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CANNABIS REGULATION**

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February 8, 2019

Honorable Members of the Rules, Elections, and Intergovernmental Relations Committee
City Clerk
City Hall, Room 395

**DEPARTMENT OF CANNABIS REGULATION - RECOMMENDATION FOR AMENDMENTS
TO THE CITY'S CANNABIS PROCEDURES (C.F. 14-0366-S5)**

Dear Honorable Members:

The Department of Cannabis Regulation appreciates the opportunity to report on the status of the City of Los Angeles's commercial cannabis regulatory program at the February 15, 2019 meeting of the Rules, Elections, and Intergovernmental Relations Committee. In advance of the meeting, DCR would like to recommend a number of amendments to the regulatory program that it believes would make our licensing process more efficient, transparent, and, most important, equitable.

In November 2016, the people of the State of California voted to approve Proposition 64, the Adult Use of Marijuana Act (AUMA), which decriminalized certain activities related to non-medical cannabis in California. Subsequently, the state enacted the Medicinal and Adult-Use Cannabis Regulation and Safety Act to establish a system to control and regulate the cultivation, distribution, transport, storage, manufacturing, processing and sale of both medicinal and recreational cannabis. The AUMA also provided for state licensing of commercial cannabis businesses, starting January 1, 2018. State law requires city approval in order to obtain a State License.

After the passage of Measure M, which authorized the City to license, regulate and enforce commercial cannabis activity in March 2017, the City Council established DCR and the Cannabis Regulation Commission to implement and administer related laws and regulations as they were established.

Since its inception, DCR has been working diligently alongside the Commission, and other relevant City agencies, to advise and implement the City's commercial cannabis program and related policies according to the laws, rules and regulations established by the City Council and approved by the Mayor. These laws established a comprehensive framework detailing the process for commercial cannabis licensing, including but not limited to operating requirements for commercial cannabis businesses and restrictions on the siting of commercial cannabis businesses throughout the City.

The established commercial cannabis licensing procedures require DCR to process applications to engage in commercial cannabis activity in a specified order beginning first with two phases of “Priority Processing”. The first phase of Priority Processing, commonly referred to as Phase 1, requires DCR to begin its licensing process by first administering applications to determine eligibility for *Proposition M Priority Processing*. The second phase of Priority Processing, commonly referred to as Phase 2 requires DCR to, subsequent to Phase 1, administer applications to determine eligibility for *Non-retailer Commercial Cannabis Activity Prior To January 1, 2016, Processing*. The commercial cannabis licensing procedures further require DCR to begin to administer the annual licensing process, first giving priority application review to qualified Phase 1 and Phase applicants before opening the process to new applicants.

After commencing these initial phases of priority processing, the ordinances require DCR to receive and process additional license applications with certain restrictions based on the City’s Social Equity Program which is set for in LAMC 104.20. The concept of a Social Equity Program was first discussed in May 2016, when while initially considering the licensing and regulation of commercial cannabis activity, the City Council began to explore options to “promote equitable ownership and employment opportunities in the cannabis industry in order to decrease disparities in life outcomes for marginalized communities and to address the disproportionate impacts of the war on drugs in those communities.”

To accomplish this purpose, the City established a program to provide priority processing and certain benefits to qualifying program participants. These program benefits include the following: 1. business, licensing and compliance assistance; 2. expedited renewal processing; 3. program site specific conditions; 4. the potential for fee deferrals if the City Council adopts a fee deferral program; and 5. access to an Industry Investment Fund if established. Furthermore, LAMC Sec. 104.20 (j) requires DCR to establish the following programs and incentives: 1. Recruitment and outreach to support the Social Equity Program; 2. Business, licensing and compliance assistance; 3. General business assistance; and 4. a registry for incubator projects that offer education and training to qualifying program participants.

