



September 12, 2017

Re: **CAO Recommendations Re: Cannabis Business Fees and Interim Position Authority to Implement Cannabis Regulations; Council File No. 14-0366-S5**

Honorable Council President Wesson & City Council:

The voters of California and our City, through Proposition 64 and Measure M, demonstrated that now is time to end the criminalization of cannabis, which has negatively impacted disadvantaged communities and cannabis workers for decades. Los Angeles will serve as an example for the region and the country as it endeavors to legalize adult-use cannabis. We will play a crucial role in professionalizing an industry that has been operating in the shadow of the law, and in decreasing the stigma associated with medicinal-use of cannabis.

Most importantly, the legalization of cannabis will allow the City to end the devastation that the War on Drugs has had on many of our communities, and through the social equity program, the City will have the opportunity to give back to those same communities, and support them through business ownership and job creation.

To effectuate that goal, on August 3, 2017, Council President Wesson issued a letter to the Planning Department requesting that it revise the initial draft planning ordinance to replace limited immunity with full licensing, as well as include Type 7 manufacturing and outdoor/mixed-light cultivation, mirroring those licenses issued by the state. The Planning Department responded on September 6th by issuing a staff recommendation and draft land use ordinance that incorporated most of these requests. We applaud Council President Wesson, and the Department of City Planning, for recognizing that only with full licensing and legalization can the City end the over-policing of low-income communities and cannabis workers, and create a robust local cannabis industry for the world to see.

To further decrease the disparate impact of law enforcement in low-income communities, on August 18, 2017, the Council passed a Resolution requesting that the City support and sponsor legislation to amend California Health & Safety Code §11357(a)(2) in order to address the potential impact of increased policing on those between the ages of 18-21 found to be in possession of impermissible quantities of cannabis.

The undersigned groups would like to thank the City Council for its continued efforts to legalize, destigmatize, and professionalize the cannabis industry, its patients, and its workers. We would also like to ask that the City give direction to the City Administrative Officer (“CAO”) to study and report on the interim position authority for City departments under a full-licensing framework.

On August 14, 2017, the CAO issued its Recommendations on Cannabis Business Fees and Interim Position Authority to Implement Cannabis Regulations Within the City (CAO File No. 0220-05294-001) (“Report”). The Report recommends that the City fund 66 Police Department positions, 13 Fire Department positions, six City Attorney positions, four Office of Finance positions, and one Information Technology Agency position, none of which are proposed to be filled in the Cannabis Department.

In order for the Cannabis Department to thrive, it must be equipped with adequate staff, resources, and funding. Yet, the bulk of the resources have been allocated to the Police Department. We believe that the City is committed to both social equity and to minimizing the impact of policing on 18 to 21 year olds. It is most likely that this report is a reflection of an earlier analysis completed with a limited immunity framework in mind. The current staffing proposals are counter to a licensing scheme and to the principles underlying the City’s commitment to social equity, and should be changed accordingly.

The City must allocate most of the available resources to the Cannabis Department so that it may efficiently and competently undertake the enormous task of getting a new Department and Commercial Cannabis Program off of the ground. Perhaps, this allocation can be changed over time, but at least during the first three years, the Department should house the majority of the City’s dedicated resources whether newly created positions or borrowed from existing Departments.

To be consistent with the comments herein, the “Draft Application and Licensing Process,” as exemplified by the flow chart contained in the CAO Report, will need to be modified to reflect a more streamlined and efficient procedure. The undersigned organizations will reserve comment on these procedural matters until the City has proposed a Commercial Cannabis Ordinance.

Moreover, the CAO Report does not allocate resources to the Bureau of Contract Administration (“BCA”). The BCA is responsible for enforcing labor standards. The City should follow the model put forth in Proposition 64, which expressly allocated funding to labor standards enforcement agencies.

We also ask that the City provide a more detailed analysis of its breakdown for the cannabis licensing fees provided in the CAO Report. The current price tag for a cannabis licensee is nearly \$70,000 and legally must be commensurate with the cost of

administration. This is cost prohibitive for small businesses and social equity applicants, and tips the scale in favor of large corporate enterprises.

The City has made significant strides towards creating a robust and equitable commercial cannabis program, and has diligently responded to the input of public. We continue to look forward to participating in the City's public process, working with the cannabis commission on enforcement, and offer our support to the City in these efforts.

