


CITY OF LOS ANGELES
INTER-DEPARTMENTAL CORRESPONDENCE

Date: August 18, 2016

To: Honorable Members of the Rules, Elections, Intergovernmental Relations,
and Neighborhoods Committee

From:  Miguel A. Santana
City Administrative Officer

 Sharon M. Tso
Chief Legislative Analyst

Subject: **PROPOSITION D – MEDICAL MARIJUANA DISPENSARIES – ADULT USE
OF MARIJUANA ACT (C.F. 14-0366-S5)**

SUMMARY

Pursuant to Motion (Wesson/Koretz/Martinez/Price-Huizar/Bonin/O'Farrell) introduced on May 18, 2016 (C.F. 14-0366-S5), your Committee instructed the City Administrative Officer (CAO) and the Chief Legislative Analyst (CLA) to report with options that will allow Proposition (Prop) D compliant dispensaries to conform to the newly created medical marijuana state licensing system, increase penalties and enforcement to close down all illegal marijuana-related businesses, create a regulatory framework for the City of Los Angeles (City) to implement the Adult Use of Marijuana Act (AUMA), if approved in November 2016 through Prop 64, and extend Prop D's gross receipts tax to all marijuana-related businesses.

The City's regulation of marijuana spans across many policy and program areas. As such, this report includes the input of the Office of the City Attorney (City Attorney), Department of City Planning (DCP), Department of Building and Safety (DBS), Office of Finance (Finance), and Police Department (LAPD). The City could adopt ordinances to enact a comprehensive regulatory framework which could cover the entire supply chain for medical and recreational marijuana businesses – from the cultivation, production, and processing of marijuana plants/products to point-of-sale distribution and marketing. Any imposition of new taxes or an increase in existing taxes will require a ballot measure. Since Prop D was a Council sponsored measure, it can be amended or repealed without voter approval (Charter Section 464). Policy goals of the Council will direct the organization of the regulatory framework, including subject matters such as taxation and finance; public health and safety; and governance and administration of regulations and the enforcement thereof.

This report presents options for Council's consideration on issues of: Prop D compliance with the new State law; penalties and enforcement needed to close down illegal marijuana-related businesses; a regulatory framework to implement AUMA if approved in November; and extension of Prop D's gross receipts tax to all marijuana-related businesses. For each subject area, the report provides a discussion of the issue and proposes options for further consideration. This report is not a final, comprehensive list of options, and is intended to serve as a guide to further policy discussions for all stakeholders.

BACKGROUND

On November 5, 1996, California became the first state to establish a medical marijuana program, enacted by Prop 215 and further refined by Senate Bill (SB) 420 in 2003. Prop 215, or the Compassionate Use Act, was approved by initiative with a 55% majority, allowing people with cancer, AIDS and other chronic illnesses the right to grow or obtain marijuana for medical purposes when recommended by a doctor. SB 420, or the Medical Marijuana Protection Act, established an identification card system for medical marijuana patients. Presently, medical marijuana users with a valid doctor's recommendation may grow and possess marijuana provided that it is strictly for personal use.

In May 2013, the City enacted Prop D which has been the primary tool utilized by the City, particularly the City Attorney, to provide the necessary enforcement and regulatory framework for medical marijuana dispensaries (MMDs) in the absence of state regulation. Prop D garnered wide support, thereby enacting a general ban on medical marijuana businesses, while also granting immunity from the ban to those dispensaries that: 1) have operated since September 2007; 2) previously registered in accordance with three of the City's earlier medical marijuana registration laws; and, 3) complied with specified operational requirements. While Prop D has been effective in providing enforcement and shuttering hundreds of illegal dispensaries, there are still illegal MMDs operating in the City.

In 2015, the State legislature enacted the Medical Marijuana Regulation and Safety Act (MMRSA), which establishes comprehensive regulation of medical marijuana including a licensing system and prohibition of commercial marijuana activity without possessing a State license and a local permit, license, or other authorization. MMRSA recognizes a range of medical marijuana businesses including cultivation, marijuana product manufacturers, marijuana distributors and transporters, marijuana testing laboratories, and dispensaries, and provides immunity to marijuana businesses operating with both a state license and a local permit. Under MMRSA, all medical marijuana businesses (MMBs), or persons engaged in commercial marijuana activities, must have both a state license and local permit in order to operate lawfully within California. A person cannot commence any commercial marijuana activity under a state license until the applicant has obtained a local permit, license or other authorization. However under Prop D, the City does not issue a license or permit to MMDs. Thus, when the state starts licensing medical marijuana businesses on or after January 1, 2018, the Prop D-compliant dispensaries in the City will be illegal under MMRSA. In order to ensure Prop D compliant MMDs and potential MMBs conform to state law, the City needs to update its own medical marijuana regulatory framework. On July 8, 2016, the City Attorney transmitted a confidential report (C.F. 14-0366-S4) regarding already enacted, as well as, proposed state legislation regarding medical marijuana.

The new dual licensing framework represents a much more objective standard than the existing immunity for collective and cooperative cultivation under Health and Safety Code Section 11362.775 and should make it easier for the City to determine which MMBs are operating lawfully. Rather than having to determine whether an establishment is a bona fide collective or cooperative, which can be difficult to do when dealing with all-cash businesses that often do not maintain accurate records, the City will only need to confirm that the establishment has a state license and local permit.

MEDICAL MARIJUANA REGULATION AND SAFETY ACT

The Bureau of Medical Marijuana Regulation, within the Department of Consumer Affairs, was created to administer and enforce MMRSA. MMRSA divides state licensing and enforcement responsibilities among three agencies:

- The Department of Food and Agriculture will issue medical marijuana cultivation licenses.
- The Department of Consumer Affairs will issue licenses for medical marijuana dispensaries, distributors, and transporters.
- The Department of Public Health will issue licenses for medical marijuana manufacturers and testing laboratories.

