



February 5, 2016

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, possession, and sale of marijuana (A.G. File No. 15-0120).

Background

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 made it legal under state law for individuals of any age to cultivate and possess marijuana in California for medical purposes only, specifically with a recommendation from a licensed physician. In 2003, the Legislature authorized the formation of medical marijuana cooperatives, which are nonprofit organizations of medical marijuana users that cultivate and distribute marijuana to their members through outlets known as dispensaries. State law also gives cities and counties the discretion to regulate the location and operation of such facilities. State and local governments currently collect sales tax on medical marijuana. A small number of cities also impose additional taxes on medical marijuana sales. We estimate that the total amount of state and local revenue collected statewide from the above taxes likely is in the high tens of millions of dollars annually.

In 2015, the Legislature passed and the Governor signed into law legislation to regulate the commercial medical marijuana industry, creating the Bureau of Medical Marijuana Regulation within the Department of Consumer Affairs as the lead enforcement agency. Pursuant to the legislation, medical marijuana cooperatives are in the process of being phased out within a few years and replaced by state-licensed businesses that cultivate and distribute medical marijuana. Local governments maintain the authority to regulate the location and operation of such businesses. The legislation also requires the state to set standards for labeling, testing, and

packaging medical marijuana products and to develop a system to track such products throughout the supply chain.

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. The U.S. Supreme Court ruled in 2005 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 other states.

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 21 years of age or older could legally possess, sell, transport, process, and cultivate marijuana under state law. However, it would remain unlawful for individuals to operate a motor vehicle while under the impairment of marijuana or to provide marijuana to individuals under the age of 21. The measure states that it shall be the responsibility of the Legislature to implement any regulations necessary under the measure.

Taxation of Marijuana Sales. The measure states that existing state and local sales taxes shall be applied to marijuana sold for recreational use. In addition, the measure states that the Legislature could place excise taxes on the retail sale of recreational marijuana products of up to 15 percent of their retail price. However, the measure states that marijuana sold for medical purposes shall be exempt from all sales, use, and excise taxes.

Other Provisions. The measure requires the state to establish and fund “cannabis-only diversion programs” in each county. The measure states that violations of any statute or regulation enacted or promulgated to implement the measure shall not constitute a felony and shall not be punished by imprisonment. The measure also authorizes cities and counties to ban, or limit the number of, marijuana businesses within their boundaries if such restrictions are approved by their electorate.

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) how, and to what extent, state and local governments choose to regulate and tax the commercial production and sale of marijuana, (2) future consumption by marijuana users, and (3) the extent to which the U.S. DOJ exercises its discretion to enforce federal prohibitions on marijuana activities

otherwise permitted by this measure. 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 measure would also result in state costs to establish cannabis-only diversion programs in each county. The magnitude of these costs is unknown but is unlikely to exceed several million dollars annually. In total, we estimate that the net reduction in state and local criminal justice costs from the above changes could 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 use 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.

Effects on State and Local Revenues. State and local governments would receive additional revenues, such as sales taxes from recreational marijuana sales permitted under this measure. This is largely because many individuals who are currently purchasing marijuana illegally could begin purchasing it legally under state law at businesses that collect sales taxes. In addition, the state could also receive revenue from excise taxes, if such taxes were enacted by the Legislature. However, since the measure prohibits sales and use taxes on medical marijuana products, these revenues would be partially offset by the loss of sales tax currently collected on medical marijuana sales.

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 (such as tourists) redirect spending into the state. In total, our best estimate is that the state and local governments could eventually collect net additional revenues of potentially up to several hundred million dollars annually, which assumes the enactment of an excise tax. The potential revenues could be substantially less if a significant portion of consumers purchase marijuana for medical rather than recreational use since the measure exempts medical marijuana from sales, use, and excise taxes.

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.

Summary of Fiscal Effects. We estimate that this measure would have the following major fiscal effects, which could vary considerably depending on (1) how, and to what extent, state and local governments choose to regulate and tax the commercial production and sale of marijuana, (2) future consumption by marijuana users, and (3) the extent to which the U.S. Department of Justice exercises its discretion to enforce federal prohibitions on marijuana activities otherwise permitted by this measure.

- 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.

Sincerely,

Mac Taylor
Legislative Analyst

Michael Cohen
Director of Finance