



# Memorandum

**TO:** HONORABLE MAYOR AND  
CITY COUNCIL

**FROM:** Councilmember  
Donald Rocha

**SUBJECT:** MEDICAL MARIJUANA

**DATE:** April 17, 2015

Approved

Date

4/17/15

I would like to thank the Mayor and City Staff for their past and current leadership and dedication to this complex topic. San José has become a pioneer with its attempt to regulate the medical marijuana industry. Potentially other municipalities, not only within the State of California, but across our nation, could draw upon our knowledge and experience pertaining to our work in this arena.

As we advance in this process, it is unfortunate that those businesses who are not working towards full compliance garner the most attention, while there are many business owners within the industry, who appear to be working diligently to become fully compliant and are willing to follow the letter of the law. However, as we finalize the amendments to both Title 6 and Title 20, there are potential issues on the table that we must consider as we transition, and ultimately move towards complete implementation.

## RECOMMENDATION

Please see the attached letters from stakeholders and industry representatives within the medical marijuana industry, voicing some questions and concerns as they strive to fulfill our requirements. It is from these concerns and conversations with stakeholders that I have identified the below items which may warrant: additional analysis from staff, or possible future Council policy direction, and/or clarification on our expectations for compliance:

- 1.) Allow approval of Title 6 compliance extension of up to nine months from Title 20 approval for any collectives that already has Title 20 approval and has shown a good faith effort to comply with Title 6.
  - Case studies suggest that multiple businesses have invested significant funds into creating a business in San José and have made a good faith effort to comply with the City's deadlines, may need additional time to complete tenant improvements or new construction.

- 2.) Allow Staff the discretion to allow a business with Title 20 approval already, to have up to nine months from building permit to grow product and become fully operational.
  - In the instance of a collective that is new to San José, there may be a need to enable a phase in of operations while growing occurs in order to have enough product to serve patients. Even established Collectives may have difficulty growing the product within this timeframe.
- 3.) Consider allowing legal collectives with Title 20 and Title 6 approval to exchange product (still within a closed loop) from any legal collective in San José or any vendor or collective in California deemed legal by the municipality within which the manufacturer or grower is regulated.
  - We have been told it is not physically possible in any of the facilities in San José to grow and/or manufacture all of the product.
  - Are there currently Board of Pharmacy and DEA guidelines in place for the regulation of transfer of pharmaceuticals which could potentially be replicated for any concerns we could have with product transfer?
- 4.) Ability for edibles and concentrates to be manufactured at offsite cultivation
  - Just as cultivation is allowed on-site or at an off-site location, the manufacturer of edibles and concentrates could also be allowed as long as they are at either the collective or cultivation site. The fundamental issue here is not about location but about a closed loop system with the ability for adequate oversight. If a cultivation site can be off-site or in a contiguous neighboring county it seems possible that edibles and concentrates could be treated the same way. Adoption of this could solve some of the reported landlord issues that are arising because of larger space requirements brought on by manufacture of edibles & concentrates.
  - It has been reported by the industry that approximately 50% of all industry sales are for edibles and concentrates.
- 5.) Consider allowing legal collectives with Title 20 and Title 6 approval to continue to acquire product from patient vendors.
  - It has been brought to my attention that given our current regulations, it may be difficult for the facilities in San José to grow and/or manufacture all of the product.
- 6.) Those within the industry are interested in clarification and possible changes to the current audit requirements. These should be clear, and should be developed in a manner that allows a reasonable amount of time to secure an audit and allow for the type of audit that is complete and transparent.
  - Currently, the City requires audited financials by February 15<sup>th</sup>. I have been told February 15<sup>th</sup> is a difficult turnaround time for an audited financial statement.

- It has been reported that the auditing industry has had issues providing auditing services to this industry.

7.) Ability to carry-over inventory beyond Title 6 deadline.

- According to industry representatives, a collective needs the ability to sell prior purchased stock, or take delivery of prior purchased stock and sell/transfer it. This is vital because a cultivation once permitted, will take no less than 5-6 months to produce, and the Collectives shelves could be bare. Moreover, if this is not allowed then it is assumed that collectives could have to destroy all inventories on hand at the time of Title 6 approval.

