



City of Emeryville

CALIFORNIA

MEMORANDUM

DATE: October 30, 2018
TO: Christine Daniel, City Manager
FROM: Charles S. Bryant, Community Development Director
SUBJECT: **Resolution Of The City Council Of The City Of Emeryville Establishing Initial Tax Rates For A Cannabis Business License Tax, Contingent Upon Measure S Taking Effect Following The November 6, 2018 General Election**

RECOMMENDATION

Staff recommends that the City Council adopt the attached resolution establishing initial tax rates for the cannabis business license tax, contingent upon Measure S taking effect following the November 6, 2018 general election.

BACKGROUND

At a December 19, 2017 study session, after reviewing public opinion polling results, the City Council directed staff to place a cannabis tax measure on the November 2018 ballot. Additionally, the City Council placed a housing bond on the June 2018 ballot, and continued to consider other potential revenue measures for the November 2018 ballot. The City also engaged EMC Research to conduct additional public opinion polling after the June 2018 election to determine the viability of various revenue measures, again including a cannabis tax.

On July 10, 2018, the City Council reviewed the results of the June 2018 polling and reaffirmed the direction to staff to proceed with the preparation of a cannabis business tax for the November 2018 ballot. The City Council directed staff to develop implementing ordinances for consideration, with options for how the tax rate would be set and/or modified in the future.

On July 24, 2018, the City Council considered three options for the cannabis business tax ordinance to be placed before voters. All three options provided for flexibility in setting different rates for different types of cannabis businesses (i.e. manufacturing, distribution, storefront retail, delivery, etc.) and all three options contemplated the form of the tax to be a gross receipts tax not to exceed 6%. Option 1 provided for the tax rate to be set by a simple majority vote of the City Council. Option 2 provided for the initial tax rate to be set by a simple majority vote, with the rates fixed for a period of five years, with any modifications to the rates after the five-year period subject to a supermajority (i.e. 4/5) vote of the City Council. Option 3 was similar to Option 2 except that lowering tax rates after the initial period would require a simple majority vote of the City Council, while raising rates after the initial period would require a supermajority vote.

The City Council selected Option 1, rates set and subject to modification by simple majority vote of the City Council, with a maximum rate of 6% of gross receipts. The resolution (Resolution No. 18-113) implementing this direction was submitted to the Alameda County Register of Voters and the measure was designated “Measure S”.

During the proceedings outlined above, the City Council received comments from the Emeryville cannabis business community regarding the current state of the market and the potential impacts of cannabis business taxation. Of particular concern was the businesses’ desire for certainty and stability of the City’s tax policy, as this influences the businesses’ ability to plan for the future while adapting to changing regulations and market factors as the cannabis industry is normalized.

To address these concerns, the City Council held a study session on September 17, 2018 to begin a discussion of initial cannabis tax rates in advance of the November election including Measure S. The study session included a review of the current cannabis market environment, the existing cannabis industry in Emeryville, and strategic considerations relating to a local cannabis business tax.

The City Council affirmed its intent to establish regulations that encourage the establishment of Emeryville as a regional hub for cannabis business activities, and provided direction to staff on initial tax rates. The City Council requested an agenda item for its October 30, 2018 Regular Meeting to consider establishing initial cannabis business tax rates contingent on the passage of Measure S.

DISCUSSION

In consideration of the current state of the cannabis market overall, as well as the industry in Emeryville today, the City Council directed staff to prepare a resolution to establish rates for different types of cannabis businesses, as follows:

State-Issued Medical Card Rebate

During the September 17, 2018 study session, the Council discussed the potential of establishing different rates for medical and adult-use cannabis sales. Because the City’s Cannabis Business Ordinance does not distinguish between medical and adult-use businesses, to implement this distinction in the cannabis business tax would require the collection of additional information from permittees and would add a layer of complexity to the administration of the proposed tax. Consequently, the City Council did not direct staff to establish different tax rates for medical and adult-use sales.

However, to provide cost relief for medical users in Emeryville, the City Council discussed establishing a program to rebate the cost of state-issued Medical Marijuana Identification Cards (“MMIC”) for Emeryville senior citizens, with the rebate funded by cannabis tax proceeds. MMIC card holders are exempt from sales tax on cannabis purchases, which translates to a 9.25% discount from adult-use prices for sales in Emeryville.

The MMIC Program is administered by the California Department of Public Health (“CDPH”). However, Proposition 64 requires county health departments to establish application fees for persons seeking to obtain MMICs, and Proposition 64 removed language authorizing CDPH to collect fees from the counties’ programs. County programs may charge an amount not to exceed \$100 per MMIC application or renewal, give a fifty percent reduction per card for Medi-Cal eligible applicants, and the fees must be waived for indigent patients who are eligible for and participate in the County Medical Services Program. The counties have authority to cover their expenses through the application fees; therefore, established fees vary by county.

In Alameda County, the MMIC application fee is \$100, or \$50 for applicants on Medi-Cal. Data on the MMIC program is only available at the county level. As of August 2018, 5,812 MMICs have been issued in Alameda County. Assuming MMIC holders are evenly distributed throughout Alameda County’s population, this would suggest that approximately 40 MMICs have been issued in Emeryville since the program’s inception.

