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5-15-2020

## The California Cannabis Industry: The Complexities Since Recreational Legalization

Talia Lux

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### Recommended Citation

Talia Lux, *The California Cannabis Industry: The Complexities Since Recreational Legalization*, 13 J. Bus. Entrepreneurship & L. 209 (2020)

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# THE CALIFORNIA CANNABIS INDUSTRY: THE COMPLEXITIES SINCE RECREATIONAL LEGALIZATION

Talia Lux\*

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INTRODUCTION

The cannabis<sup>1</sup> industry has become an increasingly popular, yet controversial topic. Although more than half of the United States legalized some usage of cannabis as of 2019,<sup>2</sup> cannabis continues to be illegal federally. State medical cannabis legalization occurred fairly recently, beginning two decades ago, and state recreational legalization first commenced in 2012.<sup>3</sup> Since the cannabis industry is relatively new, there is a lot of gray area in the law and thus skepticism surrounding individuals interested in partaking in the industry.

This comment will first provide a look into the history and legality of cannabis in the United States, followed by a look into California’s cannabis industry. There will be a discussion on both medical and recreational legality in California and the provisions surrounding both types of legality. Next, the complexities of the cannabis industries will be discussed in terms of opening and operating a cannabis business, the different cannabis business types and the requirements for starting them, and state and local limitations. Immediately following, there will be a federal illegality discussion and how federal illegality conflicts with California law in terms of ethical considerations for attorneys, employer

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<sup>1</sup> Throughout this article, “cannabis” and “marijuana” will be used interchangeably.

<sup>2</sup> Ten states and the District of Columbia legalized recreational and medical cannabis, and twenty-three states legalized only medical cannabis. *Map of Marijuana Legality by State: Wondering What the Law is in Your State?*, DISA, <https://disa.com/map-of-marijuana-legality-by-state> (last updated Sept. 2019).

<sup>3</sup> *State Medical Marijuana Laws*, NAT’L CONF. OF ST. LEGIS. (Sept. 27, 2019), <http://www.ncsl.org/research/health/state-medical-marijuana-laws.aspx>.

accommodation, child custody, and criminal liability. There is a section discussing cannabis financing. Lastly, regulation of cannabis sales will be discussed, particularly taxation of cannabis, the ongoing presence of illicit sales, steps California took to combat the illicit market, and other steps California could take.

## I. HISTORY

This section summarizes the legal and economic history of cannabis in the United States in general, from the early 1600s to the present. The next section discusses the legality surrounding cannabis in California from 1996 to the present day, including medicinal and recreational legality.

### A. *The History of Cannabis in the United States*

In the seventeenth century, the American government began encouraging the production of hemp.<sup>4</sup> In 1619, the Virginia Assembly passed legislation requiring hemp to be grown on every farm, and hemp was even used as currency.<sup>5</sup> At the end of the Civil War, as new products arose that replaced hemp, hemp production began to dwindle.<sup>6</sup> Cannabis production, however, began to soar.<sup>7</sup> Between 1850 and 1937, cannabis was widely used throughout the United States for medicinal purposes and was easily purchasable.<sup>8</sup> In 1910, following the Mexican Revolution,

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<sup>4</sup> *Marijuana Timeline*, PBS FRONTLINE, <https://www.pbs.org/wgbh/pages/frontline/shows/dope/etc/cron.html> (last visited Oct. 7, 2019). Hemp is the fiber of the cannabis plant used for industrial purposes, including textiles, paper, clothing, and raw materials. In fact, even the Declaration of Independence was written on hemp paper. See Logan Yonavjak & Ashoka, *Industrial Hemp: A Win-Win For The Economy And The Environment*, FORBES (May 29, 2013), <https://www.forbes.com/sites/ashoka/2013/05/29/industrial-hemp-a-win-win-for-the-economy-and-the-environment/#ac29e88289b1>.

<sup>5</sup> *Id.*

<sup>6</sup> Allison McNearney, *The Complicated History of Cannabis in the US*, HISTORY, <https://www.history.com/news/marijuana-criminalization-reefer-madness-history-flashback> (last updated Aug. 22, 2018). Cotton was the main fabric which replaced hemp. *Id.*

<sup>7</sup> *A Social History of America's Most Popular Drugs*, PBS FRONTLINE, <https://www.pbs.org/wgbh/pages/frontline/shows/drugs/buyers/socialhistory.html> (last visited Oct. 7, 2019).

<sup>8</sup> *Id.*

Mexican immigrants introduced the recreational use of cannabis.<sup>9</sup> The Great Depression sparked the concern of many Americans that cannabis was a problem—

“massive unemployment and increased public resentment and fear of Mexican immigrants escalated public and governmental concern about the potential problem of [cannabis]”—and by 1931, twenty-nine states had outlawed cannabis.<sup>10</sup> Thus, in 1937, Congress passed the Marihuana Tax Act, which criminalized cannabis.<sup>11</sup> During World War II, however, despite being amid the height of the cannabis-related controversy, the United States lifted restrictions on hemp productions.<sup>12</sup> In fact, the Department of Agriculture launched a film, “Hemp for Victory,” which encouraged farmers to grow hemp.<sup>13</sup> Nevertheless, once the War ended, hemp production was again banned.<sup>14</sup>

In 1969, the Court found the Marihuana Tax Act unconstitutional.<sup>15</sup> Following the Court’s finding of the Act’s unconstitutionality, Congress repealed the Marihuana Tax Act and implemented the Comprehensive Drug Abuse Prevention and Control Act of 1970, commonly known as the Controlled Substances Act.<sup>16</sup> The Controlled Substances Act is still in effect, and places all federally regulated substances into one of five schedules based on whether they have accepted medical use in treatment in the United States, their abuse potential, and dependency potential stemming from such abuse.<sup>17</sup> Cannabis falls under schedule one which has “no currently accepted medical use in the United States, a lack of accepted safety for use under

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<sup>9</sup> *Survey of Marijuana Law in the United States: History of Marijuana Regulation in the United States*, ALEXANDER CAMPBELL KING L. LIBR. SCH. OF L. U. OF GA., <https://libguides.law.uga.edu/c.php?g=522835&p=3575350> (last visited Oct. 7, 2019) [hereinafter *Marijuana History Survey*].

<sup>10</sup> *Id.*

<sup>11</sup> *Id.*

<sup>12</sup> *The People’s History*, 13 THE THISTLE 2 (Sept.–Oct. 2000), <https://www.mit.edu/~thistle/v13/2/history.html> (discussing how the 1942 Japanese invasion of the Philippines, the United States’ major source of hemp imports, cut the United States off from importing hemp).

<sup>13</sup> *Id.*

<sup>14</sup> *Id.*

<sup>15</sup> *Leary v. United States*, 395 U.S. 6, 37 (1969).

<sup>16</sup> *Marijuana Timeline*, *supra* note 4; 21 U.S.C. § 801 *et seq.* (2018).

<sup>17</sup> *Controlled Substances Schedules*, U.S. DEP’T OF JUST. DRUG ENF’T ADMIN. DIVERSION CONTROL DIV., <https://www.deadiversion.usdoj.gov/schedules/> (last visited Oct. 7, 2019).

medical supervision, and a high potential for abuse.”<sup>18</sup> This schedule one designation makes cannabis possession and cultivation carry the highest penalties, and makes access to cannabis extremely difficult since it is deemed medically useless.<sup>19</sup> This schedule one designation remained prominent throughout the United States for decades due to the ongoing War on Drugs.<sup>20</sup> In the last two decades, however, there has been a major shift in the public’s perception of cannabis, evidenced by many states permitting its use.<sup>21</sup>

### *B. The History of Cannabis in California*

This section explores the trajectory of cannabis legality in California from 1996 to the present day. Medical cannabis legality will be discussed first as it has been legal for over two decades, followed by a discussion of recreational legality which began with Proposition 64.

#### *1. Medical Cannabis Legality*

In 1996, Proposition 215, also known as the Compassionate Use Act, passed, making the medical use of cannabis legal in California.<sup>22</sup> The Compassionate Use Act exempted patients and caregivers who possessed and cultivated cannabis for medical purposes, and physicians who recommended cannabis, from criminal prosecution or sanctions.<sup>23</sup> In 2004, to regulate the usage of medical cannabis and resolve problems that arose

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<sup>18</sup> *Id.*

<sup>19</sup> Scott C. Martin, *A Brief History of Marijuana Law in America*, TIME (Apr. 20, 2016), <http://time.com/4298038/marijuana-history-in-america/>; *Milestones in U.S. Marijuana Laws*, N.Y. TIMES, [https://archive.nytimes.com/www.nytimes.com/interactive/2013/10/27/us/marijuana-legalization-timeline.html/#time283\\_8144](https://archive.nytimes.com/www.nytimes.com/interactive/2013/10/27/us/marijuana-legalization-timeline.html/#time283_8144) (last visited Oct. 7, 2019).

<sup>20</sup> Marijuana History Survey, *supra* note 9.

<sup>21</sup> *Id.*

<sup>22</sup> *State Medical Marijuana Laws*, *supra* note 3.

<sup>23</sup> CAL. HEALTH & SAFETY CODE § 11362.5 (West 1999).

with the passing of the Compassionate Use Act,<sup>24</sup> Senate Bill 420 was enacted, which established Proposition 215 guidelines.<sup>25</sup>

Senate Bill 420 established voluntary identification cards for qualified medical patients or caregivers, which exempted them from criminal liability.<sup>26</sup> Cardholders or other qualified patients were still subject to criminal liability for smoking cannabis where smoking is prohibited—in or within 1,000 feet of a school or the like, on a school bus, while in a motor vehicle that is being operated, or while operating a boat.<sup>27</sup> Moreover, the Bill allowed patients or primary caregivers up to six mature or twelve immature plants and up to eight ounces of dried cannabis.<sup>28</sup> The Bill exempted extremely ill patients from following such guidelines if they had a physician’s statement saying they needed more, and allowed counties and cities to establish higher guidelines.<sup>29</sup>

## 2. Prop 64 – Recreational Legality

Proposition 64, also known as the Adult Use of Marijuana Act, was approved by California voters in November of 2016.<sup>30</sup> Beginning on January 1, 2018, Proposition 64 legalized the recreational use of cannabis

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<sup>24</sup> Senate Bill 420, [http://www.leginfo.ca.gov/pub/0304/bill/sen/sb\\_0401-0450/sb\\_420\\_bill\\_20031012\\_chaptered.html](http://www.leginfo.ca.gov/pub/0304/bill/sen/sb_0401-0450/sb_420_bill_20031012_chaptered.html) (problems arose that “impeded the ability of law enforcement officers to enforce its provisions as the voters intended and, therefore, have prevented qualified patients and designated primary caregivers from obtaining the protections afforded by the act. Furthermore, the enactment of this law . . . demonstrates that more information is needed to assess the number of individuals across the state who are suffering from serious medical conditions that are not being adequately alleviated through the use of conventional medications.”).

