



Memorandum

TO: PUBLIC SAFETY, FINANCE AND
STRATEGIC SUPPORT COMMITTEE

FROM: Anthony Mata

SUBJECT: SEE BELOW

DATE: January 31, 2024

Approved

Date

2/6/2024

**SUBJECT: CANNABIS BUSINESS REGULATIONS AND ANNUAL OPERATING FEE
COMPARISONS**

RECOMMENDATION

Accept the report on how San José's cannabis regulations compare to State of California regulations and how San José's cannabis business annual operating fee compares to other jurisdictions.

BACKGROUND

Based on the Public Safety, Finance, and Strategic Support Committee's direction on October 19, 2023,¹ staff is providing an update on the following topics:

1. The possibility of aligning San José's regulations with State regulations, including but not limited to, Identification Badge Requirements while maintaining the age of purchase at 21 years in San José; and
2. Comparing San José's annual fees for cannabis operations with other jurisdictions.

ANALYSIS

The City of San José's Cannabis Regulations were originally approved in July 2014, making the City one of the first in the State of California (State) to develop this type of program. Since 2015, 16 cannabis businesses successfully registered and have been operating in the City.² The State

¹ October 19, 2023 Public Safety, Finance and Strategic Support Committee Meeting, Item (d)3. CC 23-221
[Memorandum from Jimenez 10192023.pdf \(legistar.com\)](#)

² Cannabis Regulation information can be viewed here: <https://www.sjpd.org/about-us/organization/chief-executive-officer/cannabis-regulation>

implemented a regulatory program for adult-use (recreational) and medicinal cannabis in January 2018.

Comparison of San José’s Medical and Non-medical Cannabis Regulations to State Regulations

Age – Purchase, Employment, and Verification

Purchase

Under San José’s regulatory program, only persons aged 21 or older are allowed on a cannabis business’s location or premises, or to purchase cannabis from San José’s cannabis businesses (whether on-site or via delivery). Under State regulations, adults aged 21 and older are allowed to possess, purchase, cultivate, and consume cannabis in limited quantities for personal use (“Adult Use”). Additionally, adults aged 18 and older are allowed to possess, purchase, cultivate, and consume cannabis for medicinal purposes with a valid physician’s recommendation (“Medicinal Use”). San José’s regulatory program predates the State’s regulations and established the higher minimum age for purchase to help ensure cannabis and cannabis products do not easily make their way into the hands of San José’s youth.

If San José were to align its regulations with the State’s by allowing persons under 21—which would include many area high school students—to remain on a cannabis business’s property and/or purchase medicinal cannabis from San José retailers, it would facilitate easier access to cannabis and products containing cannabis for area high schoolers. These concerns are heightened by the fact that under the State’s regulations qualified medicinal patients can purchase more cannabis daily than an adult-use customer, and are allowed access to concentrated cannabis products that contain higher concentrations of THC (the psychoactive component in cannabis) per package than adult-use products. By maintaining the aged 21 or older restriction to be on a cannabis business’s property for both medical and adult use customers, San José’s regulatory program limits access to these high concentration products which could be easily diverted to our youth.

Employment

In regard to employment, San José’s regulations align with the State’s in that both require persons retained to work within or at a cannabis business’s location or premises to be at least 21 years of age.

Verification

Both San José's and the State's regulations require age verification prior to purchase; however, they differ in how that is accomplished. San José regulations require use of an electronic age verification device which scans a government-issued identification (driver license, identification card, passport, etc.) and displays the person's age. The State's regulations require "inspecting" a valid form of identification (ID). This leaves it up to the person inspecting the ID to know the "age 21 by" date, and/or to do the math to determine if the presenter of the ID is under 21 years old. In addition to the requirement for San José businesses to use electronic age verification, they are required to provide the results of age scans (date, time, and age) to San José's Division of Cannabis Regulation (Division) staff for analysis. Combined with the Division's ability to monitor video surveillance (discussed below), staff routinely confirms businesses are turning away persons (and parties with persons) under the age of 21.