State licenses will be valid for one year and a separate state license is required for each commercial marijuana business location. Each of the state licensing authorities is responsible for creating regulations governing their respective areas of responsibility. Once MMRSA's regulatory framework is in operation, which the State anticipates will be in January 2018, the medical marijuana industry will operate as follows:

- Medical marijuana cultivators and manufacturers produce medical marijuana products in accordance with state and local regulations.
- Medical marijuana cultivators and manufacturers deliver their products to a medical marijuana distributor.
- The distributor confirms the identity and quality of the products and sends them to a medical marijuana testing laboratory.
- The testing laboratory performs batch testing on a random sampling of the product. If the product meets the safety standards established by the state, the testing laboratory issues a certificate of analysis and returns the product to the distributor.
- The distributor performs a final quality assurance review and then transports the product to a medical marijuana dispensary.
- The dispensary distributes the medical marijuana to qualified patients and primary caregivers.

REGULATORY OPTIONS AVAILABLE TO THE CITY

The City has a wide range of land use regulatory options to address medical marijuana. The following regulatory options can be applied to Prop D MMDs and potential MMBs we may wish to authorize.

Options include:

- Express bans – MMRSA recognizes a range of new medical marijuana businesses, including cultivators, manufacturers, distributors, transporters, and testing laboratories. The City may opt to ban all or specific activities under MMRSA.
- Regulatory framework – Since MMRSA establishes a state framework for regulating all aspects of the medical marijuana industry, the City could explore the option of allowing some or all such businesses through some form of a local regulatory permit/license system.

For example, a regulatory permit system could:

- A) Require an annual renewal;
- B) Impose safety-related operating requirements;
- C) Impose operating requirements which may include:
 - a. the use of licensed security guards;
 - b. designated hours of operation;
 - c. prohibition against sales of alcohol and/or tobacco;
 - d. prohibition against on-site alcohol and/or tobacco consumption;
 - e. installation of adequate odor control devices and ventilation systems;
 - f. limitations on access to minors; and,
 - g. mandatory inspections by LAPD, DBS, and Finance.
- D) Impose locational restrictions, including zoning designation and separation requirements to avoid clustering of MMBs;
- E) Specify certain zoning designations to encourage clustering (e.g. within an industrial zone); and,
- F) Limit the number and type of MMB permits that are issued.

If the City establishes a regulatory framework for MMBs under MMRSA, the City should expect to be inundated with permit inquiries and/or applications. Additionally, unsuccessful applicants will likely look for potential ways to attack the City's selection and evaluation process. Therefore, the City should give careful consideration to how applications will be processed for MMBs. The enabling ordinances should provide clear guidelines as to what information is required in the application, what grounds constitute a basis for denial of a permit, the type of permit or license to be issued, Conditional Use Permit (CUP) or other regulatory permit, and the responsible party for making the decision on issuing the permit.

The City could utilize a number of approaches to processing applications and issuing permits, such as:

- A) Scoring System – The City could implement a subjective evaluation process to review MMB applicants. Applicants would receive a score based on a review of their applications. Those applicants who receive the highest scores would then be recommended for approval to the decision making authority. If this selection method is used, it may be preferable to use a neutral outside consultant to review the applications and make recommendations.
- B) First Come, First Serve – The City could accept and review applications in the order they are received, subject to applicable zoning requirements and separation restrictions. The reviewer will ensure that the applicant meets the applicable standards for a MMB and on that basis either grant or deny the permit.
- C) Lottery – The City should expect to receive a large number of applications and may want to consider a lottery system for issuing permits. The advantage of the lottery system is that it provides a degree of neutrality in the selection process. The disadvantage is that a lottery can deprive the City of control over who gets a permit.
- Permissive zoning – The Zoning Code is drafted in a permissive fashion such that any use not enumerated therein is presumptively prohibited. Under permissive zoning principles, the omission of any particular land use from local zoning regulations is the equivalent of an expressed ban unless the City finds that the proposed use is substantially the same in character and intensity as those land uses listed in the code. If the City can make this finding, such a use is subject to the permit process and zoning requirements which govern the land use category in which it falls. The City can rely on permissive zoning to prohibit medical marijuana uses if it so chooses. However, medical marijuana establishments may argue that they fall within various land use categories and descriptions, such as pharmacies, retail sales, nurseries, and agriculture. The City should be cautious in relying on permissive zoning to prohibit medical marijuana land use. These case-by-case requests could result in time-consuming administrative hearings and costly and uncertain litigation. If the City wishes to ban all or some medical marijuana activities, the City should consider adopting expressed prohibitions or create new zones for MMBs and MMDs.

ADULT USE OF MARIJUANA ACT (AUMA)

The potential passage of AUMA – the state-wide initiative that California voters will consider in November 2016 (Prop 64) – could present another expansive change in the regulation of marijuana. AUMA's passage would legalize recreational marijuana throughout the state and allow the City, at its sole discretion, to institute a licensing system for cultivation, manufacturing, processing, distribution, and testing of marijuana, mirroring that in MMRSA. AUMA recognizes similar categories of marijuana businesses as MMRSA and requires these businesses to obtain a state license in a manner very similar to MMRSA. AUMA does not contain a dual licensing requirement; marijuana businesses can apply for a state license

without having to show proof of compliance with local regulations. However, AUMA contains a provision preserving local control and states that nothing in AUMA shall limit or supersede the authority of local jurisdictions “to completely prohibit the establishment or operation of one or more types of businesses licensed under” AUMA. With regard to personal cultivation, AUMA provides that local agencies can completely prohibit outdoor cannabis plants at private residences and can reasonably regulate indoor cannabis plants at private residences. Such an expansion of the marijuana market calls for the City to be duly equipped to regulate it through ordinance and/or ballot initiative.

MATTERS REQUIRING A BALLOT INITIATIVE

Any imposition of new taxes or an increase in existing taxes will require a ballot measure. Prop D increased the City’s gross receipts tax on medical marijuana businesses from five percent (5%) to six percent (6%). If the City wishes to address the gross receipts taxes for marijuana businesses covered under MMRSA and AUMA, the City could draft a ballot measure that would:

- expand the existing tax to cover all marijuana businesses;
- propose a new tax on marijuana businesses not covered under Prop D;
- propose a series of new taxes for different types of marijuana businesses; or,
- propose an increase to the existing tax and expands the tax to cover all marijuana businesses.

Attachment 2 provides a summary of the marijuana taxes adopted in other California cities.

