

June 22, 2015

Hon. Kamala D. Harris
Attorney General
1300 I Street, 17th Floor
Sacramento, California 95814

Attention: Ms. Ashley Johansson
Initiative Coordinator

Dear Attorney General Harris:

Pursuant to Elections Code Section 9005, we have reviewed the proposed statutory initiative related to the cultivation, use, possession, and sale of marijuana (A.G. File No. 15-0027, Amendment #1).

BACKGROUND

Federal Law. Federal laws classify marijuana as an illegal substance and provide criminal penalties for various activities relating to its use. These laws are enforced by federal agencies that may act independently or in cooperation with state and local law enforcement agencies.

State Law and Proposition 215. Under current state law, the possession, cultivation, or distribution of marijuana generally is illegal in California. Penalties for marijuana-related activities vary depending on the offense. For example, possession of less than one ounce of marijuana is an infraction punishable by a fine, while selling marijuana is a felony and may result in a jail or prison sentence.

In November 1996, voters approved Proposition 215, which legalized under state law the cultivation and possession of marijuana in California for medical purposes. State law also authorizes cities and counties to regulate the establishment of medical marijuana dispensaries in their jurisdictions. The U.S. Supreme Court ruled in 2005, however, that federal authorities could continue under federal law to prosecute California patients and providers engaged in the cultivation and use of marijuana for medical purposes. Despite having this authority, the current policy of the U.S. Department of Justice (DOJ) is not to prosecute marijuana users and businesses that act in compliance with state and local marijuana laws so long as those laws are written and enforced in a manner that upholds federal priorities. These priorities include ensuring that marijuana is not distributed to minors or diverted from states that have legalized marijuana to those that have not. State and local governments currently collect sales tax on medicinal marijuana sales.

PROPOSAL

This measure changes state law to legalize the possession, cultivation, and sale of marijuana. Despite these changes to state law, activities related to the use of marijuana would continue to be prohibited under federal law.

State Legalization of Marijuana-Related Activities

Under the measure, individuals age 21 or over could legally possess, sell, transport, process, and cultivate marijuana under state law. The measure also prohibits state and local law enforcement agents from enforcing federal prohibitions on marijuana. Although the measure would generally legalize marijuana, certain marijuana-related activities would remain unlawful, including (1) operating a motor vehicle while under the impairment of marijuana, (2) smoking marijuana in public places, (3) exporting or importing to or from states where marijuana remains illegal under state law, or (4) providing marijuana to individuals under the age of 21.

Marijuana Cultivation for Personal Use

The measure permits the cultivation of marijuana for personal use of up to 500 square feet per adult, up to a maximum of 1,500 square feet per parcel. In addition, individuals could possess the following amounts of marijuana for personal use: (1) five pounds of dried marijuana flowers, (2) one pound of marijuana extract (such as hash), and (3) three gallons of liquid marijuana extract. The measure states that all marijuana gardens must be completely obscured from public view, with the exception of aerial observation, and that all marijuana cultivated or possessed for personal use must be made inaccessible to the public and minors. In addition, the measure states that individuals cultivating marijuana must comply with all local, county, and state building and property ordinances. However, the measure specifies that local governments cannot impose any “discriminatory” zoning requirements or other restrictions on the cultivation or possession of marijuana for personal use.

Regulation of Marijuana Businesses

The measure states that local governments cannot ban the cultivation, sale, or use of recreational or medical marijuana. However, the measure allows cities to restrict the number of recreational marijuana businesses based on “legal reasonable necessity policies.” In addition, the measure also requires various state departments to regulate different aspects of the marijuana industry. For example, it requires the Department of Public Health (DPH) to regulate marijuana testing facilities, the Department of Food and Agriculture (DFA) to regulate marijuana that is consumed for dietary (such as non-psychoactive) purposes, and various state agencies, including the California Environmental Protection Agency (CalEPA) to regulate marijuana that is non-consumable and intended for industrial use (such as in cosmetic or clothing products).

As we discuss below, the measure also includes provisions specifically related to recreational and medical marijuana.