In summary, aligning San José's age requirements to the State's would make it easier for high school students to obtain cannabis in San José by befriending or becoming an 18- to 20-year-old qualified medical patient. It would also remove the Division's ability to effectively review and monitor the presence of underage individuals purchasing cannabis at San José's dispensaries by removing the age verification logs routinely audited by Division staff.

	San José Regulations	State Regulations	Alignment
Age (Adult Use Purchase)	21 and older	21 and older	Aligned
Age (Medicinal Use Purchase)	21 and older	18 and older	Not aligned
Age (Employment)	21 and older	21 and older	Aligned
Age (Verification Method)	Electronic ID scanning	Inspecting ID	Not aligned

Identification Badge - Background and Display RequirementsBackground Checks

San José requires a criminal background investigation on all persons involved in the cannabis business – inclusive of owners (more than 10% aggregate interest, legal or equitable, or otherwise), managers (including but not limited to officers of a corporation and/or board members) and employees. This criminal background investigation reviews State criminal histories. The State evaluates state and federal criminal histories of owners (aggregate ownership interest of 20% or more) and individuals who manage, direct, or control a cannabis business (including but not limited to corporate officers or a member of the board of directors of a nonprofit).

	San José Regulations	State Regulations	Alignment
Background Required			
• Owners	more than 10%	20% or more	Not Aligned
• Board Members	Yes	Yes	Aligned
• Corporate Officers	Yes	Yes	Aligned
• Managers	Yes	Yes	Aligned
• Drivers	Yes	No	Not Aligned
• Employees	Yes	No	Not Aligned

San José regulations prohibit persons from owning, managing, or working at a cannabis business if the person has a disqualifying conviction³ within the last ten (10) years or in their lifetime for a crime of moral turpitude. The State may deny a license to an owner if they have a disqualifying felony conviction⁴. The State does not specify a time frame for the conviction but does take into consideration the number of years that have elapsed since the date of the offense. The crimes for which convictions could lead to disqualification or denial of a license are similar between San José and the State, and include crimes such as violence, force, fear, fraud, deception, theft, embezzlement, firearms, illicit drugs (excluding cannabis). Both San José and the State require all persons with a financial interest in the business be disclosed; however, only those persons who meet the above-described criteria are backgrounded.

As a part of the City's criminal history background check of specified persons working at or for the cannabis business, for delivery drivers, the Division verifies the driver has a valid driver license and insurance before issuing the identification badge. Another check important to delivery operations is the verification that the owner of the delivery vehicle (some are owned by the cannabis business, but many are not) knows the vehicle will be used to deliver cannabis. Similar to the requirement that property owners acknowledge the use of their property for cannabis operations, the Division thinks it is important for vehicle owners to know how their vehicles will be used.

People working in these businesses have behind-the-scenes access to cannabis, money, and sensitive business information such as building layouts and security measures. One of the concerns raised by the industry is the number and extent of burglaries associated with cannabis businesses, both here and in other cities. Including employees and managers – not just owners – in these background checks promotes a safer work environment in a sensitive industry.

³ San Jose Municipal Code Section 6.88.450.A.2 and 6.88.450.A.3

⁴ California Business and Professions Code Section 26057 and Department of Cannabis Control Medicinal and Adult-Use Commercial Cannabis Regulations (November 2023)

Display of Identification Badges

Both San José's regulations and the State's regulations require persons working at certain cannabis businesses to wear a specific identification badge; however, they differ greatly in purpose. The identification badge issued by the Division is issued after an individual has been fingerprinted as part of the criminal background investigation. By wearing the badge, it allows for quick and easy identification of those persons who have initiated the background process versus those who have not. The State requires an identification badge issued by the cannabis business be displayed by all employees working for a retail sales licensee or participating in a temporary cannabis event. This badge does not assist Division staff in determining who is undergoing the background check and who is not.

If San José's criminal background check and identification display requirements were removed, it would adversely disrupt the business' normal operations. Persons with identified criminal convictions involving violence, theft, or unlawful possession of firearms in the past ten years or crimes of moral turpitude at any point in time would have behind-the-scenes access to business operations, cannabis, and cash. During inspections, Division staff would need to contact each employee individually and have them stop working so they could retrieve their government-issued identification for comparison to our list of persons who have started the background process. For smaller businesses with less employees, this would be disruptive in their ability to conduct daily operations and assist customers. An additional benefit of the current identification badge issuance process is it affords the Division the opportunity to ascertain accurate employee counts to ensure compliance with Labor Peace Agreement requirements. The Division-issued badge serves as a simple visual indicator of whom the Division has processed as an owner, manager, or other employee, and who has not.

