

December 23, 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. 15-0104, Amendment #1).

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 legislation to regulate the commercial medical marijuana industry, with a new Bureau of Medical Marijuana Regulation within the Department of Consumer Affairs as the lead enforcement agency. Under the legislation (effective January 2016), medical marijuana cooperatives will be phased out within a few years and replaced by state-licensed businesses. In particular, businesses cultivating marijuana will be licensed by the Department of Food and Agriculture (DFA); businesses testing and processing marijuana will be licensed by the Department of Public Health (DPH); and businesses transporting, distributing, and retailing marijuana will be licensed by the bureau. Local governments will continue to have the authority to regulate the location and operation of such businesses. The legislation also requires the

state to set standards for labelling, 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 age 21 or over could legally possess, use, sell, transport, and cultivate recreational marijuana under state law. However, certain marijuana-related activities would remain illegal. For example, it would remain unlawful for individuals to operate a motor vehicle while under the impairment of marijuana or provide non-medicinal marijuana to individuals under the age of 21. The measure also states that no employer may terminate, or take any other adverse action against, an employee for using recreational marijuana unless (1) the employee possesses or is impaired by marijuana while at work or (2) the employer has a contractual or statutory requirement to maintain a drug-free workplace.

Regulation of Commercial Marijuana Activities. This measure authorizes the state Board of Equalization to regulate commercial cultivation, manufacturing, distribution, and sales of recreational marijuana. Individuals or organizations engaging in commercial manufacturing, distribution, and retail sale of recreational marijuana would be required to obtain a license from the board. The measure authorizes the board to charge license fees in order to cover the cost of regulating the recreational marijuana industry. The measure requires the board to develop an electronic system for reporting the movement of recreational marijuana products throughout the supply chain. The measure also requires other state agencies to regulate certain aspects of the recreational marijuana industry. Specifically, it requires DFA and the state Department of Pesticide Regulation to regulate cultivation and DPH to regulate manufacturing, packaging, testing, labeling, and storage. Under the measure, the state would have the exclusive authority to regulate recreational marijuana and any local laws that conflict with the measure would be preempted.

Taxation of Commercial Marijuana Sales. The measure states that existing state and local sales and use taxes shall be applied to the sale of marijuana. In addition, the measure places a state excise tax of 5 percent on the retail sale of recreational marijuana. The measure states that the state excise tax shall be the only state tax applied specifically to the sale of marijuana. The measure also authorizes cities and counties to place additional taxes on marijuana. Specifically, a city or county could implement (1) a cultivation tax of up to \$2 per square foot of plant canopy on all marijuana and

(2) a retail sales tax of up to 5 percent on recreational marijuana. The measure states that these local taxes shall be in lieu of any local taxes placed specifically on marijuana.

Revenues collected from the state marijuana excise tax would be deposited in a new special fund, the Cannabis Tax Fund. According to the measure, monies deposited in the fund would first be allocated for the following purposes (in order of priority): (1) to reimburse the board for its cost of collecting taxes on marijuana, (2) to reimburse state agencies for the costs of regulating the commercial marijuana industry, (3) to support research on the implementation and effects of the measure, and (4) to support research on the medical use of marijuana. Any remaining funds after the above allocations would be annually allocated as follows:

- 40 percent for the California Department of Education to fund preschool programs.
- 40 percent for various state agencies to clean up and restore environmental damages created by illegal marijuana cultivation and for the operation and maintenance of the state park system.
- 20 percent for research into curing or managing certain diseases (such as cancer) that affect children.

Local Zoning Regulations for Marijuana Businesses. Under the measure, the retail sale of recreational marijuana would be limited to areas zoned for commercial, manufacturing, or industrial uses. In addition, the measure states that recreational marijuana may be cultivated, manufactured, and stored on premises zoned for agricultural, manufacturing, or industrial use. Under the measure, businesses cultivating, manufacturing, testing, selling, or distributing recreational marijuana could not be located within 600 feet of a school, unless otherwise allowed by local ordinance. Cities and counties could establish additional zoning regulations for retail recreational marijuana businesses provided the regulations do not completely ban such businesses or “unreasonably” restrict access to marijuana.

Marijuana Cultivation and Possession for Personal Use. Under the measure, individuals over the age of 21 could lawfully (1) possess for personal use three ounces or less of marijuana and products (such as edibles) containing six grams or less of the psychoactive ingredient found in marijuana in a public place and (2) cultivate up to six marijuana plants for personal use. Individuals could also lawfully possess any amount of marijuana for personal use provided that it is possessed on private property. Under the measure, cultivation of recreational marijuana for personal use that takes place on a property zoned for residential use would only be allowed indoors or in a greenhouse structure with a locking door.

Authorization of Civil and Criminal Penalties. Under the measure, it would be a misdemeanor crime punishable by a fine of up to \$5,000, imprisonment in county jail for up to one year, or both, to engage in the business of manufacturing, distributing, transporting, or selling recreational marijuana without a license. In addition, any person engaging in unlicensed commercial recreational marijuana activities would be subject to civil penalties of up to twice the amount of the license fee for each violation. The measure also states that providing recreational marijuana products to individuals under the age of 18 would be punished in the same way as if they were cigarettes.

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. In total, we estimate that the 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. In addition, the measure would result in costs for the state to regulate the commercial production and sale of recreational marijuana. These costs would vary depending on how, and to what extent, the state chooses to regulate marijuana but would be unlikely to exceed several tens of millions of dollars annually. Eventually these costs would likely be entirely offset by revenues from license fees and the state excise tax on recreational marijuana.

Effects on State and Local Revenues. State and local governments would receive additional revenues, such as sales taxes from 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 would receive revenue from the state excise tax imposed by the measure on recreational marijuana. As noted earlier, the revenues derived from the excise tax would be deposited in the Cannabis Tax Fund to reimburse state implementation costs and to benefit various programs including preschool education, environmental protection, and medical research. 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. However, since the measure preempts existing local taxes specifically on medical marijuana the above revenues would be slightly offset by the loss of such taxes. 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 additional fine revenue generated from the new penalties created by the measure (such as for engaging in unlicensed commercial recreational marijuana activities).

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 up to several hundred million dollars annually related to the production and sale of marijuana, a portion of which would be required to be spent to reimburse state implementation costs and to benefit various programs including preschool education, environmental protection, and medical research.

Sincerely,

Mac Taylor
Legislative Analyst

Michael Cohen
Director of Finance