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Advancing Legal Medical Marijuana Therapeutics and Research

September 12, 2017

Mr. Richard H. Llewellyn, Jr.
Interim City Administrative Officer
Los Angeles City Hall
200 N. Spring Street
Los Angeles, CA 90012

Re: August 14, 2017 Report on Cannabis Business Fees and Interim Position Authority to Implement Cannabis Regulations CAO File No. 0220-05294-0001 Council File No. 14-0366-S5

Dear Mr. Llewellyn:

We are in receipt of your August 14th report and below list our concerns.

American for Safe Access (ASA) has been involved in Los Angeles City (the City) efforts to regulate cannabis since 2007, when our California Director worked with Councilman Zine's office to bring forward the City's first registry for cannabis dispensaries.

I suggested to the City that they form a working group during that period, and was proud to be the founding member of that group. Today I serve on the City's current group.

Over a ten year period, we contributed materially to each new ordinance draft.

When the City was twice threatened by inappropriate cannabis voter initiatives we worked closely with the entities who sought to defend the City's interests. Today, we stand in proud partnership with the Southern California Coalition, the only cannabis trade association to make minority equity a part of its platform.

Over the years, ASA has helped thousands of municipalities regulate and our organization is hopeful that the suggestions below will be helpful in moving the City towards policies which are both fair and inclusive. Most everyone involved in the City's cannabis industry is a medical cannabis patient and thus we feel that the City must be particularly careful not to harm this vulnerable population.

This harm can manifest in various ways but they all have the same result: patient access to medical cannabis is negatively affected or ceases altogether. Since patient access to medical cannabis was the reason the City chose to allow dispensaries within its borders ten years ago, we are deeply concerned that the City's core goal of access by patients to medical cannabis, will be undermined by policies or protocols which create artificial bars to access.

Our concerns are as follows:

- **Problem: Expensive, automatic audits are proposed even when there is no evidence of financial malfeasance.**

See: Page 1 paragraph 1 & Page 5 paragraph 4

Discussion:

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The issuance of Business Tax Registration Certificates (BTRCs) is a matter of public record and is currently being tracked on the City's website. See: <https://controllerdata.lacity.org/Revenue/191-Prop-D-Compliant-Medical-Marijuana-Businesses/vva2-przx/data>. As this is the case, any Department of Finance employee could look up the current status of existing businesses, a formal audit should not be required. Older payments would be noticed in each applicant's existing file. The City **has already had to verify cannabis business tax payments** to decide whether or not to issue Business Tax Registration Certificates (BTRCs) to those claiming to be eligible for limited immunity. Thus, if the City issued a BTRC to a business in the previous year all back taxes due would have already been verified as paid, no audit would be required.

Businesses that are involved in payment plans or have other issues are already clearly delineated and their status is carefully tracked by the Department of Finance. Given the above, it would seem like overkill to create and fund four new auditor positions which would merely recreate work already done by existing employees. Or engage in audits when no evidence of malfeasance was manifest.

New businesses pay estimated taxes for the current year. They are not paying on the previous year's income. Thus, any auditing that was done would have to take place AFTER at least one year of sales. The City would simply be conducting an audit based purely on estimates rather than actual sales if it tried to audit prior to a history of sales commencing.

Because of existing state regulations for seed-to-sale tracking and other inventory controls that are part of state regulations, the ability of a cannabis business to underpay will be non-existent and eliminates the need for on-going audits of existing businesses. Instead, the Department of Finance should audit when anomalies arise, saving the City and patient providers time, money and wasted effort.

The persistent assertion that marijuana businesses are largely cash businesses in Los Angeles and thus need continual auditing is an urban myth. Finance Department Assistant Director, Todd Bouey, testifying before a government hearing convened by California Treasurer John Chiang, stated that only 20% of the cannabis taxes remitted to the City were cash payments. Thus, if the justification for continual audits rest on cash payments the City needs to revise down its need for auditors.

Because a key element of effective audits is surprise, mandating on-going audits just gives bad actors a heads-up on what to expect. No other taxing entity announces in advance who they will be auditing and when they will do so.

It's important to remember that the City still has a number of unauthorized entities which have saturated the market and suppressed the sales in Prop D eligible shops. What appears to be a situation of under-reporting may be a dip in sales attributable to the fact that unauthorized entities cannot, per a City resolution, pay City taxes.