Regulation of Recreational Marijuana. The measure changes the name of the Department of Alcohol Beverage Control to the Department of Cannabis and Alcoholic Beverage Control (DCABC) and requires it to develop and implement regulations for recreational marijuana. For

example, the department would be required to develop licensing regulations for marijuana businesses. According to the measure, the licensing of recreational marijuana businesses must be analogous to and no more onerous than the licensing of businesses selling beer and wine. In addition, the measure states that any violation of license requirements established by the department would be punished consistent with punishments for alcohol-related violations. The measure also requires the DFA to license businesses cultivating, processing, or producing recreational marijuana. In addition, the measure includes various requirements related to recreational marijuana businesses. For example, the measure prohibits: (1) recreational marijuana delivery services; (2) the establishment of businesses that sell only recreational marijuana within 1,000 feet of a school, licensed daycare facility, public playground, or nonprofit youth facility; and (3) the employment of individuals under the age of 21 by recreational marijuana businesses.

Regulation of Medical Marijuana. The measure requires that medical marijuana be sold through either a traditional pharmacy or a medical marijuana pharmacy licensed by DPH and the State Board of Pharmacy (BOP) within the Department of Consumer Affairs in a manner analogous to existing traditional pharmacies. The measure states that existing medical marijuana dispensaries would by default be considered recreational marijuana businesses unless the dispensary is granted a license to become a medical marijuana pharmacy. The measure also requires that all farms or facilities cultivating medical marijuana be regulated by DPH and DFA.

Taxation of Marijuana

Taxation of Recreational Marijuana. The measure states that state and local sales taxes would apply to marijuana sold for recreational use but that no recreational marijuana-specific taxes could be imposed by local governments. The measure also places a permanent 15 percent excise tax on recreational marijuana products beginning on January 1, 2017. Under the measure, revenue from the excise tax would be allocated to different entities for specified purposes, including K-12 public schools and public universities, state agencies responsible for the regulation of recreational marijuana, state and local law enforcement, and grants for research related to medical marijuana.

In addition, the measure places a temporary 5 percent implementation tax on all retail sales of recreational marijuana between January 1, 2017 and January 1, 2022. Under the measure, the revenues from the implementation tax would be allocated to different entities for specified purposes, including state agencies responsible for the regulation of recreational marijuana, the Department of Corrections and Rehabilitation to facilitate the measure's proposed release of marijuana offenders (as described below), the Department of Education for marijuana-related education programs, and local governments.

Taxation of Medical Marijuana. The measure states that medical marijuana would not be subject to any state or local sales tax and that no medical marijuana-specific taxes could be imposed by local governments. The measure places a temporary implementation tax of 10 percent on all sales of medical marijuana between January 1, 2017 and January 1, 2022. Under the measure, half of the revenue from the implementation tax would be allocated for the BOP. The remaining half of the revenue would be used to educate health care professionals regarding medical marijuana. Beginning January 1, 2022, the measure places a permanent

3 percent “maintenance” tax on medical marijuana. Under the measure, BOP, DFA, and DPH would each receive 33 percent of the revenue from the maintenance tax. The remaining 1 percent of revenue would be allocated to the state General Fund.

Taxation of Industrial and Dietary Marijuana. Under the measure, industrial and dietary marijuana would be subject to state and local sales tax, but no industrial or dietary marijuana-specific taxes could be imposed by local governments. However, the measure places additional state taxes on industrial and dietary marijuana at various rates depending on its form. Such taxes include \$1 per pound of dry flowers, 10 cents per pound of dietary oil, and 5 cents per pound of fiber or pulp. Under the measure, the CalEPA, the Division of Occupational Safety and Health within the Department of Industrial Relations, and DFA would each receive 30 percent of the revenue from the above taxes. The remaining 10 percent would be allocated for road improvements.

Other Provisions

Individuals Previously Convicted of Marijuana Crimes. The measure requires the release of all non-violent offenders currently in state correctional facilities solely for marijuana-related offenses. In addition, the measure requires the expungement of criminal records and the dismissal of fines or warrants for non-violent offenders who have committed only marijuana-related offenses.

Marijuana Drug Testing. The measure also prohibits the use of drug testing for marijuana unless performed by an agent of the state in an official capacity. Under the measure, law enforcement agents could no longer use existing drug testing methods (such as blood, urine, hair, or saliva testing) to determine when a driver is impaired by marijuana. The measure requires the state to instead develop a “performance-based” standard to test whether drivers can safely operate a motor vehicle.

