Government of the District of Columbia
Office of the Chief Financial Officer

Jeffrey S. DeWitt
Chief Financial Officer

MEMORANDUM

TO: **The Honorable Phil Mendelson**
Chairman, Council of the District of Columbia

FROM: **Jeffrey S. DeWitt**
Chief Financial Officer

Jeffrey S DeWitt

DATE: **October 17, 2019**

SUBJECT: **Fiscal Impact Statement – Safe Cannabis Sales Act of 2019**

REFERENCE: **Bill 23-280, as Introduced**

Please note that there is currently a federal prohibition against spending District funds in support of the legalization of non-medical marijuana. As a result, none of the costs or revenues described here may be included in a budget or financial plan at this time.

Conclusion

Funds are not sufficient in the fiscal year 2020 through fiscal year 2023 budget and financial plan to implement the bill. The bill establishes a regulatory framework and retail sales tax on marijuana for non-medical use that will generate $8.7 million in dedicated tax revenue beginning in fiscal year 2021 and $78.7 million over the four-year financial plan[1]. Beginning with the first full year of revenue collections (assumed here to be fiscal year 2021), tax revenues generated will be sufficient to cover costs of the bill. However, prior to the collection of revenue, $823,000 in funding will be needed in fiscal year 2020 for start-up implementation costs. The bill dedicates revenue not needed for administration to affordable housing programs.

Background

The bill establishes a taxation and regulatory system for marijuana and marijuana products sold for non-medical adult[2] use in the District. The Alcoholic Beverage Control Board is designated the

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[1] The District of Columbia budget is subject to the General Provisions included federal Appropriations Act. The Consolidated Appropriations Act, 2019, includes General Provision 809, which states that "[n]o funds available for obligation or expenditure by the District of Columbia government under any authority may be used to enact any law, rule, or regulation to legalize or otherwise reduce penalties associated with the possession, use, or distribution of . . . any tetrahydrocannabinols derivative for [non-medical] purposes."
[2] Adults are 21 years of age or older.

regulatory agency for marijuana (including medical marijuana) and is renamed the Alcoholic Beverage and Cannabis Board ("Board"). The bill imposes a sales tax of 17 percent on sales of marijuana and marijuana products and maintains the existing six percent sales tax on medical marijuana[3]. The Board is authorized to grant licenses to marijuana product cultivators[4], manufacturers, distributors, and retailers (including off-premises[5] and on-premises[6] retailers). The licenses will be effective for three years with the ability to renew. No more than two cultivation, manufacturer, distributor, or retailer licenses per entity are permitted. A medical dispensary license will not count toward off-premises retailer license limits. A cultivation license for medical marijuana will automatically convert to a cultivation license under the bill, which will not distinguish between medical or adult use sales. The Board may also create endorsements for other categories of marijuana businesses, such as the medical marijuana endorsement[7] and the marijuana delivery endorsement. The total number of licenses that may be issued is left to the discretion of the Board, and the Board is explicitly permitted to limit the number of licenses per Ward to prevent a high concentration of licenses in any given Ward.

All managers and employees of licensed entities must obtain either a manager's license or a worker's license from the Board before working or volunteering at a licensed facility. The bill outlines the requirements for these individual licenses, including District residency requirements[8], security plans, and background checks to be performed in conjunction with the Metropolitan Police Department (MPD). Licensees must notify the Board within one business day if a manager or worker is no longer employed. The Board must provide license orientation classes free of charge.

Within 60 days following the licensure of an independent testing facility in the District, all marijuana sold must be tested by an independent licensed testing facility. The bill requires testing of plants and manufactured products, for contaminants and potency, to be performed by licensed marijuana testing facilities operated by licensed laboratory agents. The Board will issue both facility and laboratory operator licenses, establish protocols for testing in consultation with the Department of Forensic Sciences (DFS), and set fees for registration. Testing facilities must notify the Board of any changes in authorized agents within one day.