In such a situation, the unauthorized entities (who may not be carrying insurance or running a payroll) are able to offer cannabis goods much cheaper than those shops eligible for limited immunity which do pay taxes. This materially suppresses taxable revenue from legitimate sources and in many cases has brought legitimate operators to the brink of bankruptcy.

Thus, if the Department of Financing begins auditing before the City Attorney's Office has completed enforcement actions against unauthorized entities, market factors, rather than under-reporting would account for the drop in tax revenues. Unauthorized actors tend to re-open in new locations once they are closed by the City so you see a domino effect where tax revenues fall as the result of unauthorized entities serially opening in close proximity to a previously healthy city-sanctioned businesses.

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The Department of Finance is targeting one particular industry and it appears they are doing so under the assumption that cannabis businesses are so morally bankrupt that they require constant monitoring. This is not only inappropriate, it's deeply insulting.

Rather than perpetually auditing patient providers, enacting a tax amnesty program would allow those who wished to honorably repair their tax history to do so without affecting their ability to achieve licensure. By allowing entities to voluntarily come forward, the City potentially saves millions in auditing expenses.

Given all of the above, mandating on-going audits for all cannabis businesses would appear to be expensive and unnecessary. It punishes businesses which have never underpaid as they will have to pay for these audits and submit to surrendering extensive records for no reason. Such audits might result in good actors being accused of under-reporting when the loss of tax revenue was really due to unfair competition.

Solution:

The City should not audit absent evidence of malfeasance. Until such time as the City Attorney's Office has completed its shutdown of unauthorized actors, the City should allow those subject to audits to provide proof of unauthorized activity in close proximity to their business. Rather than imposing serial audits, the proposed budget should be used to hire and train staff who would work with cannabis stakeholders to remedy current complaints about Department of Finance policies, behavior and inadequate personnel. To collect taxes from those who wished to come forward and repair their tax history, an amnesty program should be established.

- **Problem: The City proposes to burden the City Attorney's office with administrative duties more appropriately handled by the Cannabis Division.**

Page 2 Item No. 3, first paragraph

Discussion:

The City Attorney's Office is already saddled with closing down hundreds of unauthorized cannabis businesses across the City. Additionally, the passage of Prop 64 has reduced most cannabis crimes to misdemeanors, all of which are the prosecutorial responsibility of the City Attorney. To have the City Attorney's office responsible for prosecuting cannabis businesses while simultaneously participating in "the administration of the application, licensing, renewal and revocation processes" creates a situation where a city agency primarily charged with enforcement is now given broad powers over who receives or maintains a license.

The City cannot truly have a thriving cannabis industry until unauthorized actors have left the marketplace. The City Attorney's Office has been instrumental in closing over 800 unauthorized entities, using a unique formula and a dedicated staff. To saddle this venerable organization with administration of thousands of cannabis applications when the City has created a cannabis division and hired an executive director for that division seems to be a needless burden. We rely on our City Attorney to prosecute crimes, not babysit business applications.

Solution: Remove responsibility for administration and coordination of licensing activities from the City Attorney's Office and center those responsibilities in the new Cannabis Division. Apportion budget monies between the two entities so that the City Attorney's Office can write ordinances and formulate regulations in tandem with the Cannabis Division, but will not otherwise be burdened with administrative duties.

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- **Problem: The City proposes to hire 66 narcotics officers to perform duties better handled by city employees unaffiliated with law enforcement and trained to promote public safety rather than investigate crimes.**

Page 2 Item No. 4

Discussion:

Currently, the Los Angeles Police Department handles all LiveScans required by Proposition D. This is appropriate because verifying criminal records is traditionally a law enforcement activity. It is anticipated that the number of LiveScans to be processed will increase dramatically once licensing begins, thus an increase in staff is warranted.

Reviewing Security Plans is another area where law enforcement oversight is appropriate and new staff may need to be hired.

A limited immunity construct requires that each suspected violator be investigated for land use violations or as a public nuisance and prosecuted in court. Traditionally such investigations would be conducted by law enforcement.

