




**SAN RAFAEL CITY COUNCIL AGENDA REPORT**

**Department: Economic Development/City Manager**

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City Manager Approval: \_\_\_\_\_ 

**TOPIC: SAN RAFAEL CANNABIS INDUSTRY TAX RATE SETTING**

**SUBJECT: RESOLUTION SETTING LOWER CANNABIS INDUSTRY TAX RATES FOR CANNABIS DELIVERY BUSINESSES, FOR THE PERIOD OF JANUARY 1, 2023 THROUGH DECEMBER 31, 2024**

**RECOMMENDATION:**

Adopt the Resolution setting lower cannabis industry tax rates for cannabis delivery businesses, for the period of January 1, 2023 through December 31, 2024.

**BACKGROUND:**

In June 2018, San Rafael voters approved Measure G. This voter-approved measure, Ordinance [No. 1961](#), codified at [Chapter 3.40](#) of the San Rafael Municipal Code, imposes a special business tax on businesses engaged in commercial cannabis activity in the City. The ordinance authorizes the City Council to adjust tax rates by resolution. Tax rates shall be set for a minimum of a two (2) year term. The rate may not exceed 8%.

Currently, the City taxes cannabis businesses at the rates in Table 1, based on state license type.

**Table 1: Current Tax Rates (percent of gross receipts)**

State License Type	Current Rates
Delivery, non-storefront retail	4%
Infused Products Manufacturing	3%
Cannabis Testing Labs	1%
Distribution	1%

The proposed resolution would lower the tax rate only for licensed cannabis delivery businesses from 4% to 2%, for the time period of January 1, 2023 through December 31, 2024. Beginning January 1, 2025, the current tax rate of 4% would go back into effect. Tax rates for the three other types of businesses

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**FOR CITY CLERK ONLY**

**Council Meeting:** \_\_\_\_\_

**Disposition:** \_\_\_\_\_

engaged in commercial cannabis activity – manufacturing, testing labs, and distribution - would stay at their current rates. Table 2 presents the rates that would apply starting January 1, 2023 if the Council adopts the resolution.

**Table 2: Proposed Tax Rates (percent of gross receipts)**

State License Type	Current	Proposed January 1, 2023 – December 31, 2024	Proposed January 1, 2025 and thereafter
Delivery, non-storefront retail	4%	<b>2%</b>	4%
Infused Products Manufacturing	3%	3%	3%
Cannabis Testing Labs	1%	1%	1%
Distribution	1%	1%	1%

**ANALYSIS:**

The City regulates licensing of commercial cannabis activities in the City under Chapter 10.96 of the San Rafael Municipal Code. The program under Section 10.96.050, “Commercial Cannabis Businesses Authorized”, authorizes four types of commercial cannabis business licenses:

- Cannabis Delivery, non-storefront retail (State License Type 9)
- Cannabis Infused Product Manufacturing (State License Type N)
- Cannabis Testing Labs (State License Type 8)
- Cannabis Distribution (State License Type 11)

The City’s Economic Development Department has been responsible for licensing, revenue collection and tracking of the State’s regulatory framework.

Periodically, the Cannabis Business Operator License ordinance is adjusted to improve program outcomes and sync-up local regulations with new or revised State regulations. The State’s cannabis regulatory framework continues to evolve and can also require periodic updates at the local level. The license program was most recently modified in March 2019 through Ordinance No. [1968](#) which expanded its provisions to authorize, by license, both medical and adult-use commercial cannabis activities In San Rafael. The proposed ordinance to change the tax rates does not adjust or modify the current licensing program.

**Taxes:**

On June 30, 2022 Governor Newsom signed [Assembly Bill 195](#), which eliminated California’s cannabis cultivation tax but included a provision to allow for the increase of California’s cannabis excise tax from 15% up to 19% beginning in 2025 to make up for revenue losses from the discontinuation of the cultivation tax. This shifts the tax burden to retail and delivery businesses who are responsible for the cannabis excise tax.

There are three taxes applicable to cannabis sales in San Rafael: the 15% State excise tax, the Measure G cannabis tax, and the local sales and use tax of 9.25%. Cannabis delivery businesses in the City of San Rafael pay the following tax rates as of November 7, 2022:

Tax Type	Tax Rate
San Rafael Cannabis Tax – Delivery	4%
Combined Sales and Use Tax	9.25%
State Cannabis Excise Tax	15%
<b>Total Tax Rate as of November 2022</b>	<b>28.25%</b>

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While cannabis delivery businesses pay a total tax rate of 28.25%, San Rafael receives only the Measure G tax rate and 2% of the Sales and Use Tax revenues directly.