In addition to the requirements already discussed for DFS and MPD, the bill requires coordination of several District agencies in the regulation and enforcement of non-medical marijuana, including:

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[3] Legalization of Marijuana for Medical Treatment Initiative of 1999, effective February 25, 2010 (D.C. Law 13-315; 57 DCR 3360).
[4] The bill limits an individual cultivator to possession of no more than 10,000 plants at one time.
[5] The bill requires the Board to accept off-premises applications 6 months after the effective date of the law. It limits off-premises retailers to sales of no more than one ounce of usable marijuana flower or five grams of marijuana concentrate per day. Marijuana edible serving sizes are limited to those with no more than five milligrams of Tetrahydrocannabinol. Total sales of edibles are limited to 16 ounces per day per customer. The bill sets additional limitations on sale of liquid cannabis, marijuana tincture, and e-liquid vaping.
[6] The bill requires the Board to accept on-premises license applications 24 months after the effective date of the law.
[7] If the Board approves, a licensee may sell medical marijuana and non-medical use marijuana provided a minimum of 35 percent of inventory is set aside for medical marijuana purchase.
[8] Cultivators, manufacturers, and retailers must have a partner or official who is a District resident with more than 60 percent invested interest in the entity. Those partners officially part of a facility prior to May 2019 are exempt from this requirement. Straw ownership for the sake of fulfilling ownership requirements is prohibited. Sixty percent of all employees must be District residents.

- The Department of Health (DOH) and the Fire and Emergency Management Services (FEMS) must be involved in the development of regulations on marijuana retailers;
- DOH must ensure all marijuana establishments have health inspections; DOH must ask medical professionals authorized to recommend medical marijuana whether he or she wishes to be listed on a District website as being authorized to recommend medical marijuana;
- The Department of Consumer and Regulatory Affairs (DCRA) must ensure certificates of occupancy are issued for all marijuana establishments;
- The Department of Behavioral Health (DBH) is required to develop a public education campaign on the safe use of marijuana as well as potential negative health effects;
- The Office of Tax and Revenue (OTR) is required to collect monthly data on marijuana retail sales and report on those sales figures; and
- The Department of Insurance and Securities Banking (DISB) is required to establish the DC SAFE Can License compliance verification and data portal for use by financial institutions. The online portal must include information about marijuana licenses, personnel, products, sources of supply, records of major transactions, violations, and evidence of suspicious or illegal activities. DISB is also required to review current laws and any rules that impede the use of financial services by marijuana businesses.

There are other implicit requirements that the new regulatory framework will place on District agencies. For example, the bill establishes a prohibition on marijuana advertising and product packaging, which could place a burden that does not currently exist on DCRA and DOH. As the market for marijuana matures, purveyors may introduce new products for which agencies may require extra resources to monitor and enforce.

New Funds

The bill establishes the Cannabis Sales Tax Fund which will collect all the sales tax revenue from marijuana off-premises retailers[9]. Six months following the effective date of the law all revenues not needed for program expenses will be dedicated to affordable housing programs and initiatives. The bill does not name specific housing programs.

The bill also establishes the non-lapsing Cannabis Regulation Administration Fund, which will collect all licensing and permitting fees generated by the Act. The Regulation Administration Fund will go to support the administrative expenses of the Board. The bill sets the following fees for non-medical marijuana licenses (the fees for medical marijuana licenses are set at 50 percent of the non-medical license fees):

License Fee Category	**Fee Amount**
Cultivation license fee	$10,000
Manufacturer license fee	$6,000
Retailer license fee	$6,000
Testing license fee	$5,000
Distributor license fee	$3,000

[9] This fiscal impact statement assumes that the Cannabis Sales Tax Fund will collect sales tax revenue from the non-medical sales at off-premises retailers. The bill is unclear whether medical marijuana sales at off-premises retailers with a medical marijuana endorsement should also be deposited into the Sales Tax Fund. For this estimate we have assumed that medical marijuana revenues will not go to the Sales Tax Fund.

Application fee (for cultivation, manufacturer, retail, distributor, and testing licenses)	$1,000
Transfer license ownership fee	$500
Manager's license fee	$130
Worker's license fee	$50

The bill also cuts the fee for medical marijuana cards in half and makes newly issued medical marijuana cards and cards renewed after the effective date of the act valid for two years. Currently, they must be renewed annually. This will reduce revenue derived from medical marijuana card fees, which is further discussed in the financial plan impact section below.