Over the past year, as the City has begun to implement its commercial cannabis regulatory program, DCR has managed the City’s turbulent and ever-evolving transition into the nation’s, and potentially, world’s, largest municipal medical and adult-use commercial cannabis licensing and regulatory program. Some of our most critical past and ongoing efforts include but are not limited to the following:

- Continuing to appropriately hire staff and obtain resources for the Department
- Holding several public hearings in partnership with the Cannabis Regulation Commission
- Coordinating intra-City cannabis policy and program development and implementation
- Granting more than 180 Temporary Approvals as a part of Phase 1
- Receiving and processing approx. 600 applications as a part of Phase 2, with dozens of businesses having already received Temporary Approval
- Responding to hundreds of requests to verify local authorization from California agencies involved in commercial licensing and regulation
- Engaging with California agencies regarding ever-changing state laws and regulations

- Participating in dozens of events with community-based organization and cannabis industry organizations and hosting a number of workshops to educate interested parties on the City's licensing process
- Supporting the City's effort to enforce against unlicensed cannabis operators

Although we have taken many steps towards a more perfect process for the many stakeholders involved in, or impacted by the City's cannabis policies, DCR acknowledges that there is still much work to be done to meet our duties to promote community health and safety, harm reduction and equity within the administration of our programs. Below are DCR's recommendations to the City Council which the Department believes will help it meet the aforementioned goals of our programs.

A. Update on Implementation of Phase 3 Storefront Retail Licensing

Since the start of the City's commercial cannabis regulatory program in January 2018, DCR has been carefully considering how to implement a Phase 3 storefront retail licensing process that is efficient, transparent, and, most important, equitable. DCR recognizes that the existing licensing process provided in the Cannabis Procedures ordinance and regulations will take significant time to implement and that many Phase 3 storefront retail applicants will have to make significant investments in the application process before knowing for certain whether they might be denied because another applicant within 700 feet of them gets licensed first or the Community Plan in which they are located reaches undue concentration before they obtain a license. Nevertheless, DCR understands that many applicants have been patiently awaiting the start of Phase 3 retail storefront licensing and that is important for the Department to timely accept and process those applications.

In addition to moving forward with Phase 3 retail licensing as efficiently as possible, it is critically important that the City ensure that the Social Equity Program (SEP), which is an integral component of Phase 3, is fully-established **before** most of the opportunities to participate in the storefront retail licensing process are gone. When the City Council passed the SEP in December 2017, it recognized that simply giving Tier 1 and Tier 2 applicants priority processing was not enough, as many of those applicants, by definition, have been disproportionately excluded from the economic and professional resources that are essential to navigating a licensing process and launching a successful business. As such, the City Council provided that Tier 1 and Tier 2 applicants shall receive business, licensing and compliance (BLC) support to make participation in the SEP much more accessible by reducing the significant and well-documented barriers associated with licensing and operating a compliant cannabis business.

DCR has been working diligently over the last year to develop BLC programming, but as with any new and innovative program, development takes time. Currently, DCR is finalizing a draft Request for Proposals (RFP) to identify vendors who can provide a suite of BLC support to Tier 1 and Tier 2 applicants and it expects that these support services will be available to applicants no earlier than July 2019. Many stakeholders have shared with DCR their concerns that if storefront retail licensing begins in the Spring 2019, many Tier 1 and Tier 2 applicants who are depending on BLC support that is not yet available will completely miss the opportunity to even apply for a license because all of the City's Community Plans will have reached undue concentration well before they are ready to apply. Based on the number of EMMDs currently

pursuing annual storefront retail licenses, DCR expects approximately 200 storefront retail licenses will be available through Phase 3 before undue concentration is reached in most or all of the City's Community Plans.

B. Proposed Options for Phase 3 Retail Storefront Licensing

DCR believes that there is a solution that balances both the interest of starting an efficient storefront retail licensing process this Spring and ensuring opportunities remain for Tier 1 and Tier 2 applicants who need additional time and support to participate. With the expected 200 additional retail license opportunities in mind, DCR proposes a bifurcated storefront retailing licensing process as follows:

- Spring 2019 Processing: DCR accepts applications in Spring 2019 with the aim of licensing 100 storefront retailers and processes applications according to one of the proposed methods described below; **AND**,
- Merit-based system: The City Council, with the input of DCR, the Cannabis Regulation Commission, and stakeholders, develops a merit-based system for selecting 100 storefront retail licensing applicants. DCR estimates it may take a minimum of nine months before any applicants can be selected to apply for an annual license through a merit-based system.

