

October 14, 21015

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. 15-0052, Amendment #2).

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 other states. State and local governments currently collect sales tax on medicinal marijuana sales. A small number of cities also impose a supplemental tax on medical marijuana retail 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 states that state and local governments are prohibited from enforcing federal prohibitions on marijuana. Although the measure would generally legalize marijuana, certain marijuana-related activities would remain unlawful, including operating a motor vehicle while under the impairment of marijuana or providing marijuana to individuals under the age of 21.

Marijuana Possession and Cultivation for Personal Use. Under the measure, the cultivation and possession of marijuana for personal use generally would be exempt from regulation. The measure specifies limits on the amount of marijuana that could be cultivated or possessed for personal use. For example, individuals could not (1) cultivate a marijuana garden that exceeds six mature plants and 25 square feet in size or (2) possess more than 30 grams of dried marijuana. However, the measure provides certain exemptions to the above limits. For example, individuals could possess more than 30 grams of dried marijuana if it is a product of their personal garden or the marijuana is purchased from a licensed retailer and is not for resale. In addition, local governments could place certain restrictions on cultivation for personal use, such as by requiring that outdoor plants not be visible from a public place.

Regulation of Commercial Marijuana Activities. This measure establishes the Cannabis Regulatory Control Commission within the Department of Consumer Affairs (DCA) to regulate the commercial cultivation, processing, distribution, and sales of marijuana for recreational or medical use. The measure authorizes the commission to monitor compliance with its regulations; investigate suspected violations; and restrict, suspend, or revoke business licenses of violators. Individuals or organizations engaging in various marijuana-related commercial activities—including cultivation, processing, transportation, distribution, and sales of marijuana—would be required to pay various fees and obtain a license from the commission. For example, the measure would impose fees on commercial marijuana production generally ranging from 25 cents to \$5 per square foot of marijuana plant canopy depending on (1) the number of square feet of marijuana being cultivated; (2) whether the plants are indoors, outdoors, or in a greenhouse; and (3) whether the producer uses certain sustainable agricultural practices (such as by employing renewable energy). The measure states that the above fees are effective only until January 1, 2022, but that the Legislature could extend the fees prior to that date with a 55 percent vote. The measure also establishes the Cannabis Regulatory Control Appeals Board within DCA to hear appeals from individuals disputing decisions made by the commission. Under the measure, individuals could appeal decisions made by the board to the state Courts of Appeal or the California Supreme Court.

Taxation of Commercial Marijuana Sales. The measure establishes statewide excise taxes on marijuana products, which would initially be set at 42 cents per gram of dried marijuana and \$2 per gram of concentrated marijuana products (such as hash). Under the measure, these taxes would increase annually beginning on January 1, 2020 by the rate of inflation. The measure

states that the Legislature could (1) reduce the above tax rates with a majority vote or (2) increase the above tax rates, or impose additional taxes on marijuana, with a two-thirds vote. In addition, the measure establishes a temporary excise tax of 2.5 percent on the retail sale of marijuana products sold between July 1, 2017 and January 1, 2019. The measure also states that (1) no excise taxes shall be imposed on medical marijuana sold directly to patients, or to businesses that sell only to medical marijuana patients, and (2) no sales taxes shall be imposed on medical marijuana sold to patients diagnosed with a terminal illness. The measure also allows the Legislature to provide additional exemptions from the excise tax with a majority vote.

Revenues collected from the excise taxes would be deposited in a new special fund—the Safe Communities, Parks, and Schools Fund. The measure requires revenues deposited in the fund to first be used to reimburse state and local governments for various costs associated with implementing the measure. For example, the revenues would be used to (1) support the cost of regulating and taxing the commercial marijuana industry and (2) reimburse trial courts and local law enforcement agencies for costs associated with destroying criminal records and resentencing individuals convicted of certain marijuana-related crimes (as discussed below). Any remaining funds would be allocated as follows: (1) 34 percent for school and community-based drug education and counseling services, (2) 33 percent for projects related to the restoration and protection of state parks and public lands impacted by the production of marijuana, and (3) 33 percent for research related to the medical use of marijuana. However, the measure states that the Legislature could allocate the remaining funds for other purposes with a two-thirds vote.