## **CONCLUSION**

I would like to be clear about the above suggestions that I have offered for further additional consideration from my colleagues, the recommendations are simply intended for clarification, or potential future action should it be necessary or warranted. Should my colleagues on the Council, or staff, think any items listed is not a prudent policy direction, nor warrant additional staff time, I am very open to modifying or eliminating any of the above. My only intent is to provide a clear and effective policy around our regulation of the medical marijuana industry in our City. This is why I am trying not to be overly prescriptive, and would prefer to have our professional staff provide some direction and comments on how best to proceed and on what timeline, recognizing this is simply a study session and not a meeting intended for direct action.

April 15, 2015

City of San Jose  
Honorable Council Members  
200 E Santa Clara Street  
San Jose, CA

**RE: Issues regarding Title 20 and Title 6 implementation for discussion**

Dear Council Member:

In their memorandum of December 12, 2014, Council Members Herrera and Khamis called for a study session that would allow the Council, in particular the new Council Members, to “get up to speed on the nuances” of the City Program and State and Federal framework regarding medical cannabis.

No discussion regarding the formation of this brand new industry and its regulatory model would be accurate if does not include commendation for City Staff from The Managers Office, Planning & Building Department, Code Enforcement and Police Department in doing a fine job in attempting to create something out of nothing with minimal guidelines and little prior precedent in the way of sensible and robust regulation. This said, we must, however, address some concerns moving forward that we hope will be explored at the April 20, 2015 Council Study Session, they are as follows:

**1) Extension for Title 6 approval with the existing collective staying open (6 months - 12/31/2015)**

The need for an extension exists because of a number of factors. City related - delays in planning & building due to the fact that this has never been done before and a new process is being created - this is not an accusation but rather a technical point that anything that has not been done before takes some time to sort out. Landlord and property related delays (as listed below). Delays by Collectives - who have never interacted with City Hall underestimating the time and expense involved in permitting and finally a major problem of siting a cultivation, manufacturing of edible & extract facility especially since Santa Cruz County banned commercial cultivation and Santa Clara County is moving in that direction.

A valid Staff concern is with inattentive collectives that have done nothing beyond Title 20 and squandered approximately 9 months to the date by doing nothing toward title 6 compliance - an extension should be granted only to those Collectives that have been granted a Title 20 Zoning Certificate **and** achieved "substantial progress" in securing their Title 6 Operational Approval. "Substantial Progress" should be defined as a collective that has at a minimum filed for a planning permit, site development permit or the like or filed for building permits in an effort toward title 6 compliance (this will need some tightening of verbiage).

During this extension period a collective will be allowed to continue its operations at its existing location until Title 6 approval is granted and then the current location must close, since the ordinance does not allow for more than one location per Collective. If the collectives are closed during the extension period the black market will flourish as well as the illegal collectives that exist now that never paid taxes or bothered to file for a Title 20 Zoning Certificate or Title 6 operational certification. In addition, we have no doubt new collectives will sprout up to accommodate the \$60+ million dollar monthly San Jose market demand that is currently being met. Finally, if the Collectives are forced into closure the City will lose significant tax revenue and hundreds of employees be out of work.

**2) Some form of excessive rent gouging restrictions imposed on landlords**

Excessive rent or profiteering already exists for some housing and business in San Jose, so it is not a new concept. What is needed is a regulation similar to what exists in California Gaming where landlords cannot participate in gaming revenue thru rent and in this instance Medical Marijuana Revenue by virtue of a percentage rent or one based on a percentage or excessive rent above and beyond the market. In

California Gaming it was designed to keep Organized Crime out of Gaming through unreasonable leases. It should be the same for Medical Marijuana - which we definitely want out of the hands of the cartels and organized crime. The problem stems from the highly restrictive zoning restrictions where a collective can be located in San Jose. In some cases the gouging is so egregious that landlords are charging up to 6x's the market rent. When this occurs in the gasoline market there is a public outcry and a legal inquiry is almost a certainty. After a natural disaster price gouging is a criminal act so why should it not be treated to the similar degree when it comes to inhibiting Non-profit organizations from fulfilling the mandate under State Proposition 215.