1. Possible Processing Methods for Spring 2019

DCR proposes two possible methods for processing applications beginning in Spring 2019. **Both methods** would include a pre-application verification process whereby DCR, for a limited period of time, will verify an applicant as Tier 1 or Tier 2 if it provides documentation that demonstrates that it has an individual owner who meets the qualifications to be a Tier 1 or Tier 2 applicant. After DCR closes the verification window, it could accept and process applications **from the verified Tier 1 or Tier 2 applicants** according to one of the following two methods:

- i. First come, first served for verified Tier 1 and Tier 2 applicants

Currently, the regulations call for DCR to accept applications on a first come, first served basis. However, before DCR can determine whether an applicant receives priority over another applicant in a conflict over the 700-foot retailer buffer, it must deem the application complete, meaning DCR has reviewed the applicant's full annual license application, including reviewing and approving all of the applicant's operation plans. Additionally, the regulations do not provide a rule for determining the priority among applicants for undue concentration purposes. In short, both DCR and applicants will have to expend significant time and resources before it is certain which applicants get priority to apply for the limited number of licenses available.

The inefficiencies in the current first come, first served method could be greatly improved by determining applicants' priority for location conflicts earlier in the application process. Specifically, DCR will deem an application preliminarily complete once a verified Tier 1 or Tier 2 applicant has submitted the following:

- A letter of intent, lease agreement, or property deed at an address in the City, and a landowner authorization, if applicable;

- A complete premises diagram;
- A dated radius map, including horizontal lines and labeling of any sensitive uses applicable to storefront retailers; and
- A complete ownership and financial interest holder disclosure form.

Upon submission, DCR will provide an applicant a date and time stamp that will be effective to resolve any location conflicts described below. If an applicant submits an application without complete and sufficient versions of the documents above, DCR will provide the applicant 10 business days to cure the deficiency; otherwise its original date and time stamp will no longer be effective. An applicant deemed preliminarily complete will be eligible for full annual license processing unless its location is (i) within a 700-foot radius of an earlier-in-time applicant with a preliminarily complete application or (ii) in a Community Plan that will exceed undue concentration limits due to other earlier-in-time applicants with a preliminarily complete application.

DCR will continue to process applications until it has identified the 100 first-in-time applicants with preliminarily complete applications who have viable locations. An application deemed preliminarily complete that cannot be processed due solely to undue concentration limits may ultimately be eligible for full annual license processing if the City Council finds that approval of the license would serve public convenience or necessity.

ii. Lottery for verified Tier 1 and Tier 2 applicants

After DCR closes the verification window for Tier 1 and Tier 2 applicants, **each verified applicant will be allowed to register only one location** for a lottery drawing. Through a lottery drawing, each verified Tier 1 and Tier 2 applicant will receive a processing number. Applicants with processing numbers 1 through 100 will be part of the processing group. DCR will then resolve any 700-foot retailer buffer and undue concentration conflicts among applicants in the processing group in favor of the applicant with the earlier processing number. Applicants in the processing group on the losing end of conflicts will have an opportunity to select another location. Applicants who are not in the processing group will be placed on a waitlist and they will replace any applicants who are ultimately denied a license.

2. Processing Restrictions

The following restrictions would apply to the first come, first served and lottery methods of processing:

- A verified Tier 1 or Tier 2 applicant may only be associated with one application and may only apply at one address.
- The same address may not be associated with more than one verified Tier 1 or Tier 2 applicant. If two applicants produce a letter of intent from a landowner at the same address, then an executed lease agreement will be required before one of the applicants can move forward.
- The individual owner who allowed the applicant to be verified as Tier 1 or Tier 2 applicant must remain on the application with the requisite Equity Share during the

entirety of licensing process; that individual owner may not sell or transfer his or her place in the application.