<sup>25</sup> *SB 420 Establishes Prop. 215 Guidelines, Voluntary Patient Identification Card System*, CALIFORNIA NORML, <http://www.canorml.org/laws/sb420.html> (last visited Oct. 7, 2019) [hereinafter *Prop. 215 Guidelines*].

<sup>26</sup> Senate Bill 420, *supra* note 24. However, nothing shall authorize the individual to smoke or otherwise consume cannabis not in accordance with the Compassionate Use Act and this bill, nor shall it authorize the individual to cultivate or distribute cannabis for profit. CAL. HEALTH & SAFETY CODE § 11362.765(a) (West 1999).

<sup>27</sup> CAL. HEALTH & SAFETY CODE § 11362.79 (West 1999).

<sup>28</sup> CAL. HEALTH & SAFETY CODE § 11362.77(a) (West 1999).

<sup>29</sup> *Prop. 215 Guidelines, supra* note 25.

<sup>30</sup> *Proposition 64 – Marijuana Legalization in California*, SHOUSE CAL. L. GROUP, <https://www.shouselaw.com/prop-64.html> (last visited Oct. 7, 2019).

for people twenty-one and older.<sup>31</sup> It is currently legal for people twenty-one and older to “possess, process, transport, purchase, obtain or give away” to people twenty-one and over up to one ounce (28.5 grams) of cannabis, eight grams of concentrated cannabis, or any cannabis accessories.<sup>32</sup> It is also legal to “possess, plant, cultivate, harvest, dry, or process” up to six living cannabis plants and the cannabis produced by such, and to smoke or ingest cannabis products.<sup>33</sup> The possession of cannabis for sale, however, is a misdemeanor and subjects individuals to imprisonment or fines, unless one has valid licenses or permits issued by a state governmental authority.<sup>34</sup> Under this same provision, defendants who were convicted for possession with the intent to sell cannabis may bring a motion for resentencing, and may even get their convictions expunged, as it is now a misdemeanor offense, not a felony.<sup>35</sup>

This newfound recreational legality comes with certain limitations; the personal cultivation<sup>36</sup> of cannabis is subject to local city or county rules.<sup>37</sup> Note that a city or county cannot completely prohibit one from cultivating six cannabis plants inside a private residence or a structure located on the private residence that is fully enclosed and secure.<sup>38</sup> However, complete prohibition of the cultivation of six cannabis plants is warranted when the conduct is occurring outdoors on a private residence, unless the California Attorney General determines that such use is legal.<sup>39</sup> Moreover, retail purchases of cannabis or cannabis products are subject to state and local sales taxes.<sup>40</sup> If a customer has a valid medical cannabis card and a government-issued identification card, he is exempt

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<sup>31</sup> *Id.*

<sup>32</sup> HSC § 11362.1.

<sup>33</sup> *Id.*

<sup>34</sup> HSC § 11359.

<sup>35</sup> *Id.*; Jill Cowan, *Thousands of Californians Could Get Their Marijuana Convictions Cleared. But It's Complicated.*, N.Y. TIMES (Sept. 5, 2019), <https://www.nytimes.com/2019/09/05/us/marijuana-proposition-64-code-for-america.html>. Prosecutors will determine the eligibility under these motions on a case-by-case basis. *Id.*

<sup>36</sup> HEALTH & SAFETY § 11362.5. Medical cannabis cultivation is subject to the provisions established under the Compassionate Use Act of 1996. Health & Safety § 11362.5 *et seq.*

<sup>37</sup> Health & Safety § 11362.2.

<sup>38</sup> *Id.*

<sup>39</sup> *Id.*

<sup>40</sup> *Cannabis Tax Revenue Increases In 2nd Quarter of 2018: Rise Shows Compliance Trend Growing*, CAL. DEP'T OF TAX & FEE ADMIN. (Aug. 15, 2018), <https://www.cdtfa.ca.gov/news/18-41.htm> [hereinafter *Cannabis Tax Revenue Increases in 2nd Quarter of 2018*].



from the sales tax.<sup>41</sup> Furthermore, cannabis ingestion is prohibited 1,000 feet from a school while children are present<sup>42</sup> and where smoking tobacco is prohibited.<sup>43</sup> Similar to alcohol laws, one cannot possess an open container of cannabis or ingest cannabis while driving, operating, or riding in a motor vehicle.<sup>44</sup> One who commits any of the aforementioned violations is subject to penalties.<sup>45</sup>

While the youngest age to purchase medical cannabis is eighteen, recreational cannabis is limited to individuals who are twenty-one or older.<sup>46</sup> Thus, since individuals who are between eighteen and twenty-one can purchase medical cannabis, the penalties for recreational cannabis possession for those individuals are lesser than the penalties for those who are under eighteen. For those who are under eighteen who possess cannabis, they will be guilty of an infraction and required to complete drug education or counseling and community service.<sup>47</sup> For those between eighteen and twenty-one who are found with cannabis, they are likewise guilty of an infraction but must only pay a fine, up to \$100.<sup>48</sup>

## II. COMPLEXITIES FOR CALIFORNIANS SINCE 2018

### A. *Opening and Operating Cannabis Businesses*

Opening and operating a cannabis business in California has proven to be complicated. When starting a cannabis business, one must

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<sup>41</sup> *Tax Guide for Cannabis Businesses: Retailers*, CAL. DEP'T OF TAX & FEE ADMIN., <http://www.cdtfa.ca.gov/industry/cannabis.htm#Retailers> (last visited Oct. 7, 2019).

<sup>42</sup> The exception to this rule is if the ingestion is at a private residence and only if the ingestion is not detectable by others at such locations. Health & Safety § 11362.3(3).

<sup>43</sup> Health & Safety § 11362.3.

<sup>44</sup> *Id.*

<sup>45</sup> Health & Safety § 11362.4.

<sup>46</sup> *What Is the Age Limit of Medical Cannabis in California?*, AM. CANNABIS CO. (Sept. 18, 2018), <https://americancannabisconsulting.com/california-medial-cannabis-age-limit/>.

<sup>47</sup> Health & Safety § 11357(a)(1). For a first offense, one must “complete four hours of drug education or counseling and up to 10 hours of community service over a period not to exceed 60 days.” *Id.* For a second or subsequent offense, one must “complete six hours of drug education or counseling and up to 20 hours of community service over a period not to exceed 90 days.” *Id.*

<sup>48</sup> Health & Safety § 11357(a)(2).

first decide which type of business to pursue. There are many different types of cannabis businesses—there are the “key elements” of the industry, like cultivation and retail; logistical businesses; technology companies; and science-related businesses, like research and agriculture.<sup>49</sup> This section will only explore the cannabis businesses that newly transcended the California market when recreational legalization passed.

For all businesses “that touch the plant, licensing and permitting is essential.”<sup>50</sup> Once an individual decides which particular business to pursue, one must register with the Cannabis Department of Tax and Fee Administration (“CDTFA”) for a seller’s permit.<sup>51</sup> Cannabis business owners who make sales are required to obtain and maintain a seller’s permit as a prerequisite to being issued appropriate licenses from a State Department.<sup>52</sup> With the exception of testing laboratory licenses, all licenses must be clearly designated for medical use or commercial adult use.<sup>53</sup> Each license is valid for twelve months from its issuance and may be renewed annually.<sup>54</sup> The requirements for the different cannabis businesses will be discussed in turn.

### *1. Cultivator of Cannabis*

A cannabis cultivator is in the business of planting, growing, harvesting, drying, curing, grading or trimming cannabis.<sup>55</sup> In addition to the requirement of obtaining a seller’s permit, a cultivator must pay a cultivation tax to his distributor or manufacturer at a rate of \$9.25 per dry-weight ounce of cannabis flowers,<sup>56</sup> \$2.75 per dry-weight ounce of cannabis leaves,<sup>57</sup> and \$1.29 per ounce of fresh<sup>58</sup> cannabis plant, and must

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<sup>49</sup> Adam C. Uzialko, *How to Successfully Launch a Legal Cannabis Business*, BUSINESS.COM (May 31, 2019), <https://www.business.com/articles/legal-cannabis-industry-startup-business-guide/>.

<sup>50</sup> *Id.*

<sup>51</sup> *Cannabis Cultivator Tax Guide*, *supra* note 41.

<sup>52</sup> *Id.*

<sup>53</sup> Cal. Bus. & Prof. Code § 26050(b) (West 1979).

<sup>54</sup> Cal. Bus. & Prof. Code § 26050(c) (West 1979).

<sup>55</sup> *Cannabis Cultivator Tax Guide*, *supra* note 41.

<sup>56</sup> *Id.* Flower includes all dried flowers of the cannabis plant. *Id.*

<sup>57</sup> *Id.* Leaves include all other parts of the dried cannabis plant other than the flowers. *Id.*

<sup>58</sup> *Id.* Fresh category includes flowers, leaves, or a combination of adjoined flowers, leaves, stems, and stalks of the unprocessed fresh cannabis plant. *Id.* “To qualify for the ‘fresh’ plant category, the unprocessed cannabis must be weighed within two hours of harvesting.” *Id.*

follow invoicing requirements.<sup>59</sup> The cultivation tax applies to both medical and recreational cannabis, and applies when the cannabis “enters the commercial market.”<sup>60</sup> Beginning January 1, 2020, the CDFTA will be required to annually adjust the cultivation tax rates to account for inflation and will notify businesses of such adjustments.<sup>61</sup>

When becoming a cultivator of cannabis, one must precisely decide which type of cultivation from over a dozen options given under the Business and Professions Code.<sup>62</sup> A cultivator must decide between indoor, outdoor, mixed-light, cottage, or nurse, then choose whether he wishes to engage in small, medium, or large cannabis plants.<sup>63</sup> They must then apply for the license with the CalCannabis Cultivation Licensing division of the California Department of Food and Agriculture.<sup>64</sup> Additionally, cultivators may be subject to local city or county licenses and must contact the offices accordingly.<sup>65</sup>

## 2. *Manufacturer of Cannabis Products*

A cannabis manufacturer produces or prepares cannabis at one particular location, packages or repackages cannabis, or labels or relabels

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<sup>59</sup> *Id.* The invoice should identify the name of the licensee receiving the product, the cultivator’s name, the unique identifier for the cannabis, the cultivation tax amount, and the date of sale or transfer. *Id.*

<sup>60</sup> *Id.* “Cannabis ‘enters the commercial market’ when the cannabis or cannabis products, except for immature cannabis plants, clones, or seeds, have completed and comply with both the quality assurance review and testing as required in the Medicinal Adult-Use Cannabis Regulation and Safety Act.” *Id.* If the cannabis product does not pass testing, cannot be remediated, and does not enter the commercial market, a cultivator is entitled to the return of the cultivation tax from the distributor. The tax also applies to cannabis transferred or sold to a distributor that has not been tested if the licensing agency allows it. *Id.*

<sup>61</sup> *Cannabis Cultivator Tax Guide*, *supra* note 41. For updated tax rates, see *Tax Rates – Special Taxes and Fees*, CAL. DEP’T OF TAX & FEE ADMIN., <http://www.cdtfa.ca.gov/taxes-and-fees/tax-rates-stfd.htm> (last visited Oct. 7, 2019).