The City now intends to move towards more traditional licensing which means that anomalies which do not rise to the level where they endanger the public are given an opportunity to cure. This kind of resolution is better handled by civilian inspectors and compliance officers who specialize in public safety issues. The hiring of 66 narcotics officers to perform activities which are ministerial in nature and do not involve the investigation or deterrence of crimes is an expensive and unnecessary endeavor.

Paying law enforcement to conduct activities which are traditionally done by city or county employees sends the message that cannabis businesses are so dangerous only narcotic officers could interact with such businesses. In point of fact, non-retail cannabis businesses are quiet and largely unknown to the public. Retail outlets currently sanctioned by the City are clean well-run facilities which do not require police oversight. City employees can be easily trained to conduct inspections and determine compliance in all areas of cannabis activity.

Having such compliance officers attached to the Cannabis Division rather than the police department would not only be reassuring to licensees; it puts enforcement where it should be: in the hands of trained experts whose goal is public safety and the resolution of problems, not the investigation of crimes.

It is also more cost effective as the proposed budget indicates that 24 of the 36 hires are not officers, but lieutenants, detectives and a sergeant.

Solution: Revise the budget so that law enforcement is covered for the processing of LiveScans and the vetting of security plans. Otherwise assign budget monies and manpower to the Cannabis Division so that inspections and compliance matters are conducted by City employees supervised by the Cannabis Division rather than the narcotics division of the LAPD.

- **Problem: Proposed license fees are not adjusted for smaller businesses; instead a "one size fits all" approach forces smaller businesses to underwrite the expense of licensing larger endeavors.**

Page 3 Item No. 6

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Discussion:

The combined fee total for a first-time license is \$47,067. 00. A small business which does not take much time to vet will be charged the same amount as a large business which eats up a great amount of inspection and compliance review time. This means that a small business will be partially underwriting the expense for vetting large, complex businesses.

Indeed, you could argue that the expense entailed in licensing a small business would be such that it would force a small operator out of business. The profit margin once you subtracted the costs of licensing each year at the state and local level would be too slim to be supportable.

Additionally, businesses are subject to fees, whether or not they are warranted. For instance, a business which has always been current on its tax payments should not be subject to a tax audit fee to determine if it is current on its tax payments. If it was issued a BTRC in the previous year the business wouldn't require an audit because a BTRC is only issued when you have paid all back taxes as well as what's currently due.

Part of the reason for such extreme fees is that the City proposes to hire narcotics officers, detectives, lieutenants and sergeants to perform tasks which could be done by trained city employees at a much lesser cost.

Rather than staff the Cannabis Division and adequately fund it, various pieces of the work that are traditionally done by such a division are being jobbed out to various city departments and agencies, whether or not this is the most cost effective approach for issuing licenses. It is not the job of a licensee to provide budget and personnel expansion opportunities for City Departments.

Allowing a multi-agency approach to licensing means one department can materially delay or stop licensing. Some City departments are less burdened than others, for reasons that have nothing to do with department efficiency. This means a serious risk of unseemly delays because of bottlenecks.

Solution:

Create a scaled fee schedule so that small businesses are charges fees commiserate with their size. Impose hourly inspection rates so that large entities pay their fair share. Whenever possible, have city employees perform inspections and compliance duties so that police officers are not drawn away from more important work. Locate all inspection and compliance workers in the cannabis division.

Problem: Imposing a 7% Surcharge System Development Fee on all licensing fees is actually a tax not a surcharge and so increases the fees for licensing as to be unsupportable.

Page 3 Item No. 7

Discussion:

The City will collect a 5% tax on all medical cannabis sales and a 10% tax on all recreational sales. It's important to remember that businesses collect tax revenue but it is patients and consumers who actually pay these taxes. The tax is passed on to consumers and patients through increased cost of goods or directly as a taxation charge.

Right now so many state and local taxes are being imposed on consumers and patients in Los Angeles that there is a serious risk that patients will be driven back to the black market or choose to patronize nearby cities which do not impose such a high combined tax rate. The two graphs below illustrate the taxes patients would pay in Los Angeles and the City of West Hollywood beginning in January of 2018.

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Taxes and Fees in Los Angeles:

City Tax	5%
Sales Tax	9.2%
Excise Tax ¹	15%
Surcharge Tax	7%

Combined Tax: 36.2%

Tax if the Patient has a County ID Card: 21.2%

Taxes and Fees in West Hollywood:

City Tax	0%
Sales Tax	9.2%
Excise Tax	15%
Surcharge Tax	0%

Combined Tax: 24%

Tax if the Patient has a County ID Card: 9.2%

The proposed surcharge is a percentage. It is thus more akin to a tax than a surcharge and should not be characterized as a surcharge.