- The applicant cannot re-locate its application at any point during the licensing process.

3. Stakeholder Input

DCR has begun soliciting input on the above-proposals from a varied group of stakeholders. Below is a summary of the input received thus far:

- Stakeholders are largely in favor of a merit-based system as they feel it will allow the City to select applicants who will be good operators and provide greater access to Social Equity Applicants. Some stakeholders are concerned that a merit-based system will favor applicants who can afford to pay attorneys and consultants to prepare their applications and that selected applicants will not ultimately follow through on promises made in their applications. Lastly, many stakeholders are concerned about the amount of time it will take to develop and implement a merit-based system.
- Stakeholders largely have concerns about a lottery system, with many feeling that it will result in the selection of applicants who are not prepared to succeed in the licensing process or who will not be good operators. Many stakeholders also feel that applicants will try to game the lottery to increase their odds.
- Stakeholders have concerns about the first come, first served system being vulnerable to technical glitches that prevent an applicant from timely submitting an application on Accela.
- Some stakeholders feel that applicants that already invested in properties or made other significant investments in preparation for their application should receive some form of priority when DCR processes applications in Phase 3.

C. Additional Recommended Amendments

1. Delivery Non-Storefront Retail (Delivery) Pilot Program

By the Spring 2019, DCR expects that its application processing capacity will only be large enough to handle a limited number of delivery applications. As such, DCR proposes a delivery pilot program in which it will process 40 Tier 1 or Tier 2 applications and 20 non-social equity applications (to adhere to the 2:1 ratio). DCR recommends processing Tier 1 and Tier 2 applications through the lottery or first come, first served method described above, and non-social equity applications in the first come, first served method, and further recommends that an applicant shall not be eligible to apply in the pilot program if any of its owners are owners of (i) a Phase 1 applicant with Temporary Approval, (ii) a Phase 2 applicant or (iii) have applied or will apply for a storefront retail license in Phase 3.

2. Clarify and Relax Ownership Limits on Storefront Retail Licenses

The Cannabis Procedures ordinance provides that an applicant may hold a maximum of three storefront retail licenses. DCR understands the City Council intended to prevent any one individual or company from holding too large a portion of the storefront retail licenses; however,

given the broad definition of “Owner” used in the Cannabis Procedures ordinance, DCR finds that the current ownership limit would unduly restrict individuals and management companies from participating in the management of storefront retailers. As such, DCR recommends that a person shall only be deemed to “hold” a storefront retail license if the person has an aggregate 20% ownership or profit-sharing interest in the licensee. If a person manages a storefront retailer, but does not “hold” the license, then the person shall only be subject to management company restrictions set forth in LAMC Sec. 104.21(g).

DCR also recommends changing the storefront retail license limit from 3 to 12 when a person holds no more than a 49% ownership or profit-sharing interest in a Tier 1 storefront retailer. Given the costs associated with successfully starting and operating a storefront retailer, it is important that Tier 1 applicants are not unduly restricted in partnering with willing investors because those investors are also supporting other Tier 1 applicants.

3. Allow DCR to Grant Temporary Approval to Phase 3 Storefront Retailers

If DCR determines that a Phase 3 storefront retailer applicant meets all the requirements for a license and passes a pre-license inspection, it can only recommend that the Cannabis Regulation Commission issue a license. Given the public notice period requirements and the Commission’s expected heavy licensing workload, an applicant may have to wait several months after DCR makes its recommendation before the Commission decides whether to issue the annual license. DCR finds it is important that the Phase 3 retailer applicants, who at this point will be exclusively Tier 1 and Tier 2 applicants, be given the opportunity to operate during the period of time they are awaiting Commission action on DCR’s licensing recommendation. Therefore, DCR recommends that the City Council allow DCR to grant a Phase 3 retailer applicant Temporary Approval upon making a licensing recommendation to the Commission.

