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OFFICE OF THE CITY CLERK  
OAKLAND

2019 JAN 24 PM 5:08 **AGENDA REPORT**

**TO:** Sabrina B. Landreth  
City Administrator

**FROM:** Katano Kasaine  
Director of Finance

**SUBJECT:** Non-Medical Cannabis  
Business Tax Rate Reduction

**DATE:** January 21, 2019

City Administrator Approval

Date:

1/24/19

**RECOMMENDATION**

**Staff Recommends That The City Council Receive An Informational Report Regarding The Proposed Ordinance Amending Oakland Municipal Code Title 5, Chapter 5.04, Section 481, Non-Medical Cannabis Businesses, To Reduce The Tax Rate For Non-Medical Cannabis Businesses To Be The Same As the Medical Cannabis Business Rate of \$50.00 Per \$1,000.00 of Gross Receipts Or Fraction Thereof.**

**EXECUTIVE SUMMARY**

On November 6, 2018, Oakland voters, by a margin of 79.82 percent, approved the Oakland City Council, on its own motion, Measure V (1) allowing cannabis businesses to pay business taxes quarterly; (2) allowing cannabis manufacturing and/or cultivation businesses to deduct the value of raw materials from gross receipts in calculating business taxes; and (3) authorizing the City Council, without returning to voters, to amend medical or non-medical cannabis business taxes in any manner that does not increase the tax rate.

The focus of this informational report is Councilmember Kalb's proposed reduction of the existing business tax rate from \$100 per \$1,000, or 10%, of the gross receipts to \$50 per \$1,000, or 5%, of gross receipts on non-medical cannabis businesses. **Staff is recommending against adoption of the proposed Ordinance if it is to be effective in fiscal year (FY) 2018-19, as it would create an ongoing negative financial impact of approximately \$1.8 million without identified balancing measures. In addition, the proposed Ordinance adoption would negatively impact the possible 1% wage increases based upon the performance of unrestricted local tax revenues that is memorialized in all civilian labor bargaining groups' Memorandums of Understanding and the Local 55 Arbitration award.<sup>1</sup>**

<sup>1</sup> Wage increase tied to revenue growth- If FY 2018-19 general purposed fund unrestricted local tax revenues, as forecasted in the Third Quarter Revenue & Expenditure report or as confirmed based on audited actuals for FY 2018-19, exceed the General Purposed Fund unrestricted local tax revenues for FY 2018-19 as approved in the FY 2017-19 Adopted Policy Budget by 4.5% or more, bargaining unit members shall receive an additional 1.0% wage increase effective retroactive to the first pay period after January 1, 2019. For purposes of these calculations, unrestricted General Purpose Fund local tax revenues will be limited to ongoing revenues

## **BACKGROUND / LEGISLATIVE HISTORY**

In November 2010, Oakland voters approved Measure V increasing the tax rate on medical cannabis businesses from 1.8 (1.8%) to five percent (5%) and creating a new tax rate of 10 percent (10%) of gross receipts on non-medical cannabis businesses, referred to as adult-use or recreational. The additional 10 percent adult-use tax rate was put forth in anticipation of Proposition 19 being passed in the same election. Proposition 19 failed at the ballot box. As a result, Oakland never implemented the adult-use tax rate. Oakland's adult-use tax rate became effective for the first-time January 1, 2018 following the passage of Proposition 64 statewide in November 2016.

In February 2018, staff prepared and provided the City Council, at the request of then Council President Larry Reid, an informational report on Cannabis Business Tax Policy Analysis<sup>2</sup> that was drawn upon the work done by the Marijuana Policy Group, the University of the Pacific, Center for Business & Policy Research, and staff own experience in working the local cannabis businesses. The City Council received and filed the report on March 6, 2018.

In June 2018, the City Council adopted Resolution No. 87247 C.M.S submitting for voter consideration at the statewide general election on November 6, 2018 a proposed ordinance to (1) allow cannabis businesses to pay business taxes quarterly; (2) allow cannabis manufacturing and/or cultivation businesses to deduct the value of raw materials from gross receipts in calculating business taxes; and (3) authorize the City Council, without returning to voters, to amend medical or non-medical cannabis business taxes in any manner that does not increase the tax rate.

In November 2018, Oakland voters approved the City Council's proposed ordinance by a margin of 79.82 percent.

## **ANALYSIS AND POLICY ALTERNATIVES**

On June 19, 2018, the City Council adopted the FY 2018-19 Midcycle Budget Amendments, which, among other adjustments, included a projected upward adjustment of \$5.7 million increase in the Business License Tax category<sup>3</sup>. when compared to the FY 2017-18 Q3 Forecast. Of the \$5.7 million projected increase in the business license tax category, \$3.6 million, or 63%, was directly tied to the projected collection of business license tax from the non-medical tax rate of \$100 per \$1,000, or 10%, of the gross receipts that many cannabis businesses are expected to pay on or before March 1, 2019, with some are expected to receive an extension for the payment by April 10, 2019 or enter a repayment plan.

If adopted, the proposed reduction of 50% in the non-medical tax rate from 10% down to 5% of

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including: property taxes, sales taxes, business license taxes, utility user taxes, real estate transfer taxes, transient occupancy taxes and parking taxes.

<sup>2</sup> Cannabis Business Tax Policy Analysis:

<https://oakland.legistar.com/LegislationDetail.aspx?ID=3268538&GUID=D31F72D6-2697-4D9D-B4E4-73BBBAF2F7DE&Options=&Search=>

<sup>3</sup> Business License Tax Category: \$86,622,000 (FY 18-19 Midcycle) - \$80,962,300 (FY 2017-18 Q3 Forecast)  
<https://cao-94612.s3.amazonaws.com/documents/OAK070959.pdf>

the gross receipts will result in an equivalent 50%, or approximately \$1.8 million, less in the projected collection of business tax from the adult-use segment of cannabis businesses.