Security – Alarms, Secure Storage, Video Surveillance, Personnel

Alarms

In the area of property and product security, there are a few key differences between San José's regulations and the State's. San José requires each business to install and maintain a UL (Underwriters Laboratories) listed burglar alarm system. A UL-listed alarm system with a "Mercantile" certificate – a standard similar to jewelry stores – is required. The UL listing is a certification that indicates a product is safe to use and has undergone rigorous testing to meet specific safety standards. A UL burglar alarm system uses extensive sensors to detect any intrusion and trigger the alarm. San José's regulations also prescribe a specific response by the business: a security guard must respond within 20 minutes and attempt to verify the alarm, and the alarm company must also notify a representative of the business who must be available to respond to the location within one hour of being notified. In the event a break-in is verified (either by the guard or by video surveillance monitored by the business), the police department must be notified for a response. These regulations are intended to ensure alarm systems are robust and any response to the alarm is timely, to minimize loss. The State's regulations also

require an alarm monitored by an alarm company or agent but do not specify the standards of the alarm system (i.e.: extensive motion detection throughout the premises versus merely placing sensors on doors and windows) or the timeliness and nature of the response to an alarm activation.

Secure Storage

Both San José's regulations and the State's regulations require cannabis and cannabis products be stored indoors; however, San José additionally requires cannabis and cannabis products be stored in a safe, vault, or other secure storage inside the premises. This additional requirement is meant to make it more difficult to obtain and divert cannabis and cannabis products in the event of burglary. While alarm and secure storage regulations cannot prevent persons from breaking into a business, they can make it difficult and slow would-be burglars down. Staff have reviewed surveillance video of burglaries at San José businesses and it was apparent that perpetrators obtained less product than they would have obtained without a secure storage requirement.

Video Surveillance

Video camera systems are required by both San José and the State; however, video storage is another area in which San José's regulations differ from the State's. San José requires video be stored and made available to regulators or law enforcement for thirty (30) days, while the State requires video be retained and made available for ninety (90) days. Since the State's requirement is more restrictive, all San José businesses must follow the State's storage requirement of 90 days.

Personnel

Another difference in San José's security requirements versus the State's is the area of delivery vehicles. San José requires delivery vehicles employ a dual facing video camera system which records the view in front of the vehicle as well as inside the passenger compartment. This regulation is intended to provide a measure of safety and security in the event of theft or robbery. It also serves as a tool to assist the Division in determining if a delivery was made to a park or school. Delivery vehicle video is not required by the State and is therefore subject to San José's 30-day retention requirement.

Comparison of San José's Cannabis Business Annual Operating Fee to Other Jurisdictions

Cannabis Regulation Responsibilities

The Annual Operating Fee is intended to recover 100% of the costs incurred by the City to pay for the multi-department staff for their professional responsibilities and other costs needed to sustain the full scope of the City Council's policy direction for the Program, as set forth below.