It is important to note that the state election will be held on November 8, 2016 and the Council would need to act on requesting the City Attorney to prepare a ballot measure for the March 2017 election before knowing the results of Prop 64. The table below outlines the important dates associated with the March 2017 election cycle.

| <u>Election Date</u> | <u>Last Day for Committee Action</u> | <u>Last Day to Request City Attorney to Prepare Election Resolution(s)</u> | <u>Last Day for Council to Adopt Election Resolution(s)</u> |
|-------------------------------|--|--|---|
| A. March 7, 2017 (Primary) | October 21, 2016* | November 2, 2016*** | November 9, 2016 |
| B. May 16, 2017 (General) | December 9, 2016** | January 11, 2017*** | January 25, 2017 |

* Last Regular scheduled Rules Committee meeting by which the Committee should act.

** Date shown is a Special meeting, due to Council recess in December 2016.

*** This is the legal deadline. For purposes of practicality, Council may wish to make this request at an earlier date to allow sufficient time for preparation of the Election Resolution(s).

POLICY DISCUSSION
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A. FUNDAMENTAL QUESTIONS

As discussed earlier in this report, MMRSA requires all medical marijuana businesses (MMB), or persons engaging in commercial marijuana activities, to obtain both a state license and local permit in order to operate lawfully within California. However under Prop D, the City does not issue a permit or license to medical marijuana dispensaries (MMD). If the City wishes to allow MMDs granted limited immunity from enforcement under Prop D to apply for a state license, the City should establish a regulatory framework. In establishing a regulatory framework to complement MMRSA, staff could also recommend enhancements to the framework which would complement AUMA.

Responses to these four questions will be utilized by staff to prepare the appropriate report backs to the action items presented throughout the remainder of this report.

1. Should the City allow the MMDs granted limited immunity from enforcement under Prop D to continue to operate when State Law goes into effect?

-No: MMDs granted limited immunity from enforcement under Prop D will be unable to apply for a state license. When MMRSA goes into effect, all MMDs in the City will be non-compliant with state law and potentially subject to enforcement action.

-Yes: Go to Question #2.

2. Should the City allow the MMDs granted limited immunity from enforcement under Prop D to engage in the expanded marijuana activities provided in State Law?

-No: Instruct staff to report back on options to limit MMD marijuana activities to those contained in Prop D within the City's limits.

-Yes: Go to Question #3.

3. Should the City establish precedence for these 135 MMDs for expanded activities?

-No: Instruct staff to report back on options.

-Yes: Go to Question #4.

4. If AUMA, Prop 64, passes, should the City consider establishing regulations authorizing some, or all, recreational marijuana businesses?

-No: Instruct staff to report back on options to limit or ban recreational marijuana sales, cultivation, manufacturing, or other related activities within the City's limits.

-Yes: Instruct staff to report back on options to establish regulations for AUMA.

A chart listing the methods of implementation for policy decisions can be found in Attachment 1.

Regulatory Framework

A regulatory framework which is consistent for medical and recreational marijuana creates numerous operational efficiencies for the City's permitting, inspection, enforcement, and auditing functions since the same set of rules can be applied to all marijuana businesses based on their segment within the distribution channel. This would eliminate the confusion of identifying the client base (medical or recreational) and disincentive a business from applying for a permit type that is inconsistent with their client base.

ACTION

A1. To reduce confusion, marijuana-related business (MRB) will be used in action items throughout the remainder of this report unless the action item pertains to a specific subgroup of MRB. Should MRB represent?

- 1) MMDs granted limited immunity from enforcement under Prop D;
- 2) MMDs granted limited immunity from enforcement under Prop D which may engage in the expanded marijuana activities provided in State Law;
- 3) MMDs covered by #1 or 2 and non-Prop D MMBs which may engage in the expanded marijuana activities provided in State Law (MMRSA); or,
- 5) MMDs and MMBs covered by #3 and all other MRBs which may engage in the expanded marijuana activities provided in State Law (MMRSA and, if approved, AUMA).

ACTION

A2. Should the City establish a regulatory framework that complements MMRSA?

-No: MMDs granted limited immunity from enforcement under Prop D will be unable to apply for a state license. When MMRSA goes into effect, all MMDs in the City will be non-compliant with state law and potentially subject to enforcement action.

-Yes: Establish a regulatory framework that complements MMRSA. The framework should recognize the MRBs identified in Action Item A1.

| ACTION | |
|---|--|
| <p>A3. If the City chooses to establish a regulatory framework that complements MMRSA for medical marijuana, should the City also prepare a regulatory framework that complements AUMA for recreational marijuana?</p> <p>-No: If necessary, the City will address AUMA at a later date.</p> <p>-Yes: A3a. Establish a single regulatory framework that complements MMRSA and AUMA. The framework should recognize the MRBs identified in Action Item A1.</p> <p>-Yes: A3b. Establish separate regulatory frameworks for MRBs covered by MMRSA and MRBs covered by AUMA. The framework should recognize any additional MRB activities not covered by Prop D.</p> | |

B. RETAIL SALES, CULTIVATION, MANUFACTURE, DISTRIBUTION, AND TESTING

While marijuana remains illegal at the federal level, California and a handful of other states may allow the sale of recreational marijuana following expected votes in November. Four states and the District of Columbia have already legalized recreational marijuana, and a total of 23 states have legalized medical marijuana.

A new report by ArcView Market Research (ArcView), a leading marijuana industry investment and research firm, found “legal” marijuana sales equaled \$2.7 billion in 2014 and \$5.4 billion in 2015, and are expected to reach \$6.7 billion in 2016 and \$21.8 billion by 2020. According to ArcView, recreational marijuana sales will account for more than half (53%) of the overall market by 2020. Growth in the coming years will be driven by new laws being passed by states. California’s medical marijuana sales already account for a large portion of the total industry. If California legalizes recreational marijuana this November, it will lead to a considerable increase in regulated marijuana sales.

The potential passage of the AUMA in November would legalize recreational marijuana throughout the state, and thus require the City to determine whether recreational marijuana sales, cultivation, manufacturing, or other related activities should be authorized within the City.