Alternatively, the adoption of non-medical tax rate reduction should also be viewed in the context of the City's current economic condition, including the areas of competition and enforcement efforts on the illegal market. In the competition area, and as noted in staff's February 2018 report, "less than 30% of cities and counties in California are allowing cannabis business and, of those that are, not all are allowing all aspects of the supply chain." Of this 30%, only "14 percent of California's cities and counties currently permit recreational marijuana sales" according to the article titled "Here's how Year One of legal marijuana in California played out" and published in the Mercury News on December 28, 2018. In the area of enforcement, the same article quoted the chief of California's Bureau of Cannabis Control stating that the "focus will be primarily on getting more businesses licensed and increasing enforcement efforts on the illegal market" in 2019.

On the City's budgetary front, which, in many aspects, is the key indicator of the City's overall economic condition, the City is experiencing increases in most of every revenue type during the last several years. The increases afforded the City Council to make key investment in high priorities areas, such as homelessness, affordable housing, illegal dumping and other issues important to the Oakland community. The proposed reduction could possibly dampen the City Council's ability in continuing making the investment in priorities areas important to the Oakland community. Moreover, the making of tax policy changes are arguably best designed and reserved to spur economic growth, especially during the economic downturn. Given the City's economic condition has largely recovered since the Great Recession in late 2007, and if history is of indication, a downturn or a slowdown in economy is not farfetched.

**FISCAL IMPACT**

Under the proposed ordinance, the reduction of 50% in the non-medical cannabis business tax rate from \$100 per \$1,000, or 10%, to \$50 per \$1,000, or 5%, of **gross receipts would result in the reduction of approximately \$1.8 million annually.** Alternatively, a reduction of 25% in the non-medical cannabis tax rate from \$100 per \$1,000, or 10%, to \$75 per \$1,000, or 7.5%, of gross receipts would result in the reduction of approximately \$900,000 annually. The tax revenue being proposed to be decreased is already in the Adopted FY 2018-19 Mid-Year Operating Budget and has expenditures budgeted against the planned revenue. If the proposed Ordinance is adopted, the Council would need to identify \$1.8 million of budgeted expenditures to cut. Furthermore, adoption of the proposed Ordinance would negatively impact the possible 1% wage increases based upon the performance of unrestricted local tax revenues that is memorialized in all civilian labor bargaining groups' Memorandums of Understanding and the Local 55 Arbitration award.

| Cannabis Revenue | 2018-19 Adopted budget | 2018-19 Midcycle Forecast | Financial Impact 50% Reduction of Tax Rate | Financial Impact 25% Reduction of Tax Rate |
|------------------|------------------------|---------------------------|--|--|
| Medical          | \$ 5,580,912           | \$ 7,416,656              | \$ 7,416,656                               | \$ 7,416,656                               |
| Recreational     | \$ 3,400,000           | \$ 3,583,344              | \$ 1,791,672                               | \$ 895,836                                 |
| Total            | \$ 8,980,912           | \$ 11,000,000             | \$ 9,208,328                               | \$ 8,312,492                               |

*Recommendation*

**Due to the negative fiscal impact on the Adopted Mid-Year FY 2018-19 Operating Budget and the negative impact to adopted labor Memorandums of Understanding, staff is recommending that the City Council not adopt the proposed Ordinance reducing the current tax rate for non-medical cannabis businesses from 10% to 5% effective FY 2018-19. In addition, the proposed Ordinance adoption would negatively impact the possible 1% wage increases based upon the performance of unrestricted local tax revenues that is memorialized in all civilian labor bargaining groups' Memorandums of Understanding and the Local 55 Arbitration award.**

**PUBLIC OUTREACH / INTEREST**

No outreach was deemed necessary for this informational report beyond the standard Council agenda noticing procedures

**COORDINATION**

This report has been coordinated with the Budget Bureau.

**SUSTAINABLE OPPORTUNITES**

**Economic:** A reduction of non-medical tax rate would allow the City to stay on par with tax rates in adopted in surrounding jurisdictions and possibly encourage more cannabis businesses to stay or to open in the City. Conversely, the reduction would also result in the lower tax revenue and possibly limit the City's ability to attract and diversify its economic base due to cannabis businesses taking up more industrial buildings and/or warehouses.

**Environmental:** The most important environmental concerns related to cannabis industry are in the consumption of water and the disposal of unused or discarded waste. Robust regulations regarding the disposal of waste should minimize the impact. The use of precious water resource is, at this time, unavoidable.

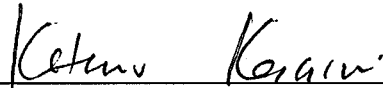
**Social Equity:** There is no social equity related to the proposed reduction of the tax rate.

**ACTION REQUESTED OF THE CITY COUNCIL**

Staff recommends that the City Council accept this informational report regarding the proposed Ordinance amending Oakland Municipal Code Title 5, Chapter 5.04, Section 481, Non-Medical Cannabis Businesses, to reduce the tax rate for non-medical cannabis businesses to be the same as the medical cannabis businesses rate of \$50.00 per \$1,000.00 of gross receipts or fraction thereof.

For questions regarding this report, please contact Margaret O'Brien, Revenue & Tax Administrator, (510) 238-7480.

Respectfully submitted,



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