4. Set Uniform Qualifications for Tier 1 and Tier 2 Applicants

In addition to different Equity Share requirements, Tier 1 and Tier 2 applicants have different qualification requirements. To qualify as a Tier 1 applicant, an individual must be Low Income and (i) have a California Cannabis Arrest or Conviction or (ii) have resided in a Disproportionately Impacted Area for at least 5 years. To qualify as a Tier 2 applicant, an individual must be (i) low income and have resided in a Disproportionately Impacted Area for at least 5 years or (ii) have resided in a Disproportionately Impacted Area for at least 10 years. These differing requirements limit individuals’ options for participating in the program, cause confusion among applicants, and create application processing inefficiencies for DCR. DCR therefore recommends that the qualification requirements, besides Equity Shares, be made uniform such that an individual qualifies as either a Tier 1 or Tier 2 applicant if the individual:

- (i) is Low Income and has a California Cannabis Arrest or Conviction;
- (ii) is Low Income and has resided in a Disproportionately Impacted Area for at least 5 years; or
- (iii) has resided in a Disproportionately Impacted Area for at least 10 years

5. Modify Calculation of Tier 3 Property Support Fee

In November 2018, City Council established a Property Support Fee to provide Tier 3 applicant an alternative to providing property to a Tier 1 applicant. On DCR's recommendation, City Council directed that the fee be the highest of the three calculations specified in LAMC Sec. 104.20(e)(1). After further consideration, DCR has found that the method of calculation specified in paragraph ii of LAMC Sec. 104.20(e)(1) (a calculation based on the rental rates paid by other licensed commercial cannabis areas within a certain vicinity) will be unduly burdensome on the Department's resources and therefore should be removed.

6. Remove "Program Site Specific Conditions" from the SEP

The SEP provides that all Tier 1, Tier 2 and Tier 3 applicants shall receive "program site specific conditions." DCR has considered how to provide such conditions but has concluded that it is not feasible do so at this time for several reasons. First, all licensees, including successful Social Equity Applicants, will have to abide by an extensive set of state regulations that cover every aspect of their day-to-day operations and which the City cannot authorize them to disregard; as such, it will be difficult to develop meaningful site specific conditions within the confines of the state regulations. Second, DCR expects to license hundreds of Social Equity Applicants and developing meaningful site specific conditions for each applicant in a fair and consistent manner will consume significant amounts of time that should be devoted to more pressing licensing and compliance matters.

7. Eliminate Tier 2 Obligation to Provide Business, Licensing and Compliance Support

Tier 2 applicants are required to provide BLC support to Tier 1 applicants. However, Tier 2 applicants themselves are entitled to receive BLC support from Tier 3 applicants. In effect, this requires a Tier 2 applicant to transfer some of the BLC support it receives from a Tier 3 applicant to a Tier 1 applicant, which is also receiving BLC support from a Tier 3. DCR believes a more efficient process would simply be to have a Tier 2 applicant receive a lesser amount of BLC support than a Tier 1 applicant receives.

8. Require Tier 3 Applicants with Temporary Approval to Enter into Social Equity Agreement at Time of Submitting an Annual License Application

A Tier 3 applicant is required to enter into a Social Equity Agreement with the City to provide support and assistance to Tier 1 and Tier 2 applicant as a condition of receiving a license. However, the SEP does not specify when exactly the Tier 3 applicant must enter into the agreement and when it must start providing the support and assistance. DCR recommends that the City Council amend the SEP to require a Tier 3 applicant with Temporary Approval to enter into a Social Equity Agreement at the time it submits an annual license application.

9. Issue Non-storefront Retail Licenses in the Manner Provided in LAMC Sec. 104.06(b)

LAMC Sec. 104.06(a) provides that the Cannabis Regulation Commission must approve the issuance of any retail license. DCR understands City Council's intent behind this provision

was to ensure an opportunity for communities to participate in a public hearing process only before the City licenses storefront retailers, which will have the most visible presence of any type of commercial cannabis business. However, the definition of “retail” in the Cannabis Procedures ordinance includes non-storefront retail activity. Therefore, DCR recommends City Council clarify its intent by specifying that DCR may make licensing decisions for non-storefront retail applications in the same manner as provided in LAMC Sec. 104.06(b). Relatedly, DCR recommends that the City Council no longer require DCR to hold a community meeting as required under LAMC Sec. 104.04 for non-storefront retail license applicants.