<sup>62</sup> Cal. Bus. & Prof. Code § 26050(a) (West 1979).

<sup>63</sup> *Id.*

<sup>64</sup> *Apply for a License*, CAL. CANNABIS PORTAL, <https://cannabis.ca.gov/apply-for-a-license/> (last visited Oct. 7, 2019).

<sup>65</sup> *Cannabis Cultivator Tax Guide*, *supra* note 41.

its container.<sup>66</sup> A manufacturer must register for a seller's permit.<sup>67</sup> Manufacturers must collect the cannabis cultivation tax from cultivators upon receipt of unprocessed cannabis, provide the cultivator with a receipt, and pay the cultivation tax to a distributor.<sup>68</sup> Even if a manufacturer does not make taxable cannabis sales, he is required to file a tax return indicating total sales with claimed non-taxable or exempt sales.<sup>69</sup>

A manufacturer must apply for a cannabis manufacturer license with the California Department of Public Health.<sup>70</sup> There are four main manufacturer licenses offered by the Department: Type 7 is for extraction using a volatile solvent, Type 6 is for extraction using a mechanical method or non-volatile solvent, Type N is for infusions, and Type P is only for packaging and labeling.<sup>71</sup> Like cultivators, manufacturers may be subject to local city or county licenses and must inquire.<sup>72</sup>

### 3. *Retailer or Dispensary Selling Cannabis or Cannabis Products*

A retailer sells cannabis directly to consumers.<sup>73</sup> A retailer must obtain a seller's permit, must charge and collect sales tax on each retail sale, and must charge and collect a fifteen percent cannabis excise tax<sup>74</sup>

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<sup>66</sup> *Tax Guide for Cannabis Businesses: Manufacturers*, CAL. DEP'T OF TAX & FEE ADMIN., <http://www.cdtfa.ca.gov/industry/cannabis.htm#Manufacturers> (last visited Oct. 7, 2019) [hereinafter *Cannabis Manufacturer Tax Guide*].

<sup>67</sup> *Id.*

<sup>68</sup> *Id.*

<sup>69</sup> *Id.*

<sup>70</sup> *Id.*

<sup>71</sup> *Manufactured Cannabis Safety Branch: Licensing FAQs*, CAL. DEP'T OF PUB. HEALTH, <https://www.cdph.ca.gov/Programs/CEH/DFDCS/MCSB/Pages/LicensingFAQs.aspx> (last visited Oct. 7, 2019). Each license is inclusive of the types that follow. There is a fifth license, Type S, for shared-use manufacturing facilities for businesses that alternate use of one manufacturing facility.

<sup>72</sup> *Cannabis Manufacturer Tax Guide*, *supra* note 66.

<sup>73</sup> *Tax Guide for Cannabis Businesses: Retailers*, CAL. DEP'T OF TAX AND FEE ADMIN., <http://www.cdtfa.ca.gov/industry/cannabis.htm#Retailers> (last visited Oct. 7, 2019) [hereinafter "Cannabis Retailer Tax Guide"].

<sup>74</sup> *Id.* This percentage is based on the "average market price" of the retail sale. The "average market price" is determined by the "type" of transaction that occurred when the product was sold. The "type" of transaction is either an "arm's length" or a "nonarm's length" transaction. "An 'arm's length' transaction is a sale that reflects the fair market price is the open market between two informed and willing parties, neither required to participate in the transaction. In an arm's length transaction, the average market price means the average retail price determined by the wholesale cost of the cannabis sold or transferred, plus a mark-up." A "nonarm's length" transaction is a sale that "does not reflect the fair

from customers who purchase cannabis.<sup>75</sup> This excise tax must then be paid to the distributor.<sup>76</sup>

A retailer must apply for a cannabis license by the Bureau of Cannabis Control within the California Department of Consumer Affairs.<sup>77</sup> A storefront retailer must obtain a Type 10 license, whereas a non-storefront retailer must obtain a Type 9 license—both must list their expected gross revenue on their application.<sup>78</sup> Most cities and counties have additional licensing requirements for cannabis retail businesses and retailers must check accordingly.<sup>79</sup>

#### 4. *Distributor of Cannabis or Cannabis Products*

A cannabis distributor procures, sells, or transports cannabis between licensed cannabis businesses.<sup>80</sup> In addition to obtaining a seller's permit, a distributor must obtain a cannabis tax permit.<sup>81</sup> A distributor must collect the cannabis cultivation tax from cannabis cultivators and manufacturers, must collect the cannabis excise tax from the cannabis retailers he supplies the cannabis to, and provide an invoice to the businesses from whom he collects these taxes.<sup>82</sup>

A distributor of cannabis must obtain a distributor license from the Bureau of Cannabis Control<sup>83</sup>—he must apply for a Type 11 license,

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market price in the open market or is not between two informed and willing parties, neither required to participate in the transaction . . . In a nonarm's length transaction, the average market price means the cannabis retailer's gross receipts from the retail sale of the cannabis or cannabis products." *Id.*

<sup>75</sup> *Id.*

<sup>76</sup> *Id.*

<sup>77</sup> *Id.*

<sup>78</sup> *Id.* The license fees range from \$2,500 to \$96,000, depending on gross expected revenue. See *Medical Marijuana Dispensary Laws: Fees and Taxes*, MPP, [https://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=1&ved=2ahUKEwjzay69o\\_1AhW7GDQIHR\\_ZDwgQFjAAegQIABAC&url=https%3A%2F%2Fwww.mpp.org%2Fassets%2Fcomponents%2Ffileattach%2Fconnector.php%3Faction%3Dweb%2Fdownload%26ctx%3Dweb%26fid%3DuO5rmagKkw8VnvXEclnRJ6AELUmXZbr&usg=AOvVaw2Hlan6V2H7-9TA\\_q8Tiefg](https://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=1&ved=2ahUKEwjzay69o_1AhW7GDQIHR_ZDwgQFjAAegQIABAC&url=https%3A%2F%2Fwww.mpp.org%2Fassets%2Fcomponents%2Ffileattach%2Fconnector.php%3Faction%3Dweb%2Fdownload%26ctx%3Dweb%26fid%3DuO5rmagKkw8VnvXEclnRJ6AELUmXZbr&usg=AOvVaw2Hlan6V2H7-9TA_q8Tiefg) (last visited Oct. 7, 2019).

<sup>79</sup> Cannabis Retailer Tax Guide, *supra* note 73.

<sup>80</sup> Cannabis Distributor Tax Guide, *supra* note 61.

<sup>81</sup> *Id.*

<sup>82</sup> *Id.*

<sup>83</sup> *Id.*

or if he wishes to transport only, a Type 13 license.<sup>84</sup> The license fee is determined by the distributor's expected gross revenue.<sup>85</sup>

### 5. *Microbusiness*

A microbusiness is encompassing of the categories mentioned above. A microbusiness license allows the cultivation of cannabis on an area less than 10,000 square feet, distribution of cannabis, manufacturing of cannabis under a Type 6 license,<sup>86</sup> and the retail sale of cannabis.<sup>87</sup> A microbusiness must engage in at least three of these four activities to obtain a license from the Bureau of Cannabis Control.<sup>88</sup> Like distributors, microbusinesses must apply not only for a seller's permit but also for a cannabis tax permit.<sup>89</sup>

### 6. *Testing Laboratory*

A testing laboratory must apply for a testing laboratory license with the Bureau of Cannabis Control.<sup>90</sup> A testing laboratory is the sole cannabis business that cannot hold another cannabis license, and testing laboratory owners cannot employ an individual employed by any other licensee that does not hold a testing license.<sup>91</sup> Thus, there is no vertical integration for testing laboratories. Like all other cannabis businesses, testing laboratories must obtain a seller's permit.<sup>92</sup> Moreover, testing laboratories must obtain ISO/IEC 17025 accreditation<sup>93</sup> prior to obtaining

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<sup>84</sup> *Cannabis Distributor License Application*, BUREAU OF CANNABIS CONTROL, [https://bcc.ca.gov/clear/distributor\\_application.pdf](https://bcc.ca.gov/clear/distributor_application.pdf) (last updated Aug. 2019).

<sup>85</sup> *Id.* The license fee ranges from \$1,500 to \$240,000 under both Distributor Type 11 and Distributor-Transport Only Type 13, but for Distributor-Transport Only Self-Transport Type 13, the fee ranges from \$200 to \$1,000.

<sup>86</sup> *Manufactured Cannabis Safety Branch: Licensing FAQs*, *supra* note 71. Type 6 is for extraction using a mechanical method or non-volatile solvent.

<sup>87</sup> *Microbusinesses*, BUREAU OF CANNABIS CONTROL, <https://bcc.ca.gov/licensees/microbusinesses.html> (last visited Oct. 7, 2019).

<sup>88</sup> *Id.*

<sup>89</sup> *Tax Permits*, CAL. CANNABIS PORTAL, <https://cannabis.ca.gov/tax-permits/> (last visited Oct. 7, 2019).

<sup>90</sup> *Id.*

<sup>91</sup> Bus. & Prof. Code § 26053(b).

<sup>92</sup> *Instructions for Completing the Cannabis Testing Laboratory Application*, BUREAU OF CANNABIS CONTROL [https://bcc.ca.gov/clear/testing\\_lab\\_instructions.pdf](https://bcc.ca.gov/clear/testing_lab_instructions.pdf) (last updated Feb. 2019).

<sup>93</sup> *Id.* "Acceptable accreditation must attest to the laboratory's competence to perform testing of the following: [c]annabinoids, heavy metals,

a license, and must provide standard operating procedures for different testing methods, sample preparation, and sampling.<sup>94</sup> Some laboratories may be issued a provisional license prior to obtaining ISO/IEC 17025 accreditation so long as the applicant provides all standard operating procedures.<sup>95</sup>

*B. Overarching Takeaway from the Different Cannabis Business*

*Requirements*

Now that all the different types of licenses have been laid out, there is a better understanding of which requirements must be met before California government agencies will issue permits and licenses. When one decides to own or operate a cannabis business, or when one wants to fully understand what California cannabis legality truly means, however, state requirements are only one layer of rules to abide by. Other relevant laws, and how they conflict with California law, are discussed in turn.