**3) Ability for edibles & concentrates to be manufactured at offsite cultivation**

Just as cultivation is allowed on-site or at an off-site location so should manufacture of edibles and concentrates so long as they are at either the collective or cultivation site. The fundamental issue here is not about location but about a closed loop system with the ability for adequate oversight. If a cultivation site can be off-site or in a contiguous neighboring county it seems logical that edibles and concentrates should be treated the same way. Adoption of this will solve some of the landlord issues that are arising because of larger space requirements brought on by manufacture of edibles & concentrates.

**4) Ability to carry-over inventory beyond Title 6 deadline**

A collective needs the ability to sell prior purchased stock or take delivery of prior purchased stock and sell/transfer it. This is vital because a cultivation once permitted will take no less than 5-6 months to produce product and the Collectives shelves will be bare unless this is allowed. Moreover, if this is not allowed then it is assumed that collectives will have to destroy all inventories on hand at the time of Title 6 approval and this would be financially devastating to the Collectives. Finally, if there is no such transition period or carry-over period in the immediate 6 month period after Title 6 then the Black Market will pick up the shortfall through illegal sales.

**5) Allow for a collective to collective membership arrangement or a Colorado like outside vendor model for sourcing product**

Patients need a diversity of product (just as Aspirin is not Tylenol is not Ibuprophen is not Vicadin is not Oxycodon, you get the picture) and this cannot be achieved with a single cultivation site. Indeed several strains of Marijuana can be grown at a location but not nearly the variety that patients require or Collectives currently stock. In the absence of allowing multiple cultivation sites for each Collective in San Jose there needs to be a model that allows for one Collective to trade/sell its surplus with another which should not be a problem in a closed loop system (because Staff can track who grew what and where the excess went). This also keeps San Jose from forcing more and more home marijuana farmers in trying to supply their medical need - nobody wants to see a proliferation of backyard farms popping up that lack the oversight, taxation, quality control and crime risk throughout San Jose or for the Black Market to exploit this gap in product supply. If this is not agreeable then a Collective should be allowed to obtain product from outside vendors similar to Colorado.

Thank you for your consideration.

Sincerely,

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15 April 2015

Angelique Gaeta  
City Manager's Office  
City of San Jose  
333 East Santa Clara Street  
San Jose, CA 95113

Dear Angelique,

I very much appreciate your time on the medical cannabis issue. On behalf of my clients I wanted to thank you for your focus and patience implementing the Council direction of last year. I hope that the two case studies that we provided have been helpful to show how some collectives have been aggressively pursuing Title 20 and Title 6 compliance and still may find it difficult to meet the July 17<sup>th</sup> deadline. It is unfortunate that you have been unavailable to schedule a phone call in the weeks leading up to the Council Study Session on this topic so that we can discuss the issues the industry is having with compliance. My clients agree wholeheartedly with your statement that the goal now is "to make the program work" and are committed to assist in anyway possible. In that light, I am writing to suggest some ways that San Jose might consider future amendments to the ordinance to allow for more efficient business operations and sales that will not only help the legal operators thrive, but will position San Jose to increase tax revenue received today and capture the maximum market share if cannabis is legalized by the voters of California in 2016.

We would hope that some of these issues might be brought to light in the Study Session with the Council in April so that the Council is informed of how implementation is going. Below is a list of potential amendments for consideration and brief background statements attached to each potential amendment. The potential ordinance amendments are in **bold**, and background in *italics*:

1. **Give staff the discretion to approve Title 6 compliance up to 1 year from Title 20 approval for any business that already has Title 20 approval and has shown a good faith effort to comply.**
  - *Case Studies show that multiple businesses that have invested millions of dollars into creating a business in San Jose and have made a good faith effort to comply with our deadlines will need additional time to complete construction.*