The measure also authorizes local governments to impose various taxes on marijuana, subject to certain conditions. Specifically, local governments could impose general purpose taxes on the sale of marijuana products provided such taxes (1) do not exceed a combined rate of 5 percent (whether on wholesale or retail sale) and (2) are approved by a majority vote of the electorate. In addition, local governments could impose special purpose taxes provided such taxes (1) do not exceed a combined rate of 5 percent (whether on wholesale or retail sale) and (2) are approved by a two-thirds vote of the electorate. However, the measure states that the Legislature could increase the limit on these tax rates with a two-thirds vote. The measure also states that no local excise taxes can be imposed on medical marijuana sold directly to patients, or to businesses that sell only to medical marijuana patients.

Local Government Restrictions on Marijuana Businesses. The measure allows local governments to establish certain restrictions on the establishment of marijuana businesses. For example, local governments could prohibit the establishment of (1) retail stores selling marijuana for recreational use in areas not zoned for commercial use, (2) businesses cultivating marijuana in areas not zoned for agricultural or industrial use, or (3) any marijuana businesses in areas zoned for residential use. Local governments could also limit the size of licensed marijuana cultivation operations to 1,000 square feet for indoor operations, 3,000 square feet for greenhouse operations, and 5,000 square feet for outdoor operations. In addition, a local government could establish further restrictions, such as completely banning marijuana businesses, if such restrictions are approved by a majority vote of its electorate.

Individuals Previously Convicted of Marijuana Crimes. Under the measure, individuals currently serving a sentence for certain marijuana-related crimes that would not have been

crimes or would have been subject to lesser penalties had the measure been in place when they were committed would be eligible for resentencing. For example, an offender serving a misdemeanor or a felony sentence for possessing, cultivating, or selling marijuana would be eligible to be resentenced. However, a court would not be required to resentence offenders if it determined that doing so would pose an unreasonable risk to public safety. In addition, individuals who have already completed their sentences for such crimes could apply to the courts to have their convictions reclassified as misdemeanors or infractions. The measure also requires the destruction of arrest and conviction records for individuals previously arrested or convicted for certain marijuana-related offenses including possession, cultivation, or giving away marijuana.

Authorization of Criminal Penalties. The measure creates various new marijuana-related crimes. For example, under the measure it would be a misdemeanor crime punishable by a fine of up to \$5,000 and/or up to a year in county jail to sell more than specified amounts of marijuana in a manner that is not authorized by the measure (such as without a proper license). It would also be a misdemeanor crime to make a false statement when applying for a marijuana business license. In addition, the measure states that possessing marijuana in an amount that exceeds the limits established by the measure is a misdemeanor crime.

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 and Court Costs. The measure would result in reduced costs to the state and local governments by reducing the number of marijuana offenders incarcerated in state prisons and county jails, 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. In total, we estimate that the 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.

In the short term, the measure would result in a temporary increase in costs to state trial courts and state and local law enforcement agencies to (1) destroy records of arrest and conviction for certain marijuana-related crimes, (2) resentence individuals serving sentences for certain marijuana-related crimes, (3) reclassify prior convictions of individuals convicted of certain marijuana-related crimes, and (4) hear appeals from individuals contesting decisions by the board. The measure states that these costs would be reimbursed from revenue generated by the new fees and taxes it imposes.

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. Any additional costs could be partially or entirely offset by additional funding allocated by the measure for 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. 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 would be entirely offset by fees authorized by the measure to be levied on marijuana-related businesses, as well as revenues from excise taxes imposed on marijuana sales.

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 excise taxes imposed on marijuana by the measure. As noted earlier, the revenues derived from the excise taxes would be deposited in the Safe Communities and Parks Account to support the costs of regulating the marijuana industry as well as various programs. Since the measure prohibits local retail 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 (such as tourists) 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, the state and local governments could eventually collect net additional revenues of up to several hundred million dollars annually. To the extent local governments impose additional taxes on marijuana, this amount would increase. To the extent that a significant amount of marijuana is purchased for medical rather than recreational use, this amount could be substantially less since the measure exempts certain medical marijuana transactions from excise and/or sales and use taxes.

Effect 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 additional fine revenue generated from the new penalties created by the measure (such as for violating regulations established by the commission).

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. DOJ 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, most of which is designated to be spent on drug education and counseling services, state parks, research related to the medical use of marijuana, and regulation of commercial marijuana activities.

Sincerely,

Mac Taylor
Legislative Analyst

Michael Cohen
Director of Finance