If the City authorizes recreational sales, cultivation, manufacturing, processing, distribution, and/or testing of marijuana, then it should consider instituting a licensing system mirroring that for MMRSA. An expansion of the existing marijuana market necessitates the City to be duly equipped to regulate new MRBs. The following policy questions should be resolved prior to staff presenting a framework to support MRBs.

ACTION

B1. If AUMA passes, should the number of all MRBs within the City be capped at 135?

-Yes: Instruct staff to report back on options to implement an effective cap including options that allot a specific number of permits/licenses to each unique activity area (e.g. MMD, MMB, recreational marijuana sales, cultivation, and manufacturing).

-No: Instruct staff to report back on one or more of the following options:

-B1a. Instruct staff to report back on options to implement an effective cap less than 135 MRBs including options that allot a specific number of MRBs to each unique activity area (e.g. recreational marijuana sales, cultivation, and manufacturing).

-B1b. Instruct staff to report back on options to implement an effective cap greater than 135 MRBs including options that allot a specific number of MRBs to each unique activity area (e.g. recreational marijuana sales, cultivation, and manufacturing).

-B1c. Instruct staff to report back on options with no cap on MRBs. Options may include caps on specific numbers of MRBs in unique activity areas (e.g. recreational marijuana sales, cultivation, and manufacturing).

ACTION

B2. If AUMA passes, should the City authorize MMDs under Prop D to participate in other MRB activities? If yes, should Prop D MMDs be subject to the same regulations/standards?

-Yes: Instruct staff to report back on options to implement the measures outlined above.

-No: Instruct staff to report back on options to limit Prop D MMDs to activities authorized under Prop D within the City's limits.

ACTION

B3. If AUMA passes, should Prop D MMBs be considered one category of marijuana businesses and all other MRBs be considered under separate categories?

-Yes: Instruct staff to report back on options to implement the measures outlined above.

-No: B3a. Instruct staff to report back on alternative options.

-No: B3b. Instruct staff to report back on options to ban recreational marijuana sales, cultivation, manufacturing, or other related activities within the City's limits.

ACTION

B4. If AUMA passes, should commercial cultivation occur within the City? If so, should commercial cultivation be limited to industrial or agricultural zones?

-Yes: Instruct staff to report back on options to implement the measures outlined above.

-No: Instruct staff to report back on options to limit or ban commercial cultivation activities within the City's limits.

ACTION

B5. If AUMA passes, should commercial manufacturing occur within the City? If so, should commercial manufacturing be limited to industrial or agricultural zones?

-Yes: Instruct staff to report back on options to implement the measures outlined above.

-No: Instruct staff to report back on options to limit or ban commercial manufacturing activities within the City's limits.

Despite Prop D limits on the number of MMDs that can operate in the City and Prop D's prohibition on delivery, there are illegal marijuana delivery services in the City. Neither the product, nor the delivery person is regulated or screened.

ACTION

B6. Should marijuana delivery be allowed and if so, under what circumstances?

-Yes: Instruct the CAO with the assistance of the City Attorney's Office to report back with recommendations.

-No: Instruct staff to report back on options to ban marijuana delivery services within the City's limits.

ACTION

B7. Should the City require the Department of Water and Power (DWP) to assess electrical systems used by MRBs and require electrical systems upgrades for operations as identified by DWP?

-Yes: Instruct staff to report back on options to implement the measures outlined above.

-No: B7a. Instruct staff to report back on alternative options to assess electrical systems used by marijuana businesses and recommend electrical systems upgrades for operations within the City's limits.

-No: B7b. The City should not require an electrical systems assessment.

Operating Conditions and Annual Inspections

The licensing and permitting processes will inform the permit types, operating conditions, and agencies that will be involved in the approval process. The City may choose to require a conditional use permit (issued by DCP) and a certificate of occupancy (issued by DBS) in addition to the business tax registration certificate (BTRC) which is issued for tax purposes.

CUPs are required for certain land uses which may need special conditions to ensure compatibility with surrounding land uses. Major issues involved with the evaluation of CUP requests include consistency with the General Plan; compatibility with surrounding land uses; conditions to ensure compatibility; land suitability and physical constraints; project design; availability of adequate access, public services, and facilities to serve the development; and potential environmental impacts and mitigation measures. The City requires these for establishments that sell alcohol (CUB) and adult entertainment (CUX). The City could adopt a similar process for marijuana businesses or create an entirely new process.

Certificates of occupancy are only issued for a new building and/or a new use or a change of use. The City could require a marijuana business to acquire a building permit which would only be approved if plans showing compliance with the terms of the Los Angeles Municipal Code (LAMC) for the new use are reviewed and approved by DBS. The site would also be inspected by DBS pursuant to the terms of the permit and the approved plans. A Certificate of Occupancy would only be issued to a marijuana business when the establishment complies with the plans and the terms of the permit and the DBS inspector approves. Currently, a marijuana dispensary is simply a retail establishment. Therefore, a dispensary going into an already approved retail store would need no approvals or inspections from DBS.

At least three City agencies have a vested interest in conducting inspections: 1) LAPD should be allowed to do up inspections of marijuana businesses in a manner similar to bars and liquor stores with a license from the California Department of Alcohol Beverage Control (ABC), 2) DBS should be allowed to verify that operating conditions are maintained after permit issuance, and 3) Finance should be allowed to audit each marijuana business. All inspections and related permit fees charged to marijuana businesses should be set at full cost recovery.

ACTION

B8. Which City Department(s) will be responsible for conducting inspections? – LAPD, DBS, Finance, or a combination of all three departments?

A. Should LAPD be allowed to do inspections of MRBs (similar to bars and liquor stores with a license from ABC)?

-Yes: Instruct staff to report back on options to implement the measures outlined above.

-No: Instruct staff to report back on alternatives.

B. Should DBS be allowed to verify that operating conditions are maintained after permit issuance?

-Yes: Instruct staff to report back on options to implement the measures outlined above.

-No: Instruct staff to report back on alternatives.

C. Should Finance audit MRBs on a regular basis?

-Yes: Instruct staff to report back on options to implement the measures outlined above.

-No: Instruct staff to report back on alternatives.

ACTION

B9. Should measures be taken to address public safety impacts?

-Yes: Instruct the CAO with the assistance of the City Attorney's Office to report back with recommendations.