<u>Timelines</u>

The bill sets maximum timelines for several regulatory milestones:

- Within 30 calendar days of the effective date of the Act, the Board must allow for DOH certified medical marijuana facilities to apply for non-medical licenses;
- Within 60 days of the notification from the Board, existing medical marijuana facilities must finalize an application for a non-medical license. Within six months after the effective date of the Act, existing medical marijuana establishments are the only entities that may be considered for a non-medical license. The Board cannot issue a license however, until regulations have been issued and a seed-to-sale tracking system is in place;
- Within six months of the effective date of the Act, the Board must submit regulations and other appropriate standards[10] to the Council for approval;
- Within six months of the effective date of the Act, the medical marijuana program at DOH must be transferred to the Board, except for the Health Occupation Board's role in reviewing medical marijuana authorized practitioner recommendations;
- Within 6 months of the effective date of the Act, the Board must begin accepting applications for off-premises retailer licenses;
- Within 18 months of the effective date of the Act, the Board must issue regulations for retailers and consider allowing marijuana sale at grocery stores and farmers' markets; and
- Within 24 months of the effective date of the Act, the Board must begin accepting applications for on-premises retailer licenses.

Financial Plan Impact

Funds are not sufficient in the fiscal year 2020 through fiscal year 2023 budget and financial plan to implement the bill. The bill establishes a regulatory framework and retail sales tax on marijuana for non-medical use that will generate $8.7 million in dedicated tax revenue beginning in fiscal year 2021 and $78.7 million over the four-year financial plan. Beginning with the first full year of revenue collections (assumed here to be fiscal year 2021), tax revenues generated will be sufficient to cover the costs of the bill. However, prior to the collection of revenue, an estimated $823,000 in funding will be needed in fiscal year 2020 for start-up implementation costs.

The bill dedicates revenue not needed for administration to affordable housing programs.

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[10] For example, the bill specifically requires license premises to not also sell gasoline or have drive-through services.

Estimating Revenue from Taxes and Fees

The Office of Revenue Analysis (ORA) estimates the non-medical marijuana market demand in the District to be approximately $257.1 million of sales annually. Once the regulatory regime is established, licenses are issued, and firms establish sufficient production, total sales should reach this amount and generate approximately $43.7 million in sales tax revenues annually. The estimate assumes there are no unforeseen roadblocks in meeting the demands of the market – such as cultivation capacity – and no change in non-medical use laws in neighboring states or jurisdictions.

To calculate estimated market demand in the District, ORA looked at the per capita sales in states with the most mature non-medical markets[11]. Averaging the per capita markets in those states and applying them to the adult population and commuter population in the District yields an estimated $257 million total market.

To estimate the total license fee collections, ORA estimated total demand would be met by approximately 20 cultivation centers and 50 retailers.

Administrative Costs

The Board will incur most of the costs to regulate non-medical cannabis in the District. The Board will require licensing specialists to review and process license applications, investigators and auditors to ensure licensee compliance with regulations, specialists in public affairs and information technology, and general administrative personnel. The Board must manage a seed-to-sale tracking system to track all marijuana products cultivated and sold in the District and will need to update the Alcoholic Beverage Regulation Administration's current license processing system to issue the new categories of cannabis licenses. It is expected that the current system used by DOH for medical marijuana plant tracking will continue to be used for medical and non-medical cannabis plant tracking. The system may need some changes or updates, however, to meet the needs of the Board's non-medical program. Lastly, the Board will incur standard start-up costs associated with a new agency – equipment, office space, transcription and interpretation services, fleet and maintenance, and supplies. The estimated costs are summarized in the chart below.

At least eight other agencies have direct or associated responsibilities under the bill. DFS must work with the Board to establish testing protocols and possibly provide spot checking of testing laboratories to ensure compliance with testing standards. DBH is required to launch a public education campaign regarding cannabis use. DISB will be required to create a portal for financial institutions on cannabis related businesses; the cost of this portal is unknown.