*C. Difficulties in Opening and Operating Cannabis Businesses:*

*Laws Conflicting with California Law*

Since many medical cannabis businesses were open and operated prior to 2018, the Legislature created a temporary license which was issued until December 31, 2018.<sup>96</sup> These temporary licenses had fewer requirements than annual licenses—to quickly process applications to allow these businesses to continue to operate.<sup>97</sup> Thus, businesses that operated prior to 2018 seemingly had initial licensing priority. However, according to New Frontier Data,<sup>98</sup> in order for a temporary license to be

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microbial impurities, mycotoxins, residual pesticides, residual solvents and processing chemicals and terpenoids (if tested).”

<sup>94</sup> *Id.*

<sup>95</sup> *Id.*

<sup>96</sup> *California Cannabis Advisory Committee: 2018 Annual Report*, BUREAU OF CANNABIS CONTROL, [https://www.bcc.ca.gov/about\\_us/documents/cac\\_annual\\_report\\_2018.pdf](https://www.bcc.ca.gov/about_us/documents/cac_annual_report_2018.pdf) (last visited Oct. 7, 2019).

<sup>97</sup> *Id.*

<sup>98</sup> New Frontier Data is an analyst firm that tracks cannabis sales and trends.

granted, businesses had to first have a local license.<sup>99</sup> There is currently a large conflict between local and state laws as most cities decided to ban cannabis shops, and many residents complained that cannabis businesses are a nuisance.<sup>100</sup> Therefore, the main issues which arise when one decides to own and operate a cannabis business are the general state limitations on the issuance permits and licenses and the furtherance of such limitations due to the conflict between state and local laws.

### 1. *General State Limitations on Permits and Licenses*

There are many limitations on how many permits and licenses a cannabis business can apply for. “California’s three cannabis licensing authorities will not issue state licenses to individuals or commercial operations inside a city or county which has banned cultivation, manufacturing, [sic] or dispensing of cannabis, [sic] or cannabis-related products.”<sup>101</sup> Although California’s three licensing authorities have not limited the number of cannabis licenses they issue, cities and counties may place limitations with which businesses and individuals must comply.<sup>102</sup>

### 2. *The Conflict Between State and Local Laws*

As noted above, California’s cannabis law allows each city or county to decide where cannabis is allowed, or if it is allowed at all.<sup>103</sup> As of February 2019, only one-third of California’s cities, 161 of 482, and less than one-half of California’s counties, 24 of 58, “opted to allow commercial cannabis activity of *any sort*.”<sup>104</sup> It is important to note that

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<sup>99</sup> J.J. McCoy, *Lessons from California, Part 2: Licensing and Compliance Issues*, NEW FRONTIER DATA (Feb. 18, 2018), <https://newfrontierdata.com/marijuana-insights/lessons-california-part-2-licensing-compliance-issues/>.

<sup>100</sup> Patrick McGreevy, *One year of legal pot sales and California doesn’t have the bustling industry it expected. Here’s why*, L.A. TIMES (Dec. 27, 2018 12:05 A.M.), <https://www.latimes.com/politics/la-pol-ca-marijuana-year-anniversary-review-20181227-story.html#nws=mcnewsletter>.

<sup>101</sup> *Frequently Asked Questions*, CAL. CANNABIS PORTAL, <https://cannabis.ca.gov/faqs/> (last visited Oct. 7, 2019).

<sup>102</sup> *Id.*

<sup>103</sup> Brooke Staggs, *Legalizing Marijuana was Supposed to Slow Illegal Activity in California. It Hasn’t*, THE ORANGE COUNTY REGISTER (Nov. 30, 2018), <https://www.ocregister.com/2018/11/30/has-legal-weed-boosted-californias-illicit-operators-so-far-yes/>.

<sup>104</sup> John Schroyer & Eli McVey, *Chart: Most California Municipalities Ban Commercial Cannabis Activity*, MARIJUANA BUSINESS DAILY (Feb. 18,



some of these cities and counties may only allow one type of cannabis business.<sup>105</sup> For example, as of January 31, 2019, only three of Los Angeles County's eighty-nine cities allow the operation of all six cannabis businesses discussed above.<sup>106</sup> Another example of these limitations can be seen in Riverside County, where the legal recreational cannabis movement took approximately a year and a half to transcend into the county's borders.<sup>107</sup> Moreover, many cities in California only allow people to apply for a license or permit once a quarter through a lottery-type basis or a first-come-first-serve basis. Nevertheless, some cities transcended from this selection process and imposed merit-based selection processes.<sup>108</sup>

### 3. *Solutions to State and Local Limitations*

In order to counter the majority of California's local governments' reluctance to permit the operation of cannabis businesses, in February 2019, the legislature introduced Assembly Bill 1356.<sup>109</sup> The Bill, if passed, requires local jurisdictions to issue a specific number of minimum licenses, but only if more than 50% of voters from that jurisdiction voted in favor of Proposition 64.<sup>110</sup> The Bill allows such jurisdictions to place a

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2019), <https://mjbizdaily.com/chart-most-of-california-municipalities-ban-commercial-cannabis-activity/> (emphasis added).

<sup>105</sup> *Id.*

<sup>106</sup> Brook Staggs, *What are the Marijuana Laws in Your California City? Explore Our Database of Local Cannabis Policies*, THE ORANGE COUNTY REGISTER (Jan. 3, 2018), <https://www.ocregister.com/2018/01/03/what-are-the-marijuana-laws-in-your-california-city-explore-our-database-of-local-cannabis-policies-2/>.

<sup>107</sup> Sam Metz, *Riverside County Issues First 69 Permit Recommendations for Cannabis Businesses in Unincorporated Areas*, DESERT SUN (July 5, 2020), <https://www.desertsun.com/story/news/politics/2019/07/05/riverside-county-issues-first-permits-cannabis-retail-and-cultivation/1639354001/>.

<sup>108</sup> *Mayors & Council Members Advanced Leadership Workshops: Cannabis Regulation: Best Practices For Your City*, 15 (June 21, 2019), <https://www.cacities.org/Resources-Documents/Education-and-Events-Section/MCMALW/2019-Session-Materials/Cannabis-Regulation-Workbook>.

<sup>109</sup> The Times Editorial Board, *Editorial: California Lawmakers Already Want to Roll Back a Key Promise of Marijuana Legalization*, LOS ANGELES TIMES (May 18, 2019), <https://www.latimes.com/opinion/editorials/la-ed-marijuana-legalization-proposition-64-local-bans-20190518-story.html>.

<sup>110</sup> *Assembly Bill 1356 Cannabis: Local Jurisdictions: Retail Commercial Cannabis Activity*, CALIFORNIA LEGISLATIVE INFORMATION (May

limitation on the number of licenses issued by having more than 50% of the voters voting in favor of the limitation.<sup>111</sup> However, this Bill creates an issue because it contradicts Proposition 64's promise of local control.<sup>112</sup> Yet, if this Bill passes, it solves some of the contradictory state and local cannabis laws.

Once local bans on cannabis businesses are lessened and obtaining the requisite permits and licenses becomes simpler, the regulation of cannabis sales, discussed in Section V *infra*, and combatting the illicit cannabis market, discussed in Section VI *infra*, will become easier. The issue of federal cannabis illegality, however, remains prevalent. Until the federal government gives full deference to the states with regard to all cannabis-related laws and regulations, regulation of sales and the illicit cannabis market remains at issue and there will be a perpetual gray-area regarding the issues discussed below.

### III. FEDERAL ILLEGALITY

Under Article VI of the Constitution, federal law preempts state law.<sup>113</sup> The Supremacy Clause holds that the “laws of the United States shall be . . . the supreme law of the land.”<sup>114</sup> The Supreme Court of the United States found preemption when state laws conflict with federal law, “including when they stand as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress.”<sup>115</sup> The concern that many people have with regard to the cannabis industry stems from this notion of preemption. Does the fact that cannabis is illegal federally trump the fact that cannabis is legal in California?

#### A. *Ethical Issues for Attorneys*

Because cannabis is illegal federally, there is an ethical issue for attorneys as to whether they should comply with the ABA Model Rules of Professional Conduct while advising clients on cannabis business ventures.<sup>116</sup> ABA Rule 1.2(d) states that a lawyer “shall not counsel a

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17,2019), [https://leginfo.legislature.ca.gov/faces/billNavClient.xhtml?bill\\_id=201920200AB1356](https://leginfo.legislature.ca.gov/faces/billNavClient.xhtml?bill_id=201920200AB1356).

<sup>111</sup> *Id.*

<sup>112</sup> The Times Editorial Board, *supra* note 109.

<sup>113</sup> U.S. CONST. amend. VI.

<sup>114</sup> *Id.*

<sup>115</sup> *Arizona v. U.S.*, 567 U.S. 387, 399 (2012).

<sup>116</sup> *Conflicting State and Federal Marijuana Laws Create Ethical Complications for Lawyers*, AMERICAN BAR ASS'N (Sept. 17, 2014),

client to engage, or assist a client, in conduct that the lawyer knows is criminal or fraudulent.”<sup>117</sup> States are split on whether advising clients on a federally illegal field violates Rule 1.2; however, all jurisdictions agree that attorneys must advise their clients about federal law.<sup>118</sup> The ABA noted that the jurisdictions approving of lawyers assisting clients in the cannabis industry relied, in part, on a 2013 memo from the U.S. Department of Justice.<sup>119</sup>

On August 29, 2013, the U.S. Department of Justice updated its federal cannabis enforcement policy.<sup>120</sup> The Department noted that for states that have enacted laws to authorize the production, distribution and possession of cannabis—so long as the states establish a strict regulatory system—the Department would defer its right to challenge their legalization laws.<sup>121</sup> On January 4, 2018, however, the Department rescinded this and other updates to its federal cannabis enforcement policies and established that, in deciding which cannabis activities to prosecute, “prosecutors should follow the well-established principles that govern all federal prosecutions.”<sup>122</sup> Thus, it seems that advising clients on engaging in cannabis businesses runs afoul to Rule 1.2. Nonetheless, many states modified the provisions of this rule.<sup>123</sup>

In California, Model Rule 1.2.1 reads the same as ABA Model Rule 1.2, but includes a subsection (b), reading “a lawyer may: (1) discuss

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[https://www.americanbar.org/news/abanews/aba-news-archives/2014/03/conflicting\\_statean/](https://www.americanbar.org/news/abanews/aba-news-archives/2014/03/conflicting_statean/).