-No:

C. OTHER CONSIDERATIONS

The Mayor and Council may wish to consider the following additional issues:

- Create criminal and administrative penalties, and give the regulatory authority the ability to suspend and/or revoke a business license or any other permit/authorization
- Include enforcement in the Administrative Citation Enforcement (ACE) program;
- Require annual renewals of licenses/permits, and possibly require all employees to have a permit to work in a marijuana business, similar to the City's regulation for employees involved in ammunition sales;
- Ensure that all fees include the cost allocation plan (CAP) rates for other City department employees involved in marijuana regulation;
- Set clear requirements for LiveScan results that would disqualify an individual from working/owning a marijuana business;
- High taxes and different tax frameworks for recreational marijuana and medical marijuana could encourage individuals to continue to buy marijuana on the black market;
- Registration and permitting process that clearly states which businesses are authorized and which ones are not. LAPD, DBS, DCP, and the Office of Finance currently have no way of knowing which MMBs are legal without significant research; and,
- Licenses should be tied to physical locations and not to individuals.

The Mayor and Council should also consider options for each unique MRB segment for the following issues:

- What is the license/application process?
- How long will licenses/permits be valid for?
- How often should licenses/permits be renewed?

- If a license/permit is revoked, what process, if any, should the City use to backfill the license/permit within City's framework?
- Should marijuana businesses be authorized to sell either medical marijuana, recreational marijuana, or both?
- How often should marijuana businesses be inspected?

D. ZONING AND LAND USE REQUIREMENTS

The following considerations are relevant to future discussion of land use regulations and/or policies related to the conduct of marijuana businesses within the City of Los Angeles.

Los Angeles Municipal Code

The Los Angeles Municipal Code (LAMC) is drafted in a permissive fashion such that any use not enumerated therein is presumptively prohibited. Therefore, a use that is not an enumerated use under the LAMC is expressly prohibited under the City's permissive zoning framework.

The use of any building, structure, location, premises or land for any type of marijuana business is not currently enumerated in the LAMC as a permitted use in any zone, nor is the use set forth on the Official Use List of the City as determined and maintained by the Zoning Administrator. (The adopted use list for Los Angeles is pursuant to ZA 2015-2348(ZAI), effective July 23, 2015).

LAMC Section 45.19.6.5 prohibits the Zoning Administrator from adding medical marijuana business as an authorized enumerated use or otherwise authorizing the use by variance. Current provisions of the LAMC Sec. 45.19.6 prohibit medical marijuana businesses, but grant a limited immunity from the enforcement of its prohibition to those medical marijuana businesses that do not violate the restrictions set forth in Prop D.

LAMC Section 45.19.6.5 states that the Zoning Administrator shall not have the authority to determine that the use of any building, structure, location, premises or land as a medical marijuana business may be permitted in any zone; to add MMBs or other marijuana businesses to the Official Use List of the City; or to grant any variance authorizing any medical marijuana business. Those procedures that might otherwise be available for allowing those land uses that are not listed in the zoning code, i.e., via Sec. 12.21-A or Sec. 12.27, are expressly prohibited for MMBs or other marijuana business uses under the current Code limitations.

The relevance of these Code provisions to recreational marijuana businesses would need to be assessed to determine if amendment of the Code would be necessary to accommodate such businesses. If Code amendments were necessary to enact enabling ordinances, they would need to be reviewed via the required legislative process, including public hearings and consideration by the Planning Commission and City Council.

| ACTION | |
|---|--|
| D1. Should the City add MRBs to the Official Use List of the City? -Yes: Instruct staff to report back on options to add MRBs to the Use List including whether existing zone(s) should be used or a new zone(s) should be created. -No: Instruct staff to report back on alternative options. | |

Land Use Compatibility

Specific zone limitations were not prescribed under Prop D, though the result of imposing the ordinance limitations was that MMBs appear to generally be located within the following seven zones: C2, C4, C5, CM, M1, M2, and M3. The existing ordinance was based on limiting medical marijuana businesses within proximity to defined sensitive uses and residential-zoned property (see below). Findings supporting the adoption of the ordinance included balancing uncontrolled proliferation of medical marijuana businesses, segregating incompatible uses, preventing new development from interfering with existing residents or businesses, and preserving the character of local communities. Adoption of the ordinance was also found to be in conformity with public necessity, convenience, general welfare and good zoning practice.

Every MMB is prohibited within a 1,000-foot radius of a school or within a 600-foot radius of a public park, public library, religious institution, child care facility, youth center, alcoholism, drug abuse recovery or treatment facility, or other MMB. Additionally, every MMB is prohibited that provides ingress or egress to its premises on any side of the location that (i) abuts, (ii) is across a street, alley or walk from, as measured at 90 degrees from the lot lines of the location, or (iii) has a common corner with any land zoned residential, except that an exit door required by this Code may be maintained for emergency egress only and must be locked from the exterior at all times. The above notwithstanding, this subsection shall not prohibit a medical marijuana business from locating across a street from, or having a common corner with, any land zoned residential if the medical marijuana business is separated from that residential zone by a public thoroughfare with a minimum roadway width of 80 feet.

The buffer requirements relative to distance may limit or preclude the establishment of a marijuana business within a particular community or neighborhood:

- some communities have a greater percentage of land designated and zoned for industrial or commercial use, while others may be predominantly zoned for residential use;
- a particular community or neighborhood may have a high concentration of churches, hospitals, parks, schools, or other defined sensitive use.

Issues of geographic equitability and potential overconcentration of marijuana businesses within a particular community or neighborhood should be considered when establishing limitations regarding proximity to sensitive uses and residential-zoned properties.

ACTION

D2. Should the City place proximity limits on the MRBs added to the Official Use List of the City?

-Yes: An updated GIS/land use analysis would need to be conducted to identify defined sensitive uses based on current data (last analysis based on 2007-2009 data). The percentage of land uses designated within a particular community and zoning classifications should also be analyzed based on current community plans updated since 2009. The scope of the survey would need to be determined recognizing that this would address land uses citywide.

-No: The City should no place proximity limits on MRBs.