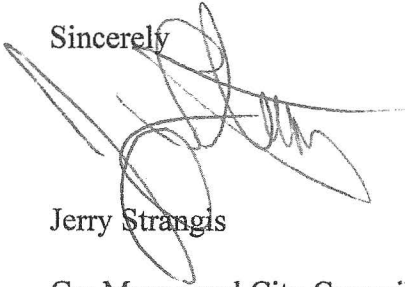
- *Many of the buildings located within the areas of the City where collectives are legal are old manufacturing and industrial buildings which need substantial renovation to meet current codes and market needs. In at least one case, the old building must be demolished and rebuilt. Also, in several cases the building had be purchased, and commercial sale transactions are often more complex and lengthy.*
- 2. Give staff the discretion to allow a business with Title 20 approval already to have up to 6 months from building permit COO to grow product and become fully operational.**
- *In the instance of a collective that is new to San Jose there is a need to enable a phase in of operations while growing occurs to have enough product to serve patients. Even established Collectives will have difficulty getting grows going in this time.*
- 3. Allow legal collectives with Title 20 and Title 6 approval to exchange product (still within a closed loop) from any legal collective in San Jose or any vendor or collective in California deemed legal by the municipality within which the manufacturer or grower is regulated.**
- *It is not physically possible in any of the facilities in San Jose to grow and/or manufacture all of the product, which are currently available to San Jose Residents.*
  - *Many popular products are proprietary and could not be manufactured in San Jose legally. San Francisco and Oakland allow collectives to acquire product without growing or manufacturing on site AND those jurisdictions allow collectives to provide delivery services. San Jose residents could drive to San Francisco or Oakland or simply order delivery of products that would be illegal to buy in San Jose under the current ordinance putting our businesses at a huge competitive disadvantage.*
  - *Approximately 50% of all industry sales are for edibles and concentrates. Putting our collectives at a competitive disadvantage for this large segment of sales will negatively impact their ability to survive and may dramatically reduce our potential tax revenues.*
  - *There are already Board of Pharmacy and DEA guidelines in place for the regulation of transfer of pharmaceuticals which could easily replicated for any concerns we could have with product transfer.*
- 4. Allow legal collectives with Title 20 and Title 6 approval to continue to acquire product from patient vendors.**
- *It is not physically possible in any of the facilities in San Jose to grow and/or manufacture all of the product, which are currently available to San Jose Residents.*

5. **Ask staff to report back on possible enforcement and regulatory strategies to stop business activities of those not following our ordinance.**
  - *A quick review of the ap Weedmaps shows that there are dozens of operations in San Jose with either storefront or delivery services that are not in compliance with Title 20 or Title 6.*
  
6. **Ask staff to investigate branch location (for retail activities only) for collectives that have Title 20 and Title 6 compliance that would have less strenuous zoning requirements (i.e. regulations for a bar versus a brewery). This could reduce overconcentration and provide for stronger retail environment in regional sales.**
  - *The original Council direction was based upon the assumption that a single location would have retail, farming and manufacturing operations. This assumption led to a very limited number of locations in San Jose. This has led to an overconcentration of locations.*
  - *This has created an environment where it is very inconvenient for most San Jose residents to get to a legal collective because they are not spread out.*
  - *This also puts San Jose at a competitive disadvantage from retail competition from other cities as this industry expands.*
  
7. **Change distance separation requirements from other uses to always use building edge for regulated facilities rather than parcel edge.**
  - *Some of our separation requirements use building edge and some use parcel edge and there should be consistency. Building edge is the most sensible separation standard.*
  
8. **Clarify and change the current audit requirements in a way that allows a reasonable amount of time to secure an audit and allow for the type of audit that is reasonable (i.e. reviewed or compiled) given that all legal collectives are already under State Board of Equalization audit supervision for sales tax compliance.**
  - *We currently require audited financials by February 15<sup>th</sup>. February 15<sup>th</sup> is an impossible turn around time for an audited financial statement.*
  - *The auditing industry has had problems providing auditing services to this industry.*
  - *Collectives already pay sales tax and therefore already are under the scrutiny of the State Board of Equalization which is an adequate level of review for all other businesses in San Jose.*
  
9. **Change the record keeping requirement to allow for electronic data storage**
  - *Currently the ordinance requires all records to be in a printable format and maintained in a fire proof safe. This would quickly lead to businesses having warehouses full of fireproof safes. Electronic data file storage should be the norm in our City.*



We look forward to the Study Session to hear feedback from the Council as well. We strongly support the City's desire to continue to insure public safety while encouraging legal business operations and providing for the health benefits of our residents. We think that the dramatic reduction in the number of collectives operating not only reduces potential neighborhood impacts, but will also lead to stronger businesses in San Jose. Once again thank you very much for your time and efforts and please let us know how we can help.

Sincerely

A handwritten signature in black ink, appearing to read "Jerry Strangis". The signature is stylized with loops and a long horizontal stroke extending to the right.

Jerry Strangis

Cc: Mayor and City Council  
City Manager Norberto Duenas  
City Attorney Rick Doyle