<sup>117</sup> *Id.*

<sup>118</sup> Stephen Carr, *Ethics Board Advises Attorneys to Avoid Medical Marijuana Clients*, AMERICAN BAR ASS’N (Nov. 21, 2016), <https://www.americanbar.org/groups/litigation/publications/litigation-news/top-stories/2016/ethics-board-advises-attorneys-to-avoid-medical-marijuana-patients/>.

<sup>119</sup> *Id.*

<sup>120</sup> *Justice Department Announces Update to Marijuana Enforcement Policy*, U.S. DEP’T OF JUSTICE (Aug. 29, 2013), <https://www.justice.gov/opa/pr/justice-department-announces-update-marijuana-enforcement-policy>.

<sup>121</sup> *Id.*

<sup>122</sup> U.S. Dep’t of Justice, *Memorandum for all United States Attorneys: Marijuana Enforcement* (Jan. 4, 2018), <https://www.justice.gov/opa/press-release/file/1022196/download>.

<sup>123</sup> *Advising Clients on Marijuana Use, Sale*, AMERICAN BAR ASS’N (Oct. 30, 2017), <https://www.americanbar.org/news/abanews/publications/youraba/2017/november-2017/the-ethical-landmines-surrounding-advising-clients-about-marijua/>.

the legal consequences of any proposed course of conduct with a client; and (2) counsel or assist a client to make a good faith effort to determine the validity, scope, meaning, or application of a law . . . .”<sup>124</sup> Comment 6 clarifies this provision by stating that when there is a conflict between California and federal law, “the lawyer may assist a client in drafting or administering, or interpreting or complying with, California laws . . . even if the client’s actions might violate the conflicting federal” law.<sup>125</sup> However, a lawyer must advise his or her client about related federal law.<sup>126</sup> A public comment argued in favor of adding an explicit medical cannabis rule, but the Commission rejected adding such a rule.<sup>127</sup> Presently, therefore, ethical issues for attorneys arising when advising clients on cannabis-related businesses remains a gray area.

### B. Criminal Liability

Before its rescission in January 2018, former President Barack Obama implemented a policy that allowed state laws regarding cannabis use to trump federal law.<sup>128</sup> Does this rescission mean that cannabis possession subjects individuals to federal criminal liability even though cannabis is legal in California?

It is important to note that the Controlled Substances Act does not recognize a difference between medical and recreational use of cannabis, as “Congress expressly found that the drug has no acceptable medical uses.”<sup>129</sup> Thus, having a medical cannabis card is irrelevant when it comes to federal prosecution. The federal government is primarily interested in prosecuting large-scale traffickers and organized crime participants.<sup>130</sup> In fact, in 2018, President Trump publicly announced his support for states

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<sup>124</sup> The State Bar of California, Model Rule 1.2.1 Advising or Assisting the Violation of Law [http://www.calbar.ca.gov/Portals/0/documents/rules/Rule\\_1.2.1-Exec\\_Summary-Redline.pdf](http://www.calbar.ca.gov/Portals/0/documents/rules/Rule_1.2.1-Exec_Summary-Redline.pdf).

<sup>125</sup> *Id.*

<sup>126</sup> *Id.*

<sup>127</sup> *Id.*

<sup>128</sup> Robert J. MacCoun, *State Marijuana Laws at Odds with Federal Enforcement*, STAN. L. SCH. BLOG (Jan. 9, 2018), <https://law.stanford.edu/2018/01/09/state-marijuana-laws-at-odds-with-federal-enforcement/>.

<sup>129</sup> *Gonzales v. Raich*, 545 U.S. 1, 27 (2005).

<sup>130</sup> *California Marijuana Laws Explained by Criminal Defense Lawyers*, SHOUSE CALIFORNIA L.GROUP, <https://www.shouselaw.com/marijuana.html> (last visited Oct. 7, 2019); see also *Answers to Frequently Asked Questions About Marijuana*, OFF. OF NAT’L DRUG CONTROL POL’Y, <https://obamawhitehouse.archives.gov/ondcp/frequently-asked-questions-and-facts-about-marijuana> (last visited Oct. 7, 2019).

deciding the issue of cannabis legalization themselves.<sup>131</sup> Therefore, it seems unlikely that personal cultivation or usage subjects an individual to criminal liability.<sup>132</sup> The possession of cannabis on federal property, however, including both THC and CBD, increases one's likelihood of being subject to criminal sanctions.<sup>133</sup> Overall, federal prosecution will likely occur in cases of cultivation, possession, or distribution where the government could seize large amounts of cannabis.<sup>134</sup>

In September 2019, the Food and Drug Administration ("FDA") issued consumer updates regarding CBD because the topic of CBD's legality seems to be a gray-area.<sup>135</sup> The FDA recognized that CBD is widespread throughout the United States and is "working to answer questions about the science, safety, and quality of products" containing CBD.<sup>136</sup> It is important to recognize that if the FDA finds that CBD products are safe,<sup>137</sup> federal criminal liability will likely become more narrowly construed to apply only to THC.

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<sup>131</sup> Daniel B. Pasternak, *Three New State Laws Legalize Marijuana Use, Sparking More Confusion and Igniting Further Conflict With Federal Law*, THE NAT'L L. REV. (Nov. 21, 2018), <https://www.natlawreview.com/article/three-new-state-laws-legalize-marijuana-use-sparking-more-confusion-and-igniting>.

<sup>132</sup> *Id.*

<sup>133</sup> *California Cannabis Laws*, CALIFORNIA NORML, [http://www.canorml.org/california\\_cannabis\\_laws](http://www.canorml.org/california_cannabis_laws) (last visited Oct. 7, 2019).

<sup>134</sup> *Federal Marijuana Law*, AMERICANS FOR SAFE ACCESS, [https://www.safeaccessnow.org/federal\\_marijuana\\_law](https://www.safeaccessnow.org/federal_marijuana_law) (last visited Oct. 7, 2019).

<sup>135</sup> See Laura Reiley, *CBD-infused Food and Beverages are Still Illegal Under U.S. law. So Why are They Everywhere?*, THE WASHINGTON POST (June 24, 2019), <https://www.washingtonpost.com/business/2019/06/24/cbd-infused-food-beverages-are-still-illegal-under-us-law-so-why-are-they-everywhere/> (discussing the widespread presence of CBD-infused food and beverages which are currently in big-box grocery stores across the country).

<sup>136</sup> *What You Need to Know (And What We're Working to Find Out) About Products Containing Cannabis or Cannabis-derived Compounds, Including CBD*, U.S. FOOD & DRUG ADMIN., <https://www.fda.gov/consumers/consumer-updates/what-you-need-know-and-what-were-working-find-out-about-products-containing-cannabis-or-cannabis> (last visited Oct. 7, 2019).

<sup>137</sup> *Id.* The FDA is working to ensure that CBD would not negatively affect the body when ingested or used for a long period of time, and to ensure that CBD will not harm "special populations (e.g., the elderly, children, adolescents, pregnant and lactating women) or types of animals. . . ."

### C. *Lawful Cannabis Usage and Employer Accommodation*

Because cannabis remains illegal under federal law, employers have no duty to accommodate for medical cannabis use.<sup>138</sup> Over one decade ago, the California Supreme Court heard a case wherein the plaintiff alleged that his employer violated the California Fair Employment and Housing Act (“FEHA”) and the Compassionate Use Act of 1996<sup>139</sup> for firing him when he failed a cannabis test.<sup>140</sup> Under the FEHA, it is unlawful

for an employer, because of the . . . physical disability, mental disability, [or] medical condition . . . of any person, to refuse to hire or employ the person . . . or to bar or to discharge the person from employment . . . or to discriminate against the person in compensation or in terms, conditions, or privileges of employment.<sup>141</sup>

An employer may refuse

to hire or discharge[e] an employee with a physical or mental disability . . . if the employee, because of a physical or mental disability, is unable to perform the employee’s essential duties [or cannot perform those duties in a manner that would not endanger the employee’s health or safety or the health or safety of others] even with reasonable accommodations . . . .<sup>142</sup>

In *Ross v. Ragingwire Telecommunications, Inc.*, the plaintiff used medical cannabis to treat the pain derived from his physical disability—he suffered from lower back strain and had muscle spasms in his back.<sup>143</sup> The plaintiff likened the usage of insulin to the usage of medical cannabis, arguing that just as the FEHA would be violated for an employer to terminate an employee for using insulin, his employer violated the FEHA

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<sup>138</sup> C. California Fair Employment and Housing Act (FEHA), Cal. Prac. Guide Employment Litigation Ch. 9-C.

<sup>139</sup> See *supra* Part I. *The Compassionate Use Act* exempted patients who possessed medical cannabis from criminal prosecution or sanctions.

<sup>140</sup> *Ross v. Ragingwire Telecommunications, Inc.*, 174 P.3d 200 (Cal. 2008).

<sup>141</sup> Cal. Gov’t Code § 12940(a).

<sup>142</sup> Cal. Gov’t Code § 12940(a).

<sup>143</sup> 174 P.3d at 204.

by terminating him for using medical cannabis.<sup>144</sup> The Court inferred from the plaintiff's allegation that he asked his employer to accommodate his medical cannabis use at home by waiving its drug test policy.<sup>145</sup> The Court held that because cannabis is still federally illegal, "[t]he FEHA does not require employers to accommodate the use of illegal drugs," even if the use is occurring at home.<sup>146</sup>

The same reigns true despite the legalization of medical and recreational cannabis usage—employers may drug test and discharge employees for positive cannabis drug tests.<sup>147</sup> Proposition 64 does not alter

[t]he rights and obligations of public and private employers to . . . require an employer to permit or accommodate the use, consumption, [or] possession . . . of cannabis in the workplace, or affect the ability of employers to have policies prohibiting the use of [cannabis] by employees . . . or prevent employers from complying with state or federal law.<sup>148</sup>

Despite the fact that California has not implemented employment protection statutes governing accommodation of medical cannabis use, many states<sup>149</sup> have done so.<sup>150</sup> Specifically, for example, in Connecticut and Rhode Island, it is important to note that both federal district courts upheld these statutes, finding no preemption.<sup>151</sup> However, no states passed

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<sup>144</sup> *Id.*

<sup>145</sup> *Id.*

<sup>146</sup> *Id.*

<sup>147</sup> C. California Fair Employment and Housing Act (FEHA), Cal. Prac. Guide Employment Litigation Ch. 9-C, *supra*, note 138.

<sup>148</sup> H.S.A. § 11362.45(f).