E. REVENUE ENHANCEMENT

As previously discussed, any imposition of new taxes or an increase in existing taxes will require a ballot measure. Nationwide “legal” marijuana sales equaled \$2.7 billion in 2014, \$5.4 billion in 2015, are expected to reach \$6.7 billion in 2016, and could reach \$21.8 billion by 2020. California’s medical marijuana sales already account for a large portion of the total sales. If California legalizes recreational marijuana this November, it will lead to a huge increase in regulated marijuana sales.

Other States Imposing Marijuana Taxes

Colorado imposes a 15 percent tax on wholesale marijuana price plus 10 percent state tax on marijuana sales price. In addition to the state tax, the City of Denver imposes two tax rates: (1) a standard sales tax rate of 3.62 percent and (2) a voter approved special tax of 3.5 percent. In 2014, Denver collected \$12.65 million in new tax revenue on \$148.8 million in retail sales.

Oregon imposes a 25 percent sales tax on recreational marijuana sales. The tax will eventually be replaced with a 17 percent state tax once the Oregon Liquor Control Commission assumes control over recreational marijuana sales later this year.

Washington imposes a 37 percent excise tax on the retail marijuana sales, plus the state Business & Occupation (B&O) gross receipts tax, plus the state sales tax of 6.5 percent, plus local sales taxes. The 37 percent excise tax replaces the earlier, more complicated tax structure: a 25 percent tax on producer sales to processors, another 25 percent tax on processor sales to retailers, and a further 25 percent tax on retailer sales to customers. The effective tax rate is approximately 37 percent. This compares to a 104 percent effective tax rate on cigarettes and 11 percent effective tax rate on beer.

Key Findings from Other States

- Marijuana tax collections in Colorado and Washington exceeded initial estimates.
- Colorado, Washington, and Oregon have all modified their initial marijuana tax rates. Recent ballot initiative proposals have proposed rates between 10 and 25 percent.
- Tax rates on final retail sales have been the most effective form of taxation. Other forms of taxation, such as taxing marijuana flowers at a certain dollar amount, taxing at the wholesale level rather than the retail level, or taxing products by their level of THC, have proven difficult to implement and enforce.
- Medical marijuana is usually more loosely regulated and taxed less than recreational marijuana. In Washington, limiting non-medical sales to the retail market has been difficult given the differentials in tax rates and regulatory structure. Washington officials wished the two systems had been tackled simultaneously.
- Revenue can be in the tens or even hundreds of millions of dollars, cash management practices, storage, and general cash flow management strategies require lead time to develop and successfully implement.
- Revenues started out slowly because consumers must become familiar with the new frameworks and regulatory infrastructure.
- Significant attention must be given to local enforcement, public safety, health, zoning, local enforcement, agricultural, and criminal penalty issues. These important issues have generally been unaddressed in ballot initiatives and left for resolution in the implementation process.

Recreational Marijuana Tax Rates by State

| State | Marijuana Tax | Other Taxes |
|------------|---|--|
| Colorado | 15 percent tax on wholesale marijuana price plus 10 percent state tax on marijuana sales price. 10 percent tax drops to 8 percent effective July 2017. | State and local sales taxes; business license fees; local marijuana taxes. |
| Washington | 37 percent excise tax on marijuana sales price. Previously a 25 percent tax on producer sales to processors, another 25 percent tax on processor sales to retailers, and a further 25 percent tax on retailer sales to customers. | State Business & Occupation (B&O) taxes; state and local sales taxes. |

| | | |
|-------------------------------|--|---|
| Oregon | 25 percent excise tax on marijuana sales price. Drops to 17 percent tax when regulatory structure begins operation in late 2016. | Localities can add another 2 percent tax. |
| Alaska (not yet in effect) | \$50 per ounce on marijuana cultivator, or approximately 20 percent effective tax rate. May change before implementation in late 2016. | |
| District of Columbia | Federal law currently prohibits DC from taxing marijuana. | |

California

Many cities in California have adopted taxes on marijuana businesses. For instance, Berkeley adopted a ten percent (10%) tax on recreational marijuana in anticipation of legalization. Sacramento (4%) and Richmond (5%) adopted gross receipts taxes which cover all marijuana businesses.

If the City wishes to address the gross receipts taxes for MRBs covered under MMRSA and AUMA, the City could draft a ballot measure that would:

- expand the existing tax to cover all MRBs;
- propose a new tax on MRBs not covered under Prop D;
- propose a series of new taxes for different types of MRBs; or,
- propose an increase to the existing tax and expands the tax to cover all MRBs.

ACTION

| | |
|---|--|
| E1. Should all MRBs be taxed at the same rate? -Yes: Instruct the CAO with the assistance of the Office of Finance to report back with a recommended rate. -No: Instruct the CAO with the assistance of the Office of Finance to report back with a list of rates that could be applied to different segments. | |
|---|--|

ACTION

E2. What types of inspection and/or permit fee(s) should be charged to marijuana businesses?

A. Fixed cost (based on square footage) per type of inspection/permit?

-Yes: Instruct staff to report back on options to implement the measures outlined above.

-No: Instruct staff to report back on alternatives for other City Departments to conduct inspections.

B. Fixed cost per type of inspection/permit + Labor (\$/hour)?

-Yes: Instruct staff to report back on options to implement the measures outlined above.

-No: Instruct staff to report back on alternatives.

Penalties

Once the City has resolved the above issues, the City should review its existing penalty and fine structure to ensure that the necessary tools are available for enforcement agencies to compel compliance. Other jurisdictions have established fines and penalties between \$10,000 and \$20,000 for marijuana related violations.

ACTION

E3. What types of penalty fee(s) should be charged to MRBs?

A. Fixed cost per type of penalty?

-Yes: Instruct staff to report back on options to implement the measures outlined above.

-No: Instruct staff to report back on alternatives for other City Departments to conduct inspections.

B. Progressive Penalty (Increase in penalty fee based on number of times MRB has been fined for penalties)?

-Yes: Instruct staff to report back on options to implement the measures outlined above.

-No: Instruct staff to report back on alternatives.