If the surcharge attaches to all licensing fees, the price for one license increases to \$50,361.69.

The City stands to reap millions in tax revenue, but only if it is reasonable about taxes and fees. Recouping things like inspection fees is routine in most any municipality. Passing on all costs involved in creating an infrastructure to receive cannabis tax monies or engaging in expensive and overbroad inspection and vetting processes is not (i.e. the City proposes to greatly increase costs by hiring 66 narcotics officers rather than using city employees for inspections and vetting).

There is a point where the City needs to absorb some of the costs of licensing and regulation, particularly when infrastructure like computer programs and platforms are utilized by multiple city agencies and are required to interface with the State.

If the City chooses to set licensing and tax expenses too high, patients and consumers who have to absorb these expenses (either directly or through increased cost of goods) will abandon the Los Angeles market for nearby locales where prices are more reasonable. The cannabis industry in Los Angeles will wither and die.

Solution: Remove the 7% surcharge.

- **Problem: The City Seeks to put inspections of cannabis businesses in the hands of narcotics officers based in the Los Angeles Police Department. This is extremely expensive and has not worked well in the past.**

Page 7 Paragraphs 1-4

Cannabis businesses seeking licensure in the City of Los Angeles are required to provide extensive information on where their funding comes from. The identification of unclean money would thus be more appropriately handled by accountants, not the police department which would have to specially train officers to review this information and who would otherwise not have the accounting skills to identify whether funding from a business could be traced back to illegal activity.

Additionally, as cannabis businesses do not receive loans from banks or other conventional funding sources, each private funding source would have to be extensively vetted, not something the police are not trained to do. Quite often funding comes from legal cannabis activity in other states which means the officer reviewing the application would have to have an extensive knowledge of laws in other states as well as the funder's economic and licensing history in that state.

¹ Patients who obtain a Medical Marijuana I.D. Card from their county health department are excused from the excise tax

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By law, police officers cannot own cannabis businesses. Thus, they have no idea what constitutes a compliant cannabis business as they have never operated one. They also tend to make assumptions which characterize benign behavior as evidence of a crime. For instance, one rationale for raiding cannabis businesses oft stated by narcotics officers in the past was that non-profit corporations could not make a profit or they were operating illegally. Interestingly enough narcotics officers never got around to raiding Goodwill, despite the fact it was a non-profit entity generating profits.

Pre-inspections of cannabis businesses should be conducted by city employees specially trained on cannabis issues and sensitive to the needs of medical cannabis patients. Patients should not be put in fear by the sudden appearance of an armed narcotics officer conducting inspections while the patient is legally acquiring his or her medicine.

It would be extremely expensive to hire 66 narcotics officers, many at high pay grades, than train them to perform tasks usually performed by city and county employees. Placing narcotics officers in this role means that the City has made the decision to treat all cannabis businesses as potential criminals, rather than as economic partners.

Compliant retail cannabis businesses are akin to nutritional centers or health food stores. They do not require continual oversight or vetting by narcotics officers. Non-retail businesses are even more discreet and would be better served by inspections conducted by public safety officers rather than narcotics detectives.

This is of particular concern for minority equity applicants who would now find themselves in the position of relying on those who injured them in the past to approve their licensure. It would be more equitable to place these decisions in the hands of neutral city employees who are part of the cannabis division and who are specially trained to resolve problems rather than investigate crimes.

Solution: Relieve narcotics officers from the responsibilities of vetting applications or conducting general inspections but allow the LAPD to continue managing LiveScans and reviewing security plans. Standard training of cannabis retailers should be conducted by city employees trained by those who have operated cannabis businesses. All inspections and vetting should be based in the Cannabis Department, not the narcotics division of the LAPD.

Problem: The draft application and licensing process does not allow for full licensing prior to state licensing and by doing so doubles fees and creates problems for those eligible for licensing and priority licensing, particularly veterans.

Page 7, Draft Application and Licensing Process Graph

Discussion:

As outlined in graph, the City would require applicants to complete most application requirements and if successful, would be issued a "local authorization" rather than a license or provisional license.