<sup>149</sup> See Rebecca Stephens, *In the Weeds: Marijuana Legalization & Employment Laws*, JD SUPRA (July 29, 2019), <https://www.jdsupra.com/legalnews/in-the-weeds-marijuana-legalization-28936/> (noting that Arizona, Connecticut, Delaware, Illinois, Minnesota, Nevada, New York and Rhode Island have implemented such statutes).

<sup>150</sup> Dean Rocco & Noelle Sheehan, *Weed at Work: Must Employers Accommodate Medical Use?*, SHRM (Feb. 13, 2019), <https://www.shrm.org/resourcesandtools/legal-and-compliance/state-and-local-updates/pages/must-employers-accommodate-medical-marijuana.aspx>.

<sup>151</sup> Stephens, *supra* note 149.

legislation that permits employees to possess cannabis, or be under the influence of cannabis, at the workplace.<sup>152</sup>

On February 7, 2018, California's legislature introduced Assembly Bill No. 2069 to amend the current employment discrimination laws regarding medical cannabis use.<sup>153</sup> The bill, if approved, "would require employers to reasonably accommodate medical cannabis use for the treatment of a known" disability or condition.<sup>154</sup> Thus, as the bill is making its way through the legislature, it is likely that California will approve the bill or implement a similar provision pertaining to accommodation of medical cannabis use in the near future. As to recreational cannabis use and anti-discrimination statutes, this is still a highly debated issue in the states.

#### *D. Lawful Cannabis Usage and Child Custody*

Similar to the cannabis-related issues that arise in the employment context, as discussed above, medical cannabis users may face the same issues when it comes to child custody. The "use of medical [cannabis], without more, cannot support a jurisdiction finding that brings [a] minor[] within the jurisdiction of the dependency court. . . ."<sup>155</sup> Smoking cannabis outside of a child's presence will not place a child under the dependency jurisdiction of the court.<sup>156</sup> Ultimately, the court found that "the mere use of [cannabis] by a parent will not support finding a risk to minors . . . [but] [t]here is a risk to [] children of the negative effects of secondhand [cannabis] smoke."<sup>157</sup> While most of the cases concerning cannabis usage pertain to medical cannabis use, it appears that the same would reign true for recreational cannabis usage. Because "[t]he law's primary concern is the protection of children,"<sup>158</sup> it is apparent that using cannabis, so long as it is outside of the presence of children and does not negatively impact the children, is permitted. Therefore, unlike the cannabis-related issues that arise under the employment context, cannabis usage and child custody seem to be more reasonable and forgiving given the state cannabis laws.

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<sup>152</sup> Pasternak, *supra* note 131.

<sup>153</sup> *Medicinal cannabis: employment discrimination*, California Assembly Bill 2069, California Legislative Information (2017-2018), [https://leginfo.legislature.ca.gov/faces/billTextClient.xhtml?bill\\_id=201720180\\_AB2069](https://leginfo.legislature.ca.gov/faces/billTextClient.xhtml?bill_id=201720180_AB2069).

<sup>154</sup> Stephens, *supra* note 149.

<sup>155</sup> *In re Drake M.*, 211 Cal. App. 4th 754, 764 (2012).

<sup>156</sup> *Id.* at 768.

<sup>157</sup> *In re Alexis E.*, 171 Cal. App. 4th 438, 452 (2009).

<sup>158</sup> *In re I.A.*, 201 Cal. App. 4th 1484, 1491 (2011).



## IV. FINANCING FOR OWNING AND OPERATING A CANNABIS

## BUSINESS

Obtaining the requisite permits and licenses is a very costly venture. For businesses “that touch the plant,” like cultivators and dispensaries, they “should be prepared to spend between \$150,000 and \$200,000 navigating the [licensing] process . . . .”<sup>159</sup> In addition to the costly licenses and permits, most businesses need funding to open storefronts, grow houses, or other commercial real estate. Moreover, businesses need to consider the costs associated with procuring product or the tools to make the product, marketing, hiring employees, testing, any necessary technology, and other relevant costs. For most, securing financing will be necessary and immensely difficult.

The continual federal illegality of cannabis, discussed in more detail in the *Federal Illegality* Section IV *supra*, is a source of this difficulty in securing financing for cannabis businesses. The majority of the banks giving out small business loans are subject to federal laws which presents this difficulty.<sup>160</sup> “Many banks are hesitant to do business with cannabis-related companies, while others refuse outright.”<sup>161</sup> Working with companies that are engaged in federally illegal activities “opens the bank up to additional oversight and liability” and there is a concern that “a federal crackdown could result in seized assets and a business catastrophe.”<sup>162</sup> Likewise, lines of credit and business loans are difficult to secure.<sup>163</sup>

It is probable, however, that banks will no longer be subject to federal penalizations for financing cannabis businesses. On September 25, 2019, the House of Representatives passed legislation which would protect

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<sup>159</sup> Uzialko, *supra* note 49.

<sup>160</sup> Georgia McIntyre, *How to Start a Marijuana Business: The Ultimate Guide*, FUNDERA <https://www.fundera.com/blog/marijuana-business> (last updated Sept. 4, 2019).

<sup>161</sup> Uzialko, *supra* note 49.

<sup>162</sup> *Id.*

<sup>163</sup> Adam C. Uzialko, *The State of Finance in the Legal Cannabis Industry*, BUSINESS NEWS DAILY (June 9, 2017), [https://www.businessnewsdaily.com/10002-finance-legal-cannabis-industry-trends.html?\\_ga=2.160140029.1127203204.1567647903-1169299143.1567647899](https://www.businessnewsdaily.com/10002-finance-legal-cannabis-industry-trends.html?_ga=2.160140029.1127203204.1567647903-1169299143.1567647899).

banks<sup>164</sup> who finance cannabis businesses in states where cannabis is legal.<sup>165</sup> If the Senate likewise passes this legislation, this legislation will take effect sometime in the near future and will protect the relationship between banks and cannabis businesses.<sup>166</sup> Although this legislation is a step in the right direction, it is narrowly construed and thus certain limitations remain in place. The legislation does not clearly dictate whether the large United States banks will be able to lend to the cannabis industry, “partly because of logistical hurdles to ensure money doesn’t flow through states where [cannabis] remains illegal . . . .”<sup>167</sup> The solution to this issue would be to apply this legislation to all the states, not only the states which legalized cannabis, but such a solution will run afoul of the policy interest of ensuring money does not reach states where cannabis is illegal. Until a solution arises, which can reasonably track where the banks’ money is going, this legislation will likely not extend to all the states.

Traditional financing methods are not the only financing options that are available presently, however. Angel investors and venture capital firms are other possibilities to look to when searching for financing.<sup>168</sup> Some companies received financing from Canadian investment funds as well.<sup>169</sup> Another option is to go through Canopy, a company which provides capital and knowledge in return for a small stake in the cannabis business.<sup>170</sup> Thus, although it is not the easiest journey to procure funding for a cannabis business venture, there are some methods which starters of a cannabis business could look to which will raise the capital they seek. Financing cannabis business ventures will likely become simpler in the coming years which would drastically change the industry, enabling a shift

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<sup>164</sup> This legislation also expands to mainstream companies that transact with cannabis businesses “in the regular course of business, such as landlords, insurers and electricians.” Andrew Ackerman, *Mainstream Companies Back Marijuana Banking*, THE WALL STREET JOURNAL (Mar. 26, 2019), [https://www.wsj.com/articles/mainstream-companies-back-marijuana-banking-11553608802?mod=article\\_inline](https://www.wsj.com/articles/mainstream-companies-back-marijuana-banking-11553608802?mod=article_inline).

<sup>165</sup> H.R. 1595, 116th Cong. (2019); Jesse Naranjo, *House Passes Bill to Protect Banking for Marijuana Businesses*, THE WALL STREET JOURNAL (Sept. 25, 2019), <https://www.wsj.com/articles/house-passes-bill-to-protect-banking-for-marijuana-businesses-11569447960>. The House passed this Bill with approximately a 75% majority vote.

<sup>166</sup> Naranjo, *supra* note 165. This legislation will also “require[] federal regulators to issue guidance to financial institutions regarding hemp . . . and businesses that sell hemp-derived cannabidiol, or CBD . . . .”

<sup>167</sup> Ackerman, *supra* note 164.

<sup>168</sup> Uzialko, *supra* note 49.

<sup>169</sup> Uzialko, *supra* note 163.

<sup>170</sup> *Id.*

from the current primarily cash-based cannabis industry.<sup>171</sup> This, in turn, will aid in the combat against the illicit cannabis market discussed in Part VI, *infra*.

#### V. REGULATION OF CANNABIS SALES

The recreational legalization of cannabis was largely supported by a high expectation of tax revenue in California. The expected sales tax revenue for 2018 was \$1 billion.<sup>172</sup> In reality, the tax revenue totaled approximately a third of that, amassing about \$340 million.<sup>173</sup> In 2019, there has been a gradual increase in tax revenue thus far, but the figures remain to be far below the expected threshold.<sup>174</sup> California collected \$74 million from April through June in cannabis excise taxes, over a 20% increase from the \$61 million collected from January through March.<sup>175</sup> This amount is dismal compared to the expected \$1 billion in tax revenue for 2018. At this rate, in 2019, California will likely collect roughly the same amount as it did in 2018, projecting to collect \$355 million in 2019 and \$514 million in 2020.<sup>176</sup>

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<sup>171</sup> Ackerman, *supra* note 164.

<sup>172</sup> Brooke Staggs, *California Made \$345 million, Not Predicted \$1 Billion, on Legal Cannabis in 2018*, THE ORANGE COUNTY REG. (Feb. 19, 2019), <https://www.ocregister.com/2019/02/19/california-made-345-million-not-predicted-1-billion-on-legal-cannabis-in-2018/>.

<sup>173</sup> *Cannabis Tax Revenue Increases in 2<sup>nd</sup> Quarter of 2018*, *supra* note 40. The industry generated \$60.9 million in the first quarter, \$74.2 million in the second, \$100.8 million in the third, and \$103.3 million in the fourth. *California Department of Tax and Fee Administration Reports Cannabis Tax Revenues for Fourth Quarter of 2018*, CAL. CANNABIS PORTAL (Feb. 19, 2019), <https://cannabis.ca.gov/2019/02/19/california-department-of-tax-and-fee-administration-reports-cannabis-tax-revenues-for-fourth-quarter-of-2018/>.

<sup>174</sup> *California State Cannabis Tax Revenues Reflect Slow, Steady Increase in Legal Market Sales*, MARIJUANA BUS. DAILY (Aug. 23, 2019), <https://mjbizdaily.com/california-state-cannabis-tax-revenues-reflect-slow-steady-increase-in-legal-market-sales/>.