- **City-Wide Policy Coordination, Implementation, and Sustainment:** Cannabis policy analysis requires coordination of multiple departments, including: each division of the Department of Planning, Building and Code Enforcement, the Fire Department, the Finance Department, the Police Department, and the City Attorney's Office. The Police Department's Division of Cannabis Regulation provides Program oversight and serves as the point of contact for the registered businesses and the policy development and implementation lead.
- **Non-criminal Law Enforcement and Investigation:** The Division of Cannabis Regulation is responsible for the coordination of the regulatory law enforcement and compliance work, administering internal enforcement procedures and training on such procedures, and serving as a liaison between the City and other law enforcement agencies. Staff are responsible for performing the day-to-day regulation of the businesses, including conducting inspections, and regulating and taking civil action against businesses if they are not in compliance with the Program regulations.
- **Code Enforcement and Zoning:** Planning and Code Enforcement staff provide resources for the necessary ongoing inspections for compliance with the Program regulations as they relate to both land use and business operations. Staff conduct repeated inspections of business sites, meet with business representatives to ensure compliance with Program regulations, issue administrative citations and/or compliance orders to non-compliant businesses, and appear before administrative bodies and in court to support the City in its enforcement actions.
- **Financial and Compliance Review:** Staff review the financial records of all businesses and coordinate with the City Manager's Office, the City Attorney's Office, the Police Department, and the Code Enforcement Division on financial investigations and financial audits of the businesses to ensure fiscal compliance with the Program regulations.
- **Legal:** The City Attorney's Office staff provide legal advice, support in interpreting the regulatory ordinances, and support in drafting updates to ordinances and policies related to the Program. In addition, the attorneys are charged with bringing legal civil action against businesses operating in violation of the Program regulations. Those actions could include preparing cases for and representing the City at administrative officer hearings, hearings before the Appeals Hearing Board, and civil court.

Comparison of Operating Fees or Permits

Staff reviewed the annual operating fee for cannabis business activities for notable neighboring California cities (Mountain View, Oakland, Sacramento, and San Francisco). The information is provided below. The operating fees vary between being charged per permit type, cannabis activity, or business. When the fee is based on permit type or activity, it is important to note one business may hold multiple permits or conduct multiple activities, and the total fee each business pays is based on the number of permits/activities.

	Number of Businesses or Permits	Annual Operating Fee
San José	16 Businesses (plus up to 10 equity allowed)	Per Business \$139,406
Mountain View	1 Business (maximum of 3 allowed)	Per Business \$139,619
Oakland	266 Businesses (including 106 equity)	Per Permit ranging from \$509.75 to \$17,618*
Sacramento	291 Permits (including 41 equity)	21 Permit Types ranging from \$2,590 to \$36,800 each*
San Francisco	108 Permits (including 40 equity)	Per Activity \$5,000*

* one business may hold multiple permits or have multiple activities; the fee paid by each business varies based on the number of permits/activities

San José's Annual Operating Fee Per Business

As stated above, San José's cannabis regulation staffing is based on regulatory and enforcement operations related to the 16 registered cannabis businesses. The costs for the program are paid by the registered businesses in their annual operation fee and other fees for service. Since the cannabis regulatory program was moved to the Police Department, the annual operating fee regulatory staffing levels have decreased from 11.33 to 7.25. The annual operating fee is currently based on 16 registered businesses.

Fiscal Year	16-17	17-18	18-19	19-20	20-21	21-22	22-23	23-24
Police	3.94	3.38	4.89	5.17	5.11	5.11	5.07	5.02
Finance	1.75	1.69	1.69	1.54	1.34	1.19	0.98	0.98
CMO	0.14	0.10	0.22	-	-	-	-	-
CAO	3.50	2.70	2.27	1.15	1.15	1.04	1.04	0.74
PBCE	2.00	1.91	0.94	1.09	0.81	0.81	0.33	0.51
Total FTE	11.33	9.78	10.01	8.95	8.41	8.15	7.42	7.25
Annual Fee	\$149,132	\$131,846	\$150,610	\$138,148	\$143,333	\$147,645	\$130,345	\$139,406

In addition to the regulations themselves, San José, the State, and other municipalities each take different approaches to their programs. San José's regulatory structure is one of full cost recovery and is reflected in the fees. The State's fee structure is based on the size and type of business and is not based on full cost recovery. Other cities devote staff to regulate cannabis businesses, but their fees are also not based on a full cost recovery model. A robust set of regulations paired with an appropriately staffed oversight program helps ensure these businesses are operating as expected. Additionally, having local staff in addition to State regulators monitoring cannabis businesses provides additional oversight and more robust safety protections.