Local governments can tax cannabis sales at their discretion with voter approval. Local Cannabis Business Tax rates range as low as 1% and as high as 15% depending upon where you purchase legal cannabis across California.

Below is a sampling of local cannabis tax rates in California:

<b>Jurisdiction</b>	<b>Cannabis Tax Rate</b>
San Francisco City/County	Cannabis business tax has a suspension until 2023. San Francisco voters approved the tax in Nov. 2018, which imposes a 1% to 5% citywide tax on gross receipts from cannabis businesses.
Sonoma County	2% of gross receipts for retail and/or delivery businesses
Santa Cruz County	6% of gross receipts for retail and/or delivery businesses
Alameda County	Since launching their program, they have not instituted local cannabis tax for unincorporated areas
Monterey County	4.5% of gross receipts for retail and/or delivery businesses
Lake County	4% of gross receipts for retail and/or delivery businesses
Sonoma County	2% of gross receipts for retail and/or delivery businesses
City of Berkeley	5% of gross receipts for retail and/or delivery businesses
City of Santa Rosa	3% of gross receipts for retail and/or delivery businesses
City of Cotati	3% of gross receipts for retail and/or delivery businesses
City of Vallejo	7% of gross receipts for retail and/or delivery businesses
City of Sacramento	4% of gross receipts for retail and/or delivery businesses
City of Oakland	5%, for business with revenues over \$1.5M in sales annually General non-equity 4% for \$750-\$1.5M, and 5% for \$1.5-\$5M
City of Walnut Creek	No tax for medical delivery (2 permitted companies) and no adult recreational delivery permitted
City of Fairfield	6% of gross receipts for retail and/or delivery businesses
City of Petaluma	Since launching their program, they have not instituted local cannabis tax
City of Marysville	3% of gross receipts for retail and/or delivery businesses
City of Long Beach	8% of gross receipts for retail and/or delivery businesses
City of San Diego	8% of gross receipts for retail and/or delivery businesses
City of Novato	While the city does not have a special tax for cannabis businesses, it does enter into " <a href="#">community benefit agreements</a> " where the businesses provide the city or other organizations such as nonprofits a percentage of its gross receipts each year. All three businesses will be providing 1.5% to 4% of their gross receipts in these agreements.

**Challenges:**

As the California cannabis market continues to develop, our local businesses face many challenges. Cannabis businesses have significant capital requirements without access to traditional lending and banking services, costly compliance measures, competition with the black market, and relatively low profit margins, along with the significant business taxation.

Banking will continue to be a challenge because cannabis companies in the U.S. cannot legally access traditional banking services. According to the [American Bankers Association](#) (ABA), the possession, distribution or sale of cannabis remains illegal under federal law, which means any contact with money

that can be traced back to state cannabis operations could be considered money laundering and expose a bank to significant legal, operational and regulatory risk.

Cannabis companies did not have access to federal loan programs during the Covid-19 pandemic. Federal rules governing the Small Business Administration (SBA) loans program deemed cannabis business ineligible for popular programs like the Paycheck Protection Program (PPP) that provided critical support to the business community during the pandemic. The SBA considers a business ineligible for loans if that business is engaged in any illegal activity at the Federal, State, or local level ([13 CFR § 120.110\(h\)](#)).

All of these factors have left cannabis businesses feeling the burden of financial strain. Given the increased cost to do business and the lack of access to traditional financial relief streams, many cannabis businesses are considering ceasing operations. The City has had one cannabis business sell their operation this year.

To alleviate some of this burden and support our local businesses, staff is recommending program adjustments to the City’s Cannabis Tax for Delivery, non-storefront retail (State License Type 9) businesses. The proposed adjustment would be in the form of a 50% decrease in the current tax rate, adjusting the collected rate from 4% to 2% for two years. The tax relief program would go into effect beginning with receipts received January 1, 2023, and ending December 31, 2024. The current tax rate of 4% would go back into effect beginning January 1, 2025. At this time the council could reevaluate if the tax reduction provided the intended relief and should be extended or stopped.

The City has little control over many of the outstanding challenges facing cannabis businesses. The City Council has the authority to adjust cannabis tax rates by resolution from time to time, but not to exceed the maximum 8% rate authorized by the voters. The tax rates are set for at least two-year terms. Setting a rate for multiple years provides greater certainty to the industry and allows for the collection of data and information to inform the Council for any potential rate changes or rebates in the future.

Below is a breakdown of the estimated revenue impacts to the City if the Council were to implement a temporary tax relief of a 25% and 50% tax rate decrease for delivery businesses.