<sup>175</sup> *Id.*

<sup>176</sup> Bill Chappell, *California Says Its Cannabis Revenue Has Fallen Short of Estimates, Despite Gains*, NPR (Aug. 23, 2019), <https://www.npr.org/2019/08/23/753791322/california-says-its-cannabis-revenue-has-fallen-short-of-estimates-despite-gains>.

The low tax revenue figures are mainly attributed to the continued operation of illegal cannabis businesses.<sup>177</sup> In its 2018 annual report, the Cannabis Advisory Committee attributed this continued operation to enforcement which is fragmented and uncoordinated, creating a “thriving environment” for illegal cannabis businesses, and creating unfair competition for licensed cannabis businesses.<sup>178</sup> According to New Frontier Data, approximately 80% of the cannabis sold comes from illegal cannabis businesses.<sup>179</sup>

The black market of cannabis is not only a California problem, but it is also a national problem—New Frontier Data estimates that there are \$70 billion in illegal sales.<sup>180</sup> Regardless, illicit cannabis sales are most prevalent in California, and this is due, in part, to the surplus of cannabis that has been accumulating since medical cannabis was legalized in 1996.<sup>181</sup> Another contributing factor is the popularity of vaping, cannabis edibles, and other cannabis derivative products.<sup>182</sup> These products are smaller and are easier to transport as they are more inconspicuous than cannabis flower itself.<sup>183</sup>

Moreover, the high tax rates for both consumers and business owners, and the local bans discussed above, facilitate the continued operation of illegal cannabis businesses. Those operating illegal cannabis businesses do not see a reason to transfer into the legal market when it is immensely difficult, or impossible, to obtain the proper permits and licenses, and when most purchasers of cannabis in California are still buying from the unregulated market.<sup>184</sup> Consumers are continuing to buy from illegal cannabis businesses because they can avoid this high tax rate.<sup>185</sup> Further, consumers are drawn in by other incentives, including

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<sup>177</sup> Patrick McGreevy, *California’s Black Market for Pot Is Stifling Legal Sales. Now the Governor Wants to Step Up Enforcement*, L.A. TIMES (Feb. 18, 2019), <https://www.latimes.com/politics/la-pol-ca-gavin-newsom-crackdown-pot-black-market-20190219-story.html>.

<sup>178</sup> *California Cannabis Advisory Committee: 2018 Annual Report*, *supra* note 96, at 30.

<sup>179</sup> McGreevy, *supra* note 177.

<sup>180</sup> Scott Zamost et al., *A Look Inside the Black Market for Weed Shows the Huge Threat to Legal Businesses*, CNBC (July 12, 2019), <https://www.cnbc.com/2019/07/11/las-black-market-for-weed-threatens-the-growth-of-its-legal-business.html>.

<sup>181</sup> Thomas Fuller, *‘Getting Worse, Not Better’: Illegal Pot Market Booming in California Despite Legalization*, THE N.Y. TIMES (Apr. 27, 2019), <https://www.nytimes.com/2019/04/27/us/marijuana-california-legalization.html>.

<sup>182</sup> *Id.*

<sup>183</sup> *Id.*

<sup>184</sup> McGreevy, *supra* note 100.

<sup>185</sup> McGreevy, *supra* note 100.

open consumption, the ability to purchase cannabis after 10:00 P.M., and even free cannabis in exchange for a good review on Weedmaps, a website that lists every legal and illegal store across the nation.<sup>186</sup> This presents a downward spiral for regulation of the cannabis industry because the government, business owners, and consumers alike are contributing to the issues. This makes it increasingly difficult to transfer from an illicit market to a well-regulated market.

#### A. Taxation Issues

The high tax rates associated with cannabis businesses are inevitable. The tax rates differ amongst the different cannabis business types.<sup>187</sup> The basic categories of tax rates in California are for growers and distributors.<sup>188</sup> Retailers, for example, are subject to the typical state base tax<sup>189</sup> and local tax, a 15% excise tax on the average market price of the cannabis product, and a 5–15% business tax which varies by city and county.<sup>190</sup> Thus, those who wish to engage in cannabis businesses could be taxed up to 40% solely from California state and local taxes. Not only are these California state and local taxes imposed, but cannabis businesses are subject to federal taxes, as well. The Internal Revenue Code section 280E provides that “[n]o deduction or credit shall be allowed for any amount paid or incurred . . . in carrying on any trade or business if such trade or business consists of trafficking in controlled substances.”<sup>191</sup> Since cannabis remains a schedule one drug within the meaning of the Controlled Substances Act,<sup>192</sup> this provision applies to cannabis businesses. This affects cannabis businesses because cannabis businesses pay taxes on gross income.<sup>193</sup>

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<sup>186</sup> Zamost et al., *supra* note 180.

<sup>187</sup> See *supra* Part **Error! Reference source not found.**

<sup>188</sup> *California Cannabis Sales Tax: A Guide for Accountants Who Want to Go Green*, LUMATAX (Mar. 17, 2019), <https://lumatax.com/blog/cannabis-sales-tax-in-california-a-guide-for-accountants-who-want-to-go-green/>.

<sup>189</sup> *Id.* The state base tax as of 2019 is 7.25%. *Id.*

<sup>190</sup> *Id.*

<sup>191</sup> 26 U.S.C. § 280E.

<sup>192</sup> *Drug Scheduling*, U.S. DRUG ENFORCEMENT ADMIN., <https://www.dea.gov/drug-scheduling> (last visited Oct. 7, 2019).

<sup>193</sup> *Internal Revenue Code Section 280E: Creating an Impossible Situation for Legitimate Businesses*, NAT’L CANNABIS INDUSTRY ASS’N., <https://thecannabisindustry.org/uploads/2015-280E-White-Paper.pdf> (last visited Oct. 7, 2019).

Tax collection also became a large regulatory issue. Many cannabis businesses are operated on a cash-only or mostly cash basis.<sup>194</sup> The primary reason for this is because many legal cannabis businesses are unbanked.<sup>195</sup> Until cannabis businesses can be financially backed by banks, this problem will likely persist. On August 28, 2018, the Governor signed Assembly Bill 1741 to facilitate tax collection.<sup>196</sup> This Bill waives a penalty for cannabis licensees that was implemented when monthly tax payments over \$10,000 were paid in cash.<sup>197</sup> This Bill helped to alleviate some of the burden off cannabis businesses; however, the collection issues which stem from primary cash-only cannabis businesses will likely persist until cannabis businesses can be financially backed by banks.

*B. Dangers Arising from the Illicit Market*

The illicit cannabis market clearly affects state tax revenue and licensed cannabis businesses' revenue. The illicit market has more than only financial repercussions, however. There is a wide array of dangers associated with the illicit cannabis market and such dangers will be discussed below.

Illegal cannabis growth in the national forests leave "behind a trail of garbage, human waste, dead animals and caustic chemicals."<sup>198</sup> The Mexican drug cartel is behind the majority of these farms, posing dangers for the environment and also to individuals who encounter them.<sup>199</sup> One large issue is carbofuran, a deadly chemical banned in the United States, which is sprayed onto cannabis plants by these illegal growers to protect the plants from wildlife.<sup>200</sup> Traces of this chemical have been found in streams and rivers, poisoning the water supply, and in animals, both dead

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<sup>194</sup> Justin Rohrlich, *Cannabis Companies Are Paying Federal Taxes in Cash and It's Giving the IRS a Headache*, QUARTZ (Nov. 14, 2018), <https://qz.com/1461947/the-irs-cant-handle-cannabis-companies-all-cash-tax-payments/>.

<sup>195</sup> *Id.*; see also *supra* Part **Error! Reference source not found.**

<sup>196</sup> *Tax Guide for Cannabis Businesses: Overview*, CAL. DEP'T OF TAX & FEE ADMIN., <http://www.cdtfa.ca.gov/industry/cannabis.htm#Overview> (last visited Oct. 7, 2019).

<sup>197</sup> *2018 Legislation*, CAL. GROWERS ASS'N, [https://www.calgrowersassociation.org/2018\\_legislation](https://www.calgrowersassociation.org/2018_legislation) (last visited Oct. 7, 2019).

<sup>198</sup> Piper McDaniel, *Illegal Cannabis Farms Still Scarring Public Lands, Two Years After Prop. 64*, L.A. TIMES (Aug. 29, 2019), <https://www.latimes.com/environment/story/2019-08-28/cannabis-california-national-forests-environment>.

<sup>199</sup> *Id.*

<sup>200</sup> *Id.*

and alive.<sup>201</sup> Moreover, these growers leave behind toxic garbage, including car batteries, propane tanks, pesticides, herbicides, and rodent killers.<sup>202</sup> California Governor Gavin Newsom also stated that these illegal cannabis plants “are devastating [California’s] pristine forests, and are increasingly becoming fire hazards themselves.”<sup>203</sup>

Additionally, cannabis purchased from illegal cannabis businesses can be very dangerous. The cannabis potency and dosage is unreliable and inconsistent in the illicit market.<sup>204</sup> Further, illegal cannabis is not tested, and thus, cannabis may contain toxic chemicals, pesticides, mold, E. coli, and other bacteria.<sup>205</sup> Toward the later-half of 2019, many cases of individuals getting sick from vaping arose.<sup>206</sup> Many state governors commented on the issue, noting that many of these vaping-related illnesses arise from illicit cannabis cartridge sales, and warned against purchasing cartridges from illicit vendors.<sup>207</sup> In a statement made by the Centers for Disease Control and Prevention, of the 805 people who have gotten sick and the twelve who died since the end of September 2019, some vaped nicotine, but most reported vaping THC they bought from illegal cannabis sellers.<sup>208</sup> Given the reports of illicit cannabis-related vaping illnesses, it is clear that purchasing cannabis products from illicit markets poses certain health-related issues.

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<sup>201</sup> *Id.*

<sup>202</sup> *Id.*

<sup>203</sup> Jeff Daniels, *California Wages War Against Illegal Weed Farms; Gov. Newsom Wants Trump to Pay Some Costs*, CNBC (Apr. 3, 2019), <https://www.cnbc.com/2019/04/03/california-wages-war-against-illegal-marijuana-farms-retailers.html>.

<sup>204</sup> *Shop Licensed Cannabis Retailers Only.*, BUREAU OF CANNABIS CONTROL, [https://bcc.ca.gov/about\\_us/documents/weedwise\\_posters.pdf](https://bcc.ca.gov/about_us/documents/weedwise_posters.pdf) (last visited Oct. 7, 2019).

