



CALIFORNIA STRATEGIES, LLC

May 15, 2018

City of Goleta
City Council
130 Cremona Drive, Suite B
Goleta, California 93117

Re: Item F.1 Cannabis Business Tax Methodology and Consideration of a Draft Ordinance

Honorable Mayor and Councilmembers,

We represent several existing and prospective cannabis operators who are highly interested to locate their businesses in the City of Goleta, including non-storefront retail (delivery), manufacturing (both extraction and packaging), distribution and testing labs – all critical components of the cannabis supply chain. These are experienced operators that are compliance-driven.

Our clients have begun searching and securing property, but have indicated they will abandon their efforts to locate in the City of Goleta should the tax rate as proposed be adopted by your Council. These operators will employ hundreds of living wage employees and are planning to recruit from the local workforce. In addition, they are planning to use local contractors and vendors for millions of dollars of capital investment in various facilities.

We do not support the staff's recommended tax rates and are concerned that these taxes will not attract experienced and compliance-driven operators to Goleta. Alternatively, we recommend that your Council direct staff to return with the following amended tax rates – indicated in red - for a ballot measure in November 2018:

1.5%	Nursery
3% 4%	Cultivation
6%	Retail
3%	Non-Storefront Retail, Delivery only
2.5% 0%	Distribution
3.5% 0%	Manufacturing
1%0%	Testing Labs

We support limited taxing of the local cannabis industry, but caution the City to tax each commercial activity appropriately, as each component of the supply chain is different. **We recommend decreasing the tax on manufacturing, distribution and testing labs to 0%. We also suggest the Council set a tax rate specifically for Non-Storefront Retail (Delivery only) of 3% gross receipts.**

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Non-Storefront Retail, Delivery Only: Non-storefront retail/delivery is a completely different business model than traditional dispensaries, which have a storefront component. Therefore, it is appropriate to set a different tax rate for non-storefront retail/delivery-only activities. Non-storefront retail license type is similar to any other delivery fulfillment center, such as an Amazon fulfillment center. Since an increasing number of consumers are requesting products delivered to their doorstep, it would be strategic for the City to encourage delivery services to invest in Goleta.

Manufacturing: Staff has proposed 3.5% gross receipts tax rate for manufacturing. This is far too high and inconsistent with other jurisdictions that have either not taxed manufacturing, or implemented a rate of 1-2%. For example, the City of Santa Rosa taxes manufacturing at 1% gross receipts. In comparison to other license types, manufacturing requires some of the most expensive equipment, safety controls, build-out and third party specialist certifications. Manufacturing may also be one of the most rapidly growing commercial activities, as consumers are increasingly demanding extracted products such as soft gels, oils, tinctures and lotions. It would be short sighted to tax manufacturing at 3.5% gross receipts, which will not allow these businesses to be sustainable long-term.

Distribution: The proposed \$2.5% tax rate on distribution is also higher than many jurisdictions. We encourage the City to adopt a tax rate that will encourage compliant distributors to locate in Goleta because this is a low impact commercial activity. Distribution licensees play a critical role in the new supply chain by not only transporting product, but also conducting quality assurance and quality control. For example the distributor coordinates with a compliance testing lab to pull random samples of product for testing. The product cannot be transported until it passes testing. The distributor also verifies that the product is properly packed and labeled - ensuring the product is in child-proof packaging and does not exceed the THC limits per serving. As an example, the City of Santa Rosa does *not* tax distribution.

Testing Labs: Lastly, high-level testing labs will not locate in the City of Goleta if there is a tax on this activity because there are plenty of other jurisdictions that are not taxing labs. Testing lab licensees are responsible for conducting third party testing of cannabis goods and maintaining ISO/IEC 17025 accreditation. Testing will ensure that cannabis is safe for consumption, and that the consumer has accurate knowledge of the contents of the product. Labs are required to test for cannabinoids, heavy metals, microbial impurities, pesticides, residual solvents and

processing chemicals, etc. Testing labs have significant start-up costs, including specific equipment needed to meet the new standards.

