

California Adopts Emergency Cannabis Regulations for Licensing Beginning on January 1, 2018

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On November 16, 2017, California published the long awaited rules and regulations to implement voter approved Proposition 64, the Adult Use of Cannabis Act of 2016, which legalized adult use of cannabis in the State of California. The California Legislature passed and the Governor signed into law the Medicinal and Adult-Use Cannabis Regulation and Safety Act (MAUCRSA), which creates the general framework for the regulation of both commercial medicinal and adult-use (recreational) cannabis. The State agencies that regulate cannabis, the Bureau of Cannabis Control (distribution, testing, retail and microbusiness), Department of Food and Agriculture (cultivation) and Department of Public Health (manufacturing), established new regulations under an “emergency” rule-making process for commercial medicinal and adult-use (recreational) cannabis industries. The “emergency” regulations will be followed by a formal rule-making process beginning next year.

California’s new cannabis regulations will be of interest to the growing number of Canadian companies and investors involved in the cannabis industry.

The regulations include:

Temporary Permits – In December 2017, California will begin accepting on-line applications for temporary business permits. Priority application review will be provided for annual licenses applicants that were in operation under the Compassionate Use Act prior to September 1, 2016. Temporary permits will be good for four months (120 days) for cannabis businesses, which may be extended for two 90-day extensions (only if the temporary licensee has applied for an annual license). There is no fee for temporary permits. Cannabis businesses will need local approval for conducting commercial cannabis activities, which must be demonstrated to receive a temporary permit. Beginning January 1, 2018, an email notification will be issued from the State confirming that a temporary permit has been approved.

Transitional Rules – Licensed cannabis companies will have a six-month grace period

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(until July 1, 2018) to sell products in their inventory (with specified labeling) that do not comply with regulation (testing and labeling) guidelines and may work with other licensed businesses without worrying about whether their permits are for medical and recreational activities. During the transitional period, licensees will not be required to use the State's track-and-trace system but will need to complete manifests and other paperwork to keep track of cannabis products.

Two Types of Licenses – There will be two types of licenses: A-License (adult use) and M-License (medical cannabis). It is unclear whether an A-license can be used for a medical dispensary or a business would require *separate* A and M licenses. Testing labs may test cannabis goods for both types of licenses.

License Fees/Activities – Annual cannabis license fees are based on a sliding scale ranging from \$800 to \$120,000 based on activity and revenues. Activities include retail operations, cannabis events, distribution, cultivation, manufacturing and products, laboratory testing and microbusiness (multiple commercial cannabis activities are permitted under one license).

Retail Operations: Adult-use cannabis sales are limited to adults 21 years and over. Stores cannot be located within 600 feet of schools (K-12 school, day care center, or youth center), must close by 10:00 p.m., and must have 24-hour surveillance. There are limitations on purchases (adult-use customers may purchase up to one ounce and medical patients up to eight ounces or more with physician's note). Only medical cannabis patients or their caregivers will be permitted to receive free cannabis products or samples. Products must be packaged, tested and labeled. Advertising is limited.

Distribution: Only a licensed distributor may transport cannabis.

Cannabis Manufacturing and Products: The California Department of Public Health (CDPH) is responsible for regulation of manufacturing of cannabis. Manufacturing licenses (A-License and M-Licenses) fall under four license types: Type 7: Extraction using volatile solvents; Type 6: Extraction using non-volatile solvents or mechanical method; Type N: Infusions; and Type P: Packaging and labeling only. All cannabis products must contain a State-mandated warning label and the CDPH-issued universal symbol and must be tested. Edible products may not be in shapes that may appeal to children – no human beings, animals, insects, or fruit shapes. There are limits on THC content. Licensees must have written procedures for inventory control, quality control, transportation, security and cannabis waste disposal. Good manufacturing practices must be followed.

Cannabis Cultivation: The California Department of Food and Agriculture regulates the cultivation of commercial cannabis. Cultivation of cannabis is divided into three categories: Cultivators (commercial cultivators); