes in state law governing the businesses operating in Santa Rosa, without putting additional measures on the ballot, the proposed ordinance gives the Council the authority to adopt, by ordinance, limited changes to the both the cannabis industry tax provisions and the general business tax provisions so long as no changes are made to the tax rates authorized by the voters.

On February 14, 2017, in anticipation of the possible cannabis tax ballot measure and in accordance with Elections Code sections 9282 and 9287, the Council authorized the appointment of a Council ad hoc subcommittee to draft the argument in support of the measure. The language of the argument is subject to approval by the full Council and will be presented to the Council on March 14th. On February 14th, the Council also authorized the ad hoc committee to prepare and submit, without need for further Council approval, a rebuttal argument, if needed.

FISCAL IMPACT

Currently, all costs listed above that the City will incur in connection with adopting, implementing and enforcing regulations for the cannabis industry in Santa Rosa, will be funded by the General Fund. As stated above, staff estimates these costs to be at least \$1,000,000 annually. Should the proposed ballot be submitted to the voters and approved, the City Council would have authority to shift those costs to the cannabis businesses operating in the City.

An analysis of the 23 cannabis businesses currently permitted or in the process of being permitted as February 10, 2017, confirmed that the initial tax rates proposed are anticipated to cover cost impacts described above. The City will not see all the revenue in the first year as most of the businesses are in the start-up phase or still going through the planning approval and building permit approval processes.

According to the County of Sonoma, based on the 89,728 currently registered voters in Santa Rosa, placing the proposed ballot measure on the ballot will cost the City approximately \$400,000, or \$4.50 per registered voter. By having two local measures on the ballot, many of the costs incurred in holding the election, including mailing, could be shared between the measures and thus reduce the cost of holding two separate elections. To ensure this cost savings, it is recommended that both measures being evaluated by the City are on the same ballot on June 6, 2017.

ENVIRONMENTAL IMPACT

This action is exempt from the California Environmental Quality Act (CEQA) because it is not a project which has a potential for resulting in either a direct physical change in

ADOPTION OF AUTHORIZATION TO IMPOSE CANNABIS TAXATION
PAGE 7 OF 7

the environment, or a reasonably foreseeable indirect physical change in the environment, pursuant to CEQA Guideline section 15378.

BOARD/COMMISSION/COMMITTEE REVIEW AND RECOMMENDATIONS

The Medical Cannabis Policy Subcommittee has held fifteen public meetings over the last year to provide input regarding shifting regulations, statewide legalization, drafting ordinances, interim policies and taxation approaches and rates. It is the Subcommittee's recommendation that the Council submit the proposed ballot measure to the voters to authorize the Council to implement a business tax on the cannabis industry and, by resolution, set initial tax rates that will go into effect if the ballot measure passes.

NOTIFICATION

To notify and obtain input on the proposed cannabis business tax, the City has placed consideration of the proposed tax on the agendas of several Cannabis Policy Subcommittee meetings which were noticed in accordance with the Brown Act and open to the public, and the City has participated in two town hall meetings with the County of Sonoma. In addition, an online poll was created in conjunction with the County to receive direct feedback on the tax proposals.

ATTACHMENTS

- Ordinance
- Resolution Declaring Fiscal Emergency
- Resolution Calling for Election and Related Items

CONTACT

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