F. ADMINISTRATION

Staffing and Administration

The regulation of marijuana-related businesses in the City may require new staff to oversee licensing and regulation. Business owners seeking a permit to operate in the City may have to receive sign-offs from various Departments (DCP, DBS, Finance, etc.) to ensure they are in compliance with the City's regulations. First, the City should identify which businesses, if any, will be allowed to apply and what requirements it will impose on business owners prior to issuing a permit to operate. These should include distance requirements, safety and security requirements, among others. If the Council decides to establish a regulatory framework, then the Council should consider existing City permitting processes and whether or not an existing process could be replicated or expanded to regulate marijuana-related businesses. The City could require a new Certificate of Occupancy (DBS), as well as, a Conditional Use Permit (CUP) for all marijuana-related businesses. The City currently issues permits for establishments that sell alcohol (CUB) and establishments that provide adult entertainment (CUX). If the City creates a process that clearly identifies which businesses are authorized to do business in the City, then Finance could establish a process to reject businesses who apply for a Business Tax Registration Certificate (BTRC) to conduct marijuana-related business without the appropriate authorization. Alternatively, the City could consider creating a new unit within an existing department or adopt an ordinance to create a new panel, board, or department to oversee and regulate marijuana-related businesses. The costs associated with marijuana regulation should also be calculated, in order to determine the appropriate fee for full cost-recovery. Further, licenses to operate a marijuana-related business should be annual, with renewals required to ensure that businesses are continuing to meet the City's requirements.

Conditional Use Permit

The City may choose to regulate marijuana sales through the Conditional Use Permit (CUP) process, overseen by DCP, much like the sale of alcohol for on- or off-site consumption. This process ensures community input is received and enables the City to effectively regulate certain types of land uses which may need special conditions to ensure that the use is compatible with the surrounding area. The CUP process is well-established, and has worked well for other sensitive uses, and could likely be expanded to include the regulation of MMBs. The CUP process would also enable the DBS and LAPD to more effectively enforce laws related to marijuana, as the right to inspection by LAPD and other requirements can be included in the CUP. If the City decides to not use the CUP process to regulate marijuana related businesses in the City, a new process should be created.

ACTION

F1. Should marijuana businesses be regulated through the CUP process?

-Yes: Instruct DCP to report on staffing and resources necessary to oversee all MRB permitting.

-No: Instruct staff to develop an alternative regulatory processes.

Other policy options to consider if the CUP process is not acceptable include: 1) establishing a City Board/Commission to oversee the regulation of marijuana-related businesses; or, 2) creating a new Panel under the authority of an existing Board/Commission to manage the City's oversight of marijuana-related businesses.

Board/Commission

Policy makers could create a new, independent Board of Commissioners to oversee all marijuana-related issues in the City. This Board could be modeled after others in the City, with five members appointed by the Mayor for staggered five-year terms and confirmed by the Council. With the exception of the Board of Public Works, all other City Boards are part-time, with Commissioners paid an attendance fee. A Board can be established by ordinance or by Charter amendment.

Panel

Instead of creating a new Board, the City could create a new Panel under the oversight of an existing Board of Commissioners, modeled after the Police Permit Review Panel (PPRP), which is responsible for issuing and overseeing permits for Café Entertainment and Shows, Motion Picture Shows, and Picture Arcades. The PPRP is composed of seven members, at least two of which have expertise that is relevant to the regulation of charitable organizations and the various activities in which they engage. Subsidiary Panels enable the Board they serve under to focus on major policy issues instead of permit issuance and oversight.

Insofar as all commercial marijuana activity is still illegal under federal law, a Police Department-affiliated body may not be the appropriate body to authorize such conduct. Ultimately, the decision to use an existing process, create a new process, or create a new entity to oversee marijuana business licenses in the City is a policy decision.

ACTION

F2. Should the entity responsible for regulating MRBs be part of an existing Department?

-Yes: Instruct staff to identify which Department is best suited to take on this authority.

-No: Instruct staff to identify what resources are needed to establish a new entity by ordinance. The new entity should be responsible for regulating all MRBs. Consider and provide examples for the following options:

- Board/Commission;
- Panel;
- Office; and,
- Department.

G. STATUS OF MARIJUANA ISSUES – FEDERAL

The scheduling of drugs in the United States comes from authority vested in Congress and the executive branch under the Controlled Substances Act of 1970. Under this law, Congress or the relevant federal agencies make determinations about substances based on their medical value, safety for medical treatment, and likelihood of abuse. The government assigns a drug to a schedule and has the power to reassign a substance to a different schedule (rescheduling).

The Drug Enforcement Administration (DEA) in its letter dated July 19, 2016, denied two petitions to reschedule marijuana under the Controlled Substances Act (CSA). In response to the petitions, DEA requested a scientific and medical evaluation and scheduling recommendation from the Department of Health and Human Services (HHS), which was conducted by the U.S. Food and Drug Administration (FDA) in consultation with the National Institute on Drug Abuse (NIDA). Based on the legal standards in the CSA, marijuana remains a Schedule I controlled substance because there is a lack of accepted safety for its use under medical supervision, and it has a high potential for abuse.

The CSA does not authorize state-approved and regulated marijuana enterprises to remain open. In fact, the CSA explicitly outlaws any such enterprise. The authority under which marijuana enterprises continue to operate, despite the substance's "absolute" prohibition under the CSA, is a series of memoranda issued by the Department of Justice (DOJ). These memos—the Cole and Ogden Memos—allow state-approved, heavily regulated operations to exist, so long as they do not violate certain areas of DOJ's concern, such as selling to minors or engaging with drug cartels.

These memos are executive actions that assert a Supreme Court-approved power of the presidency: enforcement discretion. Enforcement discretion allows the President and officials in the administration to make choices/priorities about how and under what circumstances laws will be enforced. The Cole and Ogden Memos are examples of how the Obama administration has de-prioritized the enforcement of the CSA for marijuana in certain states under certain conditions.

H. STATUS OF MARIJUANA ISSUES – STATE

The Medical Marijuana Regulation and Safety Act (MMRSA) became effective on January 1, 2016. It is comprised of three separate bills: Assembly Bill (AB) 243, AB 266 and Senate Bill (SB) 643. As a whole, the MMRSA creates the framework for a comprehensive state licensing and regulatory framework related to commercial medical marijuana activities, including cultivation, transport, manufacture, retail dispensing and testing. In all, the Act specifies seventeen types of commercial activities for licensure. The MMRSA also requires the establishment of a "track and trace program" for reporting the movement of medical marijuana products through the distribution chain.