Cannabis Regulatory Code Violations in Fiscal Year 2022 – 2023

Division Staff routinely monitor registered businesses in San José to ensure compliance with the Code, State laws, and regulations. This monitoring includes keeping track of identification badges issued and returned; ensuring delivery drivers hold valid driver licenses, delivery vehicles are registered, insured, and are equipped with secure storage containers; cannabis deliveries are not made to schools or parks; government-issued identifications are scanned by age verification devices and persons under age 21 are turned away; video cameras remain operational and function as required; and business operations and premises are not modified without notice or required building permits. Additionally, Division Staff are being trained in the State's Track-and-Trace system, which will allow Division Staff to supplement State regulators with tracking product through San José's cannabis businesses. During this routine monitoring, violations can be addressed informally in conversations with the businesses, formally via written warnings, or by issuance of a citation. Division Staff prefer to educate business operators through informal or formal warnings rather than by citation. Since Division Staff have 24/7 access to video camera and delivery vehicle GPS systems of San José's registered businesses, staff can do much of this monitoring without visiting each business in person. Video monitoring and GPS tracking of delivery vehicles can be done daily. State regulators do not have direct access to these video or GPS systems; therefore, State regulators must visit each business to ensure compliance. In conversations with businesses, it appears the State visits San José businesses about once a year, versus Division Staff constantly monitoring the businesses remotely throughout the year.

Staff formally reviewed 25 potential code violations which occurred during Fiscal Year 2022-2023. Some of the incidents investigated were violations of multiple code sections. For example, San José has a code section requiring compliance with all State codes; thus, a violation of a State code is also a violation of San José's Municipal Code. In reviewing these incidents, Staff issued 13 warning notices for violations ranging from repositioned cameras to inadequate camera failure notification systems or video storage to persons not displaying identification or visitor badges as required under local and State regulations. Three violations resulted in citations issued to two registered businesses, one of which is no longer operating. Additionally, there were three citations issued to registered businesses which Division Staff did not seek or investigate, but which Division Staff worked with another City Department to reevaluate and cancel.

Compliance is the goal of regulation. When violations of regulations occur, staff prefers to work with the businesses to develop a plan to ensure these violations are not repeated rather than to issue citations. The annual renewal of each business includes a thorough review of all forms, plans, a walk-through of each location and premises, and verification of tax compliance. Any issues uncovered during this review are typically addressed informally with business representatives to further the goal of ensuring our regulated businesses are operating as our community expects.

Under the State's regulatory program, cannabis businesses are required to have local approval to operate in addition to a State license. This allows local jurisdictions to draft and enforce local

regulations of importance to our communities. If San José were to rely solely on State regulators to monitor cannabis businesses in San José, it is highly unlikely that many of the previously discussed potential violations would have been discovered or addressed. State regulators must manage over 9,700 active licenses across all jurisdictions in California. Having local regulators monitor local businesses allows the City to maintain focus on those issues most important to the concerns of our community. Additionally, each business in San José has dedicated local personnel to whom they can ask questions and get timely answers.

Future Cannabis Regulatory Program Review

Staff is scheduled to review and discuss the possibility of expanding the San José Police Department Division of Cannabis Regulation's responsibilities to include regulating licensed tobacco retailers at the Public Safety, Finance, and Strategic Support Committee meeting on April 18, 2024.

EVALUATION AND FOLLOW-UP

Staff will continue to provide the City Council with updates via informational memoranda regarding the progress of the City's cannabis regulatory program, changes in state law, and other developments potentially impacting the regulatory landscape.

COST SUMMARY/IMPLICATIONS

The costs associated with the cannabis regulatory functions are 100% recovered by the registered businesses for a net-zero impact on the General Fund.

COORDINATION

This memorandum was coordinated with the City Attorney's Office and the City Manager's Office.

PUBLIC OUTREACH

This memorandum will be posted on the Public Safety, Finance and Strategic Support Committee Agenda website for the February 15, 2024, Committee meeting.

COMMISSION RECOMMENDATION AND INPUT

No commission recommendation or input is associated with this action.

CEQA

Not a Project, Public Project File No. PP17-008, General Procedure and Policy Making resulting in no changes to the physical environment.

PUBLIC SUBSIDY REPORTING

This item does not include a public subsidy as defined in section 53083 or 53083.1 of the California Government Code or the City's Open Government Resolution.



ANTHONY MATA
Chief of Police

For questions, please contact Wendy Sollazzi, Division Manager, Division of Cannabis Regulation, San José Police Department, at wendy.sollazzi@sanjoseca.gov or (408) 537-9890.