The applicant is then required to obtain a state license, come back to the City and qualify again for a full license and a BTRC by obtaining various department clearances, having plans approved and re-submitting to inspections which would most likely be required to obtain a local authorization in the first place.

This method of achieving full licensure is expensive and time consuming. In a worst case scenario it could easily double the cost of a local license, and drastically increase consultancy fees.

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Qualifying twice for licensure could produce an inequitable result when an applicant qualifying for a state license is subsequently unable to obtain full licensure at the local level and then must close.

Additionally, since it appears that state licensing may be delayed, and only provisional state licenses will be available, an applicant could obtain a local authorization, qualify for a provisional state license but then be unable to complete licensing at the local level because the City required a regular state license rather than a provisional one, prior to finalizing local licensure.

The state has decided that veterans will be eligible for state priority licensing across all categories. In order to qualify they must have a local license, permit or authorization. The state may be unwilling to recognize licensure if local licensing process is bifurcated. Those eligible for priority licensing and indeed all other eligible applicants should be able to obtain local provisional licenses strong enough to satisfy regulators at the state level.

The most efficient way to do this is to review City history and follow what's worked in the past. In 2007 the City established a registry. Applicants who intended to apply for licensure proved to the City's satisfaction that they had paid taxes, were carrying adequate insurance and operating within the City limits. Once they had done so, presence on the registry provided law enforcement and the City with a list of those who were operating in good faith and intended to seek licensure. As there was no state licensing requirements at that time, the fact registry applicants had to wait from 2007 to Prop D in 2013 to acquire limited immunity did not retard their ability to operate in the meantime.

The City can easily craft an application that allows applicants to:

1. Prove they carry adequate insurance, (i.e. liability, workmen's comp insurance).
2. Show that they have at BTRC or will acquire one as soon as the City allows it.
3. Provide a professional map demonstrating that the business location is compliant.
4. Provide a letter from the lessor demonstrating knowledge of the type of business.
5. Undergo a fire inspection either by the Los Angeles Fire Department or an entity designated by the City to engage in fire inspections and, if carrying food items, undergo an inspection by the health department.

Once these conditions are satisfied, the City would issue a provisional license strong enough to qualify for state licensure, which would be renewed each year until such time as the state began engaging in full licensure. Once the state began issuing full licenses, when city provisional license came up for yearly review, the applicant would be required to prove they had initiated the state licensing process or their provisional license would not be renewed.

By following this system, you get rid of the clumsy, expensive bifurcation and substitute in a streamlined application process that matches what the State is doing. Further, it's a mechanism that encourages good behavior (i.e. applicants expecting to be vetted by neighborhood councils during the full application process are likely to be good neighbors during provisional licensing).

Provisional licensing ensures that basic health and safety concerns have been resolved, that the business is in a compliant spot, carrying insurance and paying taxes. There is little that can go awry between provisional licensing and full licensure, as the provisional license period should only last as long as it takes the state to issue full licenses, two years at most.

And, historically, this system has worked. Those who appeared on the 2007 City registry and are still operating today, were so well behaved over a ten year period, that the City has allowed them favored status in every ordinance it has produced. What worked in the past will work now.

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Solution: Replace a bifurcated system of licensure with the streamlined provisional application process as described above, and require full licensing at the same time the State of California does.

Thank you for the opportunity to present commentary. If you have any questions or concerns, I can be reached at (805) 279-8229 or industry@safeaccessnow.org.

Founded in 2002, Americans for Safe Access (ASA) is the largest national member-based organization of patients, medical professionals, scientists, and concerned citizens promoting safe and legal access to marijuana for therapeutic use and research. ASA works in partnership with state, local and national legislators to overcome barriers and create policies that improve access to marijuana for patients and researchers. ASA has more than 100,000 active members with chapters and affiliates in all 50 states. Our website is: www.safeaccessnow.org

Sincerely,



Sarah Armstrong JD
Director of Industry Affairs
Americans for Safe Access

Cc: The Honorable Members of the Los Angeles City Council
Council Staff Assigned to the Cannabis Issue
Ms. Cat Packer
The Honorable Michael Feuer
Ms. Leela Kapur, Esq.
Mr. Alex Ponder
Mr. Don Duncan

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