	<b>Full Current Rate</b>	<b>3% Rate</b>	<b>2% Rate</b>
Estimated Annual Revenue - Cannabis Delivery Tax	\$500,000	\$375,000	\$250,000
Proposed Tax Reduction	0%	25%	50%
Tax Rate	4%	3%	2%
Estimated Annual Lost Revenue from Tax Relief	\$0	\$125,000	\$250,000

Staff evaluated several scenarios including a tiered rate based on gross receipts, similar to the structure in Oakland. It was found that the most impactful and immediate relief would be felt through temporary Cannabis Tax relief for delivery businesses. While San Rafael’s cannabis delivery businesses currently pay the highest City cannabis tax rate, they also experience the largest effects of the excise tax. It is staff’s recommendation that cannabis tax relief focus on delivery businesses in San Rafael.

**COMMUNITY OUTREACH:**

After initially being approached by Cannabis delivery businesses in San Rafael on the hardships and high tax rates facing the industry, the City sought input from other cities and counties on how they structure cannabis taxes in their jurisdictions. City staff met internally to come up with several solutions to bring back to the cannabis businesses and gain their input on what would provide the most relief

moving forward. After conducting these follow up meetings with industry, the City received feedback is now recommending a 50% reduction in taxes for the time of two years, which can be re-evaluated at that time should the City Council wish to do so.

**FISCAL IMPACT:**

If the proposed Resolution is adopted, staff anticipates a decrease of approximately \$250,000 annually from the loss of tax revenue to the Cannabis Fund.

The City spends \$150,000 annually on staff time and technology for the cannabis program. Between the \$150,000 in ongoing program expenditures and \$200,000 annually intended for the Alternative Response Team, this action would require a General Fund subsidy for existing programs of \$100,000 annually.

	<b>At 4% Tax</b>	<b>At 2% Tax</b>
Revenues	\$500,000	\$250,000
Expenditures	\$(150,000)	\$(150,000)
Alternative Response Team	\$(200,000)	\$(200,000)
Net Income (Loss)	\$150,000	\$(100,000)

**OPTIONS:**

The City Council has the following options to consider on this matter:

1. Adopt Resolution setting lower cannabis industry tax rates for cannabis delivery businesses, for the period of January 1, 2023 through December 31, 2024.
2. Adopt Resolution with modifications.
3. Provide feedback on Resolution and direct staff to return with more information.
4. Take no action.

**RECOMMENDED ACTION:**

Staff recommends the Council adopt the resolution setting lower cannabis industry tax rates for cannabis delivery businesses, for the period of January 1, 2023 through December 31, 2024.

**ATTACHMENTS:**

1. Resolution

**RESOLUTION NO.**

**RESOLUTION SETTING LOWER CANNABIS INDUSTRY TAX RATES FOR CANNABIS DELIVERY BUSINESSES, FOR THE PERIOD OF JANUARY 1, 2023 THROUGH DECEMBER 31, 2024**

**WHEREAS**, in June 2018, San Rafael voters approved Measure G (Ordinance [No. 1961](#), codified at [Chapter 3.40](#) of the San Rafael Municipal Code), which imposes a special business tax on businesses engaged in commercial cannabis activity in the City; and; and

**WHEREAS**, the cannabis business tax ordinance authorizes the City Council to adjust tax rates by resolution. Tax rates shall be set for a minimum of a two (2) year term. The rate may not exceed 8%; and

**WHEREAS**, the City recognizes the volatility of the newly-legalized cannabis market and desires to set tax rates to balance the financial needs of the City and to support and encourage the industry to engage in a regulated market; and

**WHEREAS**, the City Council recognizes the economic challenges facing local businesses, particularly cannabis delivery services, and wishes to support these businesses and provide temporary tax relief; and

**WHEREAS**, cannabis businesses in San Rafael with license type 9, non-storefront retailer (delivery only), currently pay a tax of 4% of gross receipts on a quarterly basis.

**NOW THEREFORE, BE IT RESOLVED** that, pursuant to San Rafael Municipal Code section 3.40.050, the City Council hereby sets the tax rate for cannabis businesses in San Rafael with license type 9, non-storefront retailer (delivery only) at 2% of gross receipts, effective January 1, 2023 through December 31, 2024, and 4% of gross receipts beginning January 1, 2025. Tax rates for cannabis businesses with other license types shall be unmodified by this resolution.

I, LINDSAY LARA, CLERK of the City of San Rafael, hereby certify that the foregoing resolution was duly and regularly adopted by the City Council of the City of San

Rafael, Marin County, California, at a regular meeting, held on the 7<sup>th</sup> day of November 2022, by the following vote, to wit:

AYES: COUNCILMEMBERS:

NOES: COUNCILMEMBERS:

ABSENT: COUNCILMEMBERS:

LINDSAY LARA, City Clerk