The City of Goleta is uniquely positioned to support the “middle” of the cannabis supply chain in the form of delivery, manufacturing, distribution and testing labs. However, unlike retail and cultivation, it will be more difficult for these critical components of the supply chain to be successful in Goleta if they are taxed, because they operate on narrow margins.

Although a 1% or 3% gross receipts tax may seem like a small amount, even a 1% gross receipts tax is significant for local start-up businesses. The newly legalized cannabis industry is struggling to compete with the black market as they are forced to absorb the extraordinary State taxes, annual application and licensing fees, and costs of compliance. Additionally, the price per pound is decreasing and the industry is highly volatile at this pivotal point in time.

As follows are just a few examples of new industry costs:

1. State tax: \$9.25 an ounce flower; 15% excise tax on retail
2. State application & license fees: range from \$1,000-\$75,000
3. Security requirements: video surveillance, fencing and lighting
4. Track and trace software: \$10,000 - \$100,000
5. Odor control: \$30,000-\$100,000
6. Product testing \$100,000
7. Certification by industrial hygienist and certified engineers
8. Local licensing and permitting fees and taxes

In conclusion, we are confident the cannabis industry is poised to spur significant economic growth in the City of Goleta in the form of excellent jobs for local residents. We urge your Council to lower the tax rates to 0% for manufacturing, distribution and testing labs, and set a rate of 3% for non-storefront retail/delivery to facilitate a sustainable, vibrant and compliant cannabis industry.

Sincerely,

Erin Weber
California Strategies, LLC

Deborah Lopez

From: Stuart Kasdin
Sent: Tuesday, May 15, 2018 8:17 AM
To: Michelle Greene; Carmen Nichols
Cc: Deborah Lopez
Subject: FW: Public Comment Cannabis Tax

FYI

Answers below in italics

From: Stuart Kasdin <skasdin@cityofgoleta.org>
Date: Monday, May 14, 2018 at 12:29 PM
To: Erin Weber <eweber@calstrat.com>
Subject: RE: Public Comment Cannabis Tax

Hi Erin,

What is the difference between "non-storefront retail, delivery only" as opposed to "distribution"?

The key difference is that distribution cannot deliver product to the consumer – either in the form of delivery or storefront retail. Only retail (storefront or non-storefront delivery) are authorized to make a sale to the consumer. So non-storefront retail should be taxed higher than distribution (but less than storefront) because non-storefront retail can charge delivery margins.

Distribution – on the other hand – is only authorized to move product within the supply chain. For example, between the cultivator and manufacturer. Since distribution is only providing a transportation and quality assurance and quality control service, they charge fairly narrow margins. A good business model is low margin, high volume. Distributor also must have the third party testing lab pull random samples at the distribution facility and hold the product in quarantine until it passes test. Distributor also verifies packaging and labeling compliance. My letter (re-attached) also addresses each license type.

Also, what is the rationale for the different rates for cultivation vs. nursery. Seems like the same family of activity.

Many jurisdictions do not tax nursery at all because the definition of nursery is immature plants that are NOT flowering. Cultivation includes growing and harvesting of flowering plants. The value is in the flower.

Also, is there a particular rationale for 0% manufacturing aside from the idea that the industry doesn't want to pay the tax and they will all go to Lompoc?

If the City of Goleta wants to attract a compliant, and sustainable industry, we recommend taxing below the County. As you know there is a robust pre-existing cultivation industry in the County. The industry is seeking permits for the rest of the supply chain (manufacturing, distribution, testing and delivery) to prepare the flower product for market. If the City of Goleta taxes are the same as the County, it is more convenient for the existing industry to just permit the rest of their operation in the unincorporated near their cultivation sites. If the City adopts a lower tax rate than the County, we believe the industry will seek permits in Goleta. I think the industry would remain interested if the City adopted .5% or 1% manufacturing.