FISCAL EFFECTS

The provisions of this measure would affect both costs and revenues for state and local governments. The magnitude of these effects would depend upon (1) the extent to which the U.S. DOJ exercises its discretion to enforce federal prohibitions on marijuana activities otherwise permitted by this measure and (2) how, and to what extent, the state chooses to regulate the commercial production and sale of marijuana. Thus, the potential revenue and expenditure impacts of this measure described below are subject to considerable uncertainty.

Reduction in Various Criminal Justice Costs. The measure would result in reduced costs to the state and local governments by reducing the number of marijuana offenders incarcerated in state prison and county jail, as well as the number placed under community supervision (such as county probation). In addition, the measure would result in a reduction in state and local costs for the enforcement of marijuana-related offenses and the handling of related criminal cases in the state court system. The above reductions would be offset somewhat in the short term by a temporary increase in costs to state trial courts and state and local law enforcement agencies to destroy records of arrest and conviction for certain marijuana-related crimes. In total, we estimate that the net reduction in state and local criminal justice costs from the above changes

could eventually range from the tens of millions of dollars to potentially exceeding \$100 million annually. In many cases, however, these resources would likely be redirected to other law enforcement and court activities.

Other Fiscal Effects on State and Local Programs. The measure could also have fiscal effects on various other state and local programs. For example, the measure could result in an increase in the consumption of marijuana, potentially resulting in an unknown increase in the number of individuals seeking publicly funded substance abuse treatment. This measure could also potentially reduce both the costs and offsetting revenues of the state's Medical Marijuana Program, a patient registry that identifies those individuals eligible under state law to legally purchase and consume marijuana for medical purposes. This is because individuals could legally possess marijuana under the measure without participating in the Medical Marijuana Program. In addition, the measure would result in costs for the state to regulate the commercial production and sale of marijuana. These costs could vary depending on how, and to what extent, the state chooses to implement the above regulations but would be unlikely to exceed several tens of millions of dollars annually. Eventually these costs could be largely or entirely offset by regulatory fees authorized by the measure to be levied on marijuana-related businesses, as well as revenue from taxes imposed by the measure.

Effects on State and Local Revenues. Assuming passage of the measure does not result in a significant change in the federal government's enforcement activities, the measure would result in increased governmental revenues. First, state and local governments would receive additional revenues, such as sales taxes, from marijuana sales permitted under this measure. This is because many individuals who are currently purchasing marijuana illegally could begin purchasing it legally under state law at businesses that collect such taxes. In addition, the state would also receive revenue from the various taxes imposed on marijuana by the measure. As noted earlier, the revenues derived from the taxes imposed by the measure would be allocated for various purposes. Since the measure prohibits sales taxes on medical marijuana, the above revenues would be partially offset by the loss of such taxes currently being collected.

In addition, the measure could result in an increase in taxable economic activity in the state, as businesses and individuals currently producing and selling marijuana illegally could begin doing so legally under state law and pay personal income and corporation taxes. Moreover, the measure would increase economic activity in the state to the extent that out-of-state consumers redirect spending into the state. The magnitude of the net increase in economic activity is unknown and would depend considerably on the extent to which the federal government enforces marijuana laws in California.

In total, our best estimate is that the state and local governments could eventually collect net additional revenues of up to several hundred million dollars annually.

Effects on Fine and Asset Forfeiture Revenues. The measure could reduce state and local revenues from the collection of the fines established in current law for marijuana offenses and the assets that are forfeited in some criminal marijuana cases. We estimate that these revenues could amount to millions or low tens of millions of dollars annually. This could be somewhat offset, however, by fines imposed by DCABC.

Summary of Fiscal Effects. We estimate that this measure would have the following major fiscal effects, which could vary considerably depending on (1) future actions by the federal government to enforce federal marijuana laws and (2) how, and to what extent, the state chooses to regulate the production and sale of marijuana.

- Net reduced costs ranging from tens of millions of dollars to potentially exceeding \$100 million annually to state and local governments related to enforcing certain marijuana-related offenses, handling the related criminal cases in the court system, and incarcerating and supervising certain marijuana offenders.
- Net additional state and local tax revenues of potentially up to several hundred million dollars annually related to the production and sale of marijuana, a large portion of which would be required to be spent for specific purposes such as education, public safety, and regulation of commercial marijuana activities.

Sincerely,

Mac Taylor
Legislative Analyst

Michael Cohen
Director of Finance