10. Miscellaneous Recommended Amendments

DCR further recommends the following amendments to the Cannabis Procedures ordinance and regulations:

- Clarify that DCR may require an applicant to submit additional information or documents after DCR deems an application complete as necessary to make a licensing decision.
- Remove the requirement in Regulation No. 10 D. 4. that a retailer store all cannabis goods in a vault or safe during non-retail hours.
- Revise Regulation No. 7 so that it provides that DCR shall process applications for licenses in a manner consistent with LAMC Section 104 and these Rules and Regulations.
- Make the City’s delivery regulations concerning the maximum value of goods delivered and delivery request receipts consistent with state regulations.
- Allow DCR to enter into Social Equity Agreements with Tier 3 applicants without Commission approval.
- Allow non-retail and non-storefront retail business premises to have exterior mounted devices like security bars, barbed-wire, etc.

D. Recommendation

It is recommended that the City Council:

1. Request the Department of Cannabis Regulation to report back within 45 days with a proposal both for a merit-based storefront retail licensing system and additional programming to further address the disproportionate harms experienced by individuals and communities due to past cannabis criminalization and the war on drugs after considering the input and recommendations of the Cannabis Regulation Commission and members of the public.
2. Request the City Attorney, with the assistance of the Department of Cannabis Regulation, to prepare and present an ordinance to amend Section 104 of Article 4 of Chapter X of the Los Angeles Municipal Code and the Rules and Regulations as necessary to:
 - a. Implement either the lottery or revised first come, first served storefront retail licensing method described in this report for Phase 3 storefront retail licensing.
 - b. Implement a Delivery Pilot Program as described in this report using either the first come, first served or lottery method for Tier 1 and Tier 2 applicants, and first come, first served for non-social equity applicants.

- c. Clarify that a person “holds” a retail storefront license when it has a 20% ownership or profit-sharing interest in the licensee, and allow a person to manage a retail storefront license within the limits specified in LAMC Sec. 104.21(g).
- d. Allow a person to hold no more than a 49% ownership or profit-sharing interest in 12 Tier 1 storefront retail licenses.
- e. Allow DCR to grant Temporary Approval to a Phase 3 storefront retail license applicant after DCR recommends that the Commission issue the applicant a license.
- f. Create uniform qualification requirements, other than Equity Shares, for Tier 1 and Tier 2 applicants.
- g. Remove paragraph ii of LAMC Sec. 104.20(e)(1) as a method of calculation for the Property Support Fee.
- h. Remove “Program Site Specific Conditions” from the SEP.
- i. Eliminate a Tier 2 applicant’s obligation to provide business, licensing, and compliance support to a Tier 1 applicant.
- j. Require Tier 3 applicants with Temporary Approval to enter into a Social Equity Agreement at the time of submitting an annual license application.
- k. Allow DCR to issue non-storefront retail licenses in the manner provided in LAMC Sec. 104.06(b) and exempt non-storefront retail license applicants from the community meeting requirement in LAMC Sec. 104.04.
- l. Clarify that DCR may require an applicant to submit additional information or documents after DCR deems an application complete as necessary to make a licensing decision.
- m. Remove the requirement in Regulation No. 10 D. 4. that a retailer store all cannabis goods in a vault or safe during non-retail hours.
- n. Revise Regulation No. 7 to provide that DCR shall process applications for licenses in a manner consistent with LAMC Section 104 and these Rules and Regulations.
- o. Conform the City’s delivery regulations concerning the maximum value of goods delivered and delivery request receipts with state regulations.
- p. Allow DCR to enter into Social Equity Agreements with a Tier 3 applicant without Commission approval.
- q. Allow non-retail and non-storefront retail business premises to have exterior mounted devices like security bars.

Sincerely,



CAT PACKER
Executive Director & General Manager
Department of Cannabis Regulation