



City of Culver City

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Staff Report

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CC - ACTION ITEM: (1) Discussion of Whether to Reduce the Cannabis Business Tax Rate for Cannabis Distribution from 2% To 0%; and (2) Direction to the City Manager as Deemed Appropriate.

Meeting Date: September 11, 2023

Contact Person/Dept.: Jesse Mays/City Manager's Office

Phone Number: (310) 253-6000

Fiscal Impact: Yes No **General Fund:** Yes No

Attachments: Yes No

Public Notification: (E-Mail) Meetings and Agendas - City Council (09/06/2023); Cannabis (09/05/2023)

Department Approval: John Nachbar, City Manager (09/05/2023)

RECOMMENDATION

Staff recommends the City Council (1) discuss whether to reduce the cannabis business tax for cannabis distribution from 2% to 0%; and (2) provide direction to the City Manager as deemed appropriate.

BACKGROUND

At its meeting on August 28, 2023, in response to a request by a representative from a permitted Culver City cannabis manufacturing, distribution, and delivery-only retail business, the City Council requested that staff agendize a discussion of whether to lower the cannabis business tax rate from 2% to 0%.

On the April 10, 2018 municipal election ballot, Culver City voters approved Measure A, a cannabis business tax. The ballot measure added Chapter 11.32 to the Culver City Municipal Code, which governs the cannabis business tax. The initial and maximum rates for the tax, as approved by voters, are as follows:

- Retail (medicinal): range of 5 -8% with an initial rate of 5%

- Retail (adult-use): range of 6-10% with an initial rate of 6%
- Manufacturing: range of 4-6% with an initial rate of 4%
- Distribution: range of 2-6% with an initial rate of 2%
- Testing: 1-1.5% with an initial rate of 1%
- Cultivation: \$12 per square foot of canopy

The initial rates were put in place for a minimum of two years, after which they have been able to be adjusted by City Council resolution. Cultivation rates were to be adjusted according to the consumer price index after a two-year initial period. To date, the City Council has not adjusted the initial rates approved by voters.

Cannabis distribution tax rates in other California cities are included in Attachment 1.

DISCUSSION

Policy arguments in favor of eliminating the cannabis distribution tax are:

- The legal cannabis industry is struggling under the weight of taxation and regulation, which is allowing the illegal industry to thrive.
- Cannabis distributors are uniquely impacted by taxes, compared to other types of cannabis businesses, because they are not able to pass along the tax to customers, since wholesale customers demand wholesale prices without added taxes.
- The amount the City is currently collecting from the distribution tax (less than \$200,000 annually) is not significant.
- The City could possibly see a net increase in tax revenue by attracting and retaining distributors who do both distribution and retail-delivery, thereby increasing the City's revenue from retail-delivery taxes (which is 6%). Distributors are less concerned about retail-delivery taxes because they can pass along the tax to consumers. However, this depends on the business decision of each individual business. Culver City has not yet had a cannabis distributor who also does retail-delivery in sufficient enough volume to equal or exceed the loss in distribution revenue.
- Some other California jurisdictions have eliminated the distribution tax.

Policy arguments in favor of maintaining the distribution tax are:

- Culver City's 2% distribution tax is already lower than the distribution tax in many other jurisdictions.
- The amount of distribution tax currently collected (less than \$200,000 annually) is not very much revenue to the City, so if distribution businesses choose to leave for another jurisdiction with a lower tax rate, it will not result in much revenue loss for the City.
- One of the main benefits of distribution cannabis businesses is that they provide tax revenue. They are businesses that are generally closed to the public, so they do not activate the street, and they add relatively few jobs to the local economy. By eliminating their tax, the City would no longer derive the main benefit these businesses provide to the City.
- Reducing the distribution tax rate to 0% would likely mean that Culver City would no longer

receive any tax revenue from cannabis manufacturers. Vertically integrated cannabis businesses, which in Culver City have both manufacturing and distribution permits, typically only pay one tax rate in cities that have a special cannabis tax. Because the transfer of the cannabis from manufacturer to distributor is within the same company, there is no “gross receipts” generated and therefore no tax due. Tax is only due when the company distributes the tax to retailers, at which point there is a third-party transaction generating gross receipts that is taxable as cannabis distribution tax. If the cannabis distribution tax rate is 0%, the manufacturer will not pay any cannabis business tax.

The Culver City Ad Hoc Cannabis Subcommittee (Mayor Vera and Council Member Eriksson) met in April 2023 to discuss this issue. The Subcommittee has not made a recommendation to the City Council on this issue.

FISCAL ANALYSIS

The impact to the City of lowering the cannabis business tax on distribution from 2% to 0% would result in a reduction of General Fund revenue of approximately \$200,000 annually.

ATTACHMENTS

1. Cannabis Distribution Tax Rates in Other California Cities

MOTIONS

That the City Council:

1. Discuss whether to lower the cannabis distribution tax from 2% to 0%; and
2. Direct the City Manager as deemed appropriate.