Notably, both of Emeryville’s permitted storefront dispensaries have agreed to certain discount programs as part of their community benefits packages, and these requirements have been included in their Cannabis Business Permit (“Operator’s Permit”) Conditions of Approval. Both storefront retailers are required to develop low-income resident discount programs for Emeryville residents who hold an MMIC. The retailers are also required to provide a 10% discount to veterans and senior citizens aged 65 or older on all products upon presentation of proof of veteran status or age. These programs must be evidenced annually upon renewal of their Operator’s Permits.

Given that the MMIC program is administered by the County, the City of Emeryville would need to create a new administrative program to provide subsidies to seniors who obtain MMIC cards from the County. Should the City Council wish to proceed with establishing such a program, the Council would need to make findings supporting the public purpose of such a program in order to avoid any question of a gift of public funds. Those findings could be based on establishing income qualifications for the subsidy, or other findings that the Council could articulate. In light of the discounts described above that are already in place for veterans, seniors, and low-income residents, staff requests further direction from the City Council with regard to developing a new subsidy program for seniors who obtain MMIC cards.

Testing

State law requires independent lab testing of all cannabis products offered for sale. There are a limited number of licensed testing labs currently operating, which has led to delays in certifying product for the marketplace. Currently, there are no testing labs located in Emeryville; however, staff has corresponded with several prospective lab operators interested in locating in the City.

At its September 17, 2018 study session, the City Council decided to establish a tax of 1% of gross receipts on cannabis testing businesses, with a provision that the portion of

gross receipts derived from testing of cannabis products manufactured in Emeryville would be rebated to the testing business. The purpose of arranging the tax this way is to incentivize testing businesses to locate in Emeryville and to transact with Emeryville manufacturing businesses thus increasing overall benefit to the City of Emeryville.

Distribution

State law requires the use of licensed distributors to transport cannabis from manufacturers and cultivators to retailers (whether storefront dispensaries or delivery businesses). Emeryville has one distributor currently operating in the City.

The City Council decided to establish a tax of 1% of gross receipts on cannabis distribution businesses.

Manufacturing

Cannabis manufacturing businesses are engaged in a variety of production activities, from extraction to the production of finished edibles, topical products, and vaping cartridges. There are three cannabis manufacturing businesses in the City.

The City Council has decided to establish a tax of 2% of gross receipts on cannabis manufacturing businesses.

Storefront Retail and Delivery

Through a competitive Request for Qualifications ("RFQ") process, the City Council has authorized two storefront retail cannabis businesses in the City. One of the two commenced operations in September 2018, while the other anticipates opening in late 2018. The City permits non-storefront cannabis retail businesses (i.e. delivery) similar to cannabis manufacturing uses, in any zone in which cannabis manufacturing is allowed, with a Conditional Use Permit and Operator's Permit. The City has one delivery-only business in operation.

The City Council decided to establish a tax of 3% of gross receipts on cannabis storefront retail and delivery businesses. For the storefront retail businesses selected through the RFQ process, any community benefits proposed in the form of payments to the City or community grant programs would be waived in favor of the 3% gross receipts tax. East Bay Therapeutics is required to contribute 1% of gross receipts to the City plus an additional 1% of gross receipts to non-profit organizations serving the Emeryville community. Rochambeau is required to contribute 0.7% of gross receipts to the City plus an additional 0.3% to the Emeryville Citizen Assistance Program ("ECAP"). These contributions would be eliminated when the storefront retailer's Operator Permits are renewed and replaced by the 3% tax on gross receipts.

Timeframe of Initial Rates

The City Council expressed interest in establishing a time period during which the initial tax rates would be effective. This would provide a degree of certainty to Emeryville's cannabis businesses and assist their business planning efforts. Accordingly, the attached resolution includes a statement indicating that the initial tax rates are intended to be effective for a term of three years; however, staff notes that, due to the approved wording of Measure S, the rates may be altered by a simple majority vote of the City Council at any time.

FISCAL IMPACT

Specific revenue projections for various cannabis business tax rates cannot be publicly provided, due to the small number of businesses involved and the potential to reveal proprietary sales figures. In the aggregate, if the above tax rates are applied to Emeryville's existing businesses, the cannabis tax would generate an estimated \$720,000 annually. This estimate does not account for any additional cannabis businesses which may be induced to locate in Emeryville due to the City's central location, efficient permitting processes and relatively low taxes.

The longer term fiscal impact due to future growth or contraction of the cannabis industry in Emeryville is difficult to estimate and is particularly sensitive to the initial cannabis business tax rates. In general, the lower the initial rates, the greater opportunity for future sales growth due to success (expansion, increased sales) of existing businesses and attraction of additional businesses.

STAFF COMMUNICATION WITH THE PUBLIC

Staff has discussed revenue and taxation issues with Emeryville cannabis businesses over the past year in the course of providing business attraction and retention services.

CONCLUSION

Staff recommends that the City Council adopt the attached resolution to establish initial tax rates, contingent on the passage of Measure S.

PREPARED BY: Chadrick Smalley, Economic Development and Housing Manager

**APPROVED AND FORWARDED TO THE
CITY COUNCIL OF THE CITY OF EMERYVILLE:**



Christine Daniel, City Manager

ATTACHMENT:

1. Resolution Establishing Cannabis Business Tax Rates