<sup>205</sup> *Id.*

<sup>206</sup> Kris Kane, *Legalizing Cannabis Is the Answer to Vaping Concerns*, FORBES (Oct. 07, 2019, 07:02 AM), <https://www.forbes.com/sites/kriskrane/2019/10/07/legalizing-cannabis-is-the-answer-to-vaping-concerns/#508bcf626948>.

<sup>207</sup> *Id.*

<sup>208</sup> Gillian Flaccus and Jennifer Peltz, *Lung Illnesses Send a Chill Through the Marijuana Vape Industry*, L.A. TIMES (Sept. 26, 2019, 10:28 AM), <https://www.latimes.com/business/story/2019-09-26/vaping-products-take-hit-health-scare>.

C. *Measures California Has Already Taken to Combat the Illicit*

*Market*

State enforcement agencies took some steps to combat the illicit cannabis market. As of February 2019, the Bureau of Cannabis Control sent out close to 3,000 cease-and-desist letters to unlicensed businesses.<sup>209</sup> However, the spokesman for the Bureau noted that “it is difficult to say how many of those letters resulted in action.”<sup>210</sup> State regulators also implemented enforcement against unlicensed businesses, including seizing their cannabis.<sup>211</sup>

Additionally, Governor Gavin Newsom announced in February 2019 that the National Guard would go after illicit cannabis farms.<sup>212</sup> The goal of the National Guard is to eliminate growth on public lands, not private lands.<sup>213</sup> The troops have insufficient funds to finance their mission, however, and are awaiting federal funds before commencing their seizure of illicit cannabis farms.<sup>214</sup> Another issue arising from the fight against illicit cannabis firms stems from the legalization of hemp.<sup>215</sup> Because hemp and cannabis share similar characteristics—a similar look and smell—hemp is sometimes used as a shield for illicit cannabis growth.<sup>216</sup>

California attempted to regulate Weedmaps’ listings through a letter sent by the Bureau—the Bureau contended that Weedmaps, in including illegal cannabis dispensaries and delivery services on their platform, was aiding and abetting violations of California cannabis laws.<sup>217</sup> Weedmaps responded, arguing “it is a service site like Google . . . and therefore subject to federally preemptive protections.”<sup>218</sup> Thus, the state took no action.<sup>219</sup>

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<sup>209</sup> McGreevy, *supra* note 177.

<sup>210</sup> *Id.*

<sup>211</sup> *Id.*

<sup>212</sup> John Schroyer, *California National Guard Not Yet Redeployed to Combat Illegal Marijuana Farms*, MARIJUANA BUS. DAILY (June 12, 2019), <https://mjbizdaily.com/california-national-guard-not-yet-redeployed-border-combat-illegal-marijuana-farms/>.

<sup>213</sup> *Id.*

<sup>214</sup> *Id.*

<sup>215</sup> Daniels, *supra* note 203.

<sup>216</sup> *Id.*

<sup>217</sup> McGreevy, *supra* note 177.

<sup>218</sup> *Id.*

<sup>219</sup> *Id.*



*D. Other Steps California Could Take to Help Combat the Illicit*

*Market*

Simply put, the illicit market, to an extent, is out of control. As of July 2019, the Bureau of Cannabis Control continues to lack sufficient resources to oversee the cannabis market.<sup>220</sup> An audit by the California Finance Department has noted that the Bureau’s current “personnel is not sustainable to provide effective and comprehensive oversight of cannabis activities throughout California.”<sup>221</sup> The audit did not examine the Department of Food and Agriculture nor the Public Health Department, which regulate cultivation and manufacturers, respectively.<sup>222</sup> These three cannabis regulatory agencies need to come together to come up with a decisive plan on how to enforce and regulate California’s cannabis marketplace.

A viable solution to help with the crackdown of the illicit cannabis market is allowing more licenses. As discussed in Part II, *supra*, if Assembly Bill 1356 is passed, this will compel local governments to issue more licenses. Further, if local governments that only allow one or a limited amount of licenses are required to issue all license types, this will also aid in combatting the market.

For cities that are against having cannabis storefronts, allowing deliveries seems like a fair compromise. In fact, the Bureau of Cannabis Control passed regulation governing cannabis deliveries, and this particular issue— “[a] delivery employee may deliver to any jurisdiction within the state of California provided that such delivery is conducted in compliance with all delivery provisions . . . .”<sup>223</sup> On April 4, 2019, however, over twenty cities and counties that restrict cannabis sales joined in a lawsuit, arguing that cannabis deliveries allowed under Section 5416(d) are in direct contrast with, and violate, Proposition 64.<sup>224</sup> The outcome of this lawsuit will help determine whether cannabis deliveries

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<sup>220</sup> Associated Press, *California Officials Struggling to Regulate Weed Market: Audit*, KTLA (July 17, 2019, 3:48 PM), <https://ktla.com/2019/07/17/california-officials-struggling-to-regulate-weed-market-audit/>.

<sup>221</sup> *Id.*

<sup>222</sup> *Id.*

<sup>223</sup> Cal. Code Reg. § 5416(d).

<sup>224</sup> Patrick McGreevy, *California Cities Sue State Over Home Deliveries of Pot*, L.A. TIMES (Apr. 5, 2019), <https://www.latimes.com/politics/la-pol-ca-california-sued-pot-deliveries-20190405-story.html>.

will remain ubiquitous throughout California. In turn, the outcome determines whether lawful cannabis deliveries can help with the fight against the illicit cannabis market.

Regardless of the outcome of Assembly Bill 1356 or the livelihood of Section 5416(d), the state can speed up the licensing process for current state licensees.<sup>225</sup> At the beginning of 2019, “it was reported that businesses across the state were losing their licenses because certain state agencies could [not] process them fast enough.”<sup>226</sup> In response, California officials proposed Assembly Bill 97 to extend the operational period given to growers and sellers under provisional licenses by five years.<sup>227</sup> The extension was proposed because cannabis governmental agencies are severely understaffed.<sup>228</sup> The California Legislature passed the Bill in June 2019,<sup>229</sup> which helped combat the illicit cannabis market in more than one way. The Bill also includes a provision where any of the three cannabis licensing agencies can impose a \$30,000-a-day fine against unlicensed cannabis businesses.<sup>230</sup>

Moreover, another simple solution would be to extend the hours of operation of cannabis stores.<sup>231</sup> The Bureau has limited retailers to sell and deliver cannabis only between 6:00 A.M. and 10:00 P.M.<sup>232</sup> If cannabis can be sold until 2:00 A.M., like the sale of alcohol in California, this could resolve the issue of buyers buying from the illicit market after 10:00 P.M.

Perhaps the best solution would be for California to lower taxes.<sup>233</sup> As of January 2019, seven states which legalized recreational cannabis

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<sup>225</sup> Griffen Thorne, *Six Ways California Can Combat the Cannabis Illicit Market*, CANNA LAW BLOG (June 13, 2019), <https://www.cannalawblog.com/six-ways-california-can-combat-the-cannabis-illicit-market/>.

<sup>226</sup> *Id.*

<sup>227</sup> Patrick McGreevy, *California to Give Struggling Cannabis Business More Time on Provisional Permits*, L.A. TIMES (June 14, 2019), <https://www.latimes.com/politics/la-pol-ca-pot-business-permits-delayed-20190614-story.html>.

<sup>228</sup> *Id.*

<sup>229</sup> John Schroyer, *California Approves Bill to Extend Provisional Permits, Curtail Illicit Cannabis Firms*, MARIJUANA BUS. DAILY (June 27, 2019), <https://mjbizdaily.com/california-to-extend-provisional-marijuana-business-permits/>.

<sup>230</sup> *Id.*

<sup>231</sup> Thorne, *supra* note 225.

<sup>232</sup> *Id.*

<sup>233</sup> *Id.*

have implemented cannabis sales tax rates.<sup>234</sup> Washington cannabis has the highest sales tax at 47.1% and California trails with a sales tax of 40.3%.<sup>235</sup> Purchasing cannabis in California, however, proves to be more costly than purchasing cannabis in Washington.<sup>236</sup> In February 2019, the average price for an eighth of cannabis in California was \$41.10, whereas the average price in Washington was \$35.42.<sup>237</sup> Therefore, it appears that the cost of the cannabis itself is one of the main issues, not the sales tax in and of itself. This is due, in part, to the difficulty and costliness in obtaining licenses.<sup>238</sup>

Furthermore, environmental issues likely hiked up the prices of cannabis in California.<sup>239</sup> “Droughts and wildfires raging through the state ha[ve] limited crop yields and driven up the prices, with some producers claiming to have lost as much as an entire year’s crop in the most recent wildfires.”<sup>240</sup> Moreover, these cannabis cultivators are required to pay taxes—cultivators have to pay \$9.25 per ounce of cannabis flower and \$2.75 per ounce of cannabis trim.<sup>241</sup> While these environmental issues cannot be regulated by humans, alleviating some of the burden on cultivators, other cannabis business owners, and cannabis consumers by reducing taxes allows California to shift from a primarily unregulated illegal cannabis market to a well-regulated legal cannabis market.

#### CONCLUSION

In sum, while California legalized recreational cannabis usage, California still encounters major obstacles pertaining thereto. This is due to the fact that even though recreational cannabis has been legalized in the state, cities and counties have the final say in deciding whether or not any

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<sup>234</sup> Janelle Cammenga, *How High Are Taxes on Recreational Marijuana in Your State?*, TAX FOUNDATION (Apr. 24, 2019), <https://taxfoundation.org/2019-recreational-marijuana-taxes/>.

<sup>235</sup> WikiLeaf, *Which States Have the Highest Taxes on Marijuana?*, PRICEONOMICS (last visited Jan. 27, 2020), <https://priceonomics.com/which-states-have-highest-taxes-on-marijuana/>.

<sup>236</sup> *Id.*

<sup>237</sup> *Id.*

<sup>238</sup> *Id.*

<sup>239</sup> *Id.*

<sup>240</sup> *Id.*

<sup>241</sup> Justin Rohrlich, *Here’s How Much Marijuana Businesses Pay in Taxes*, QUARTZ (Apr. 15, 2019), <https://qz.com/1595906/how-much-tax-do-marijuana-businesses-pay/>.

type of cannabis operation may be feasible. Because of the stigma and skepticism surrounding a complete legalization of cannabis by the majority of cities and counties, it may seem impossible for those who wish to partake in the cannabis industry to execute these objectives, and it also presents problems for consumers. The federal illegality of cannabis likewise contributes to this issue. Until the stark contrast between California state law and city, county, and federal laws is altered, the vast issues—taxation collection issues, regulatory issues, banking issues, employment issues, and all the other dangers arising from the ongoing presence of the illicit market—will persist. In order to circumvent these problems, it is essential to alter these conflicting laws, so all cannabis-related laws coincide.