The Bureau of Medical Marijuana Regulation, within the Department of Consumer Affairs (DCA), is the lead agency responsible for administration and implementation of the MMRSA. The MMRSA requires the DCA, the Department of Food and Agriculture and the Department of Public Health to promulgate regulations related to their respective responsibilities under the MMRSA. Areas to be regulated include indoor and outdoor cultivation, pesticide use, the production and labeling of edible medical marijuana products and protecting water quality.

Notwithstanding the state's licensing and regulatory authority under the MMRSA, it does not preempt the City's authority to regulate or ban commercial medical marijuana activities and businesses. The MMRSA provides expressed assurance that it is not intended to replace or restrict local medical marijuana regulation. Issuance of a state license or a determination of compliance with local law by the licensing authority shall in no way limit the ability of the City to prosecute any person or entity for a violation of, or otherwise enforce, Prop D or the City's zoning laws.

The MMRSA requires that, once state regulations are in place, all commercial medical marijuana activity be licensed by the state and authorized by the local jurisdiction where the activity is to take place: "Upon the date of implementation of regulations by the licensing authority, no person shall engage in commercial marijuana activity without possessing both a state license and a local permit, license, or other authorization. A licensee shall not commence activity under the authority of a state license until the applicant has obtained, in addition to the state license, a license or permit from the local jurisdiction in which he or she proposes to operate, following the requirements of the applicable local ordinance."

The MMRSA contains no specific date by which state regulations must be in place. However, the DCA has indicated in informational sessions that it intends to hold regulatory meetings in the summer and fall of 2016, notice draft regulations by early 2017, and issue final regulations by the end of 2017, with the goal of accepting applications by January 1, 2018. This timeline appears consistent with a provision that states, in part, "An entity that is operating in compliance with local zoning ordinances and other state and local requirements on or before January 1, 2018, may continue its operations until its application for licensure is approved or denied pursuant to this chapter."

Revocation of a local license, permit or other authorization shall terminate the ability of a medical marijuana business (MMB) to operate within that local jurisdiction until the jurisdiction reinstates or reissues the required authorization. Local authorities shall notify the DCA upon such revocation so relevant licensing authorities can be notified. Similarly, revocation of a state license shall terminate the ability of a medical marijuana licensee to operate within California until the licensing authority reinstates or reissues the state license.

Under the MMRSA's dual licensing framework, no MMB in the City of Los Angeles will be able to obtain a state license based on the present version of Prop D because Prop D does not provide for the issuance of a local permit, license or other authorization. Rather, it is premised on a blanket prohibition of all MMBs, subject only to a possible "limited immunity" from prosecution with respect to those MMBs that comply with all of its immunity requirements. Therefore, unless either Prop D or the MMRSA is changed to provide a path to state licensure, all MMBs in the City, including those presently in compliance with Prop D, will become unlawful under state law. The City may enact changes to Prop D, via ordinance or ballot initiative, to allow for the issuance of a local permit, license or other authorization to medical marijuana businesses.

The MMRSA restricts a commercial entity to a license with no more than two of the seventeen categories of distinct license classifications and further restricts which combinations of license categories can be held. Thus, it generally prohibits "vertical integration" of commercial marijuana businesses which, in this context, means the combination of more than two types of activities in the commercial marijuana supply chain, from cultivation to retail sale.

The MMRSA does not disturb local authority to levy fees and taxes. It expressly provides that "local jurisdictions retain the power to assess fees and taxes, as applicable, on facilities that are licensed pursuant to this chapter and the business activities of those licensees." Therefore, the City's ability to tax MMBs remains intact under both local and state law.

A bill to place an excise tax on medical marijuana in California was not approved on August 8, 2016 by a Senate panel after advocates for marijuana users said it would put a financial burden on patients. The Senate Appropriations Committee shelved AB 2243 with knowledge that California voters will consider a 15% excise tax and a \$9.25/ounce cultivation tax on all marijuana sales, including medical, on November 8, 2016 when they take up Proposition 64, which if passed, will also legalize recreational use of marijuana. Qualified patients possessing state ID cards would be exempted from paying sales tax on qualified medical marijuana purchases. The sales tax would be in addition to the excise and cultivation taxes.

| Method of Implementation for Policy Decisions | | | |
|--|---|---|---|
| Policy Area Section | Ballot Initiative* | Ordinance | Administrative |
| A - Fundamental Questions | None | A2 & A3 | A1, A2, & A3 |
| B - Retail Sales, Cultivation, Manufacture, Distribution, and Testing | None | B1, B2, B3, B4, B5, B6, B7, B8, & B9 | B1, B2, B3, B4, B5, B6, B7, B8, & B9 |
| C - Other Considerations | None | None | None |
| D - Zoning and Other Land Use Requirements | None | D1 | D2 |
| E - Revenue | E1 - Any imposition of new taxes or increase in existing taxes (e.g. business tax) requires voter approval. | E2 & E3 | None |
| F - Administration | None | F2 | F1 |

*Items listed in the ordinance and administrative columns may also be implemented through ballot initiative; however, a ballot initiative is not required.

List of Other California Cities with Marijuana Taxes

Berkeley

- 2.5% tax on gross sales receipts for medical marijuana
- 10% tax on recreational marijuana (in anticipation of legalization)

Oakland

- 5% tax on gross sales receipts
- Currently covers dispensaries

Cathedral City

- 10% tax on gross sales receipts
- It was 15%, but the City Council has adopted a resolution lowering it to 10%
- Covers all cannabis businesses, not merely dispensaries

Palm Springs

- 10% tax on gross sales receipts
- Can be increased to a maximum of 15%

Richmond

- Business License Tax of 5% of gross sales receipts
- Covers all cannabis businesses, not merely dispensaries

Sacramento

- 4% tax on gross sales receipts
- Enacted by voters
- Covers all cannabis businesses, not merely dispensaries

San Jose

- 10% tax on gross sales receipts
- Enacted by local ballot

Vallejo

- 10% tax on gross sales receipts
- Tax itself enacted by voters
- Council set the tax rate