Other agencies may incur additional workload due to the specialized nature of the licensed cannabis firms, although the precise additional burden is unclear at this time. DOH is required to make health inspections of the facilities, DCRA must provide certificates of occupancy, and FEMS will be required to review any new facilities for fire safety. Given that the production and sale of marijuana is a federal crime, sales tax revenue collections will be sent in atypical formats, most likely cash. The Office of Finance and Treasury may need additional cashiers and incur additional cash management equipment costs[12] to handle the increase in non-electronic sales tax payments. Cash deposits will also

[11] Colorado, Washington, and Oregon have the three oldest non-medical marijuana regulated markets.
[12] If all estimated sales tax revenue is deposited as cash, the Office of Finance and Treasury will require two additional cashiers (Grade 8) and new cash management equipment.

increase banking fees. (However, the extent to which non-medical marijuana licensees will need to pay in cash in the future is an open question. While most banks have avoided serving marijuana businesses, the number of banks and credit unions nationwide that are willing to provide services has been steadily increasing[13] and federal legislation is also being considered to address concerns associated with the cash volume of cannabis businesses.) Based on the experience of other states, it is expected that there will be a need for interagency coordination, adding to the workload of associated agencies. ORA has added to the expected administrative costs of the bill to account for this interagency effect.

Lastly, the bill requires the transfer of existing resources related to medical marijuana facilities oversight from DOH to the Board. DOH will retain the role of patient certification for medical marijuana licenses. A Council/Mayor budgetary action – and perhaps accompanying legislative language – will be needed to transfer DOH medical program funding to the Board.[14] The transfer is not included in the cost cart below.

[13] See Marijuana Banking Update by the Federal Crimes Enforcement Network which shows an increase in the number of banks working with marijuana businesses increased from 300 to 438 banks in 2018. (https://www.fincen.gov/sites/default/files/shared/Marijuana_Banking_Update_Public_Dec_2018.pdf)

[14] The DOH program is supported with fee revenue in the Department of Health O-Type revenue fund 0641 - Other medical license fees.

Fiscal Impact of Safe Cannabis Sales Act of 2019[(a)(b)] Fiscal Year 2020– Fiscal Year 2023 ($ thousands)					
	FY 2020	**FY 2021**	**FY 2022**	**FY 2023**	**Total**
REVENUE					
Sales Tax Revenue into Cannabis Sales Tax Fund[(c)]	$0	$8,743	$26,230	$43,716	$78,689
License Fees into the Cannabis Regulation Administration Fund	$158	$419	$589	$782	$1,948
Reduction in Medical Marijuana Card Fees and extending card validity to two years [(d)(e)]	($171)	($348)	($355)	($362)	($1,236)
CHANGE IN REVENUE	**($13)**	**$8,814**	**$26,464**	**$43,136**	**$79,400**
EXPENSES					
ABCA Personal Services Costs[(f)]	$150	$1,749	$2,041	$2,389	$6,329
ABCA Non-Personal Services Costs	$380	$1,106	$1,139	$1,173	$3,799
Estimated additional costs at other agencies[(g)]	$30	$367	$385	$405	$1,188
Public Education Campaign	$250	$100	$50	$25	$425
TOTAL EXPENSES	**$810**	**$3,323**	**$3,616**	**$3,992**	**$11,740**
NET FISCAL IMPACT	**($823)**	**$5,491**	**$22,848**	**$40,143**	**$67,659**

Table Notes

(a) Due to uncertainty as to when the bill will become law, and the time required to grow cannabis plants, this table assumes no sales will occur in fiscal year 2020. However, this may be revisited as the bill moves forward.

(b) Because it is expected the law will not be effective until mid-fiscal year 2020 at the earliest, and because only existing medical cannabis operators will be able to request retail licenses in the first six months, ABRA indicates it can absorb some of the costs of starting operations within current resources. Expenses ABRA can absorb in fiscal year 2020 include: writing regulations, developing application processes, and managing the transfer of the medical program from DOH to the Board. However, in fiscal year 2020, the Board will need to hire a Customer Service Representative to manage public contact and phone calls, a License Specialist to review applications and conduct background checks, and a Senior Manager to begin to plan and oversee the program. The Board will also need non-personal services funding to establish the office, build-out space, pay for "audit" type testing of products, and make updates to its licensing system.

(c) The bill dedicates all marijuana sales tax revenue to program expenses and affordable housing programs.

(d) Fees will be reduced in the Department of Health O-Type revenue fund 0641 - Other medical license fees, which supports the medical marijuana program.

(f) Alcoholic Beverage and Cannabis Administration will require an estimated 20 FTEs beginning in fiscal year 2021, and 3 FTEs for part of fiscal year 2020.

(g) With the establishment of a new legal cannabis market, we expect additional agencies (including OTR, DFS, DCRA, DISB, and DOH) will incur administrative costs related to cannabis regulation. The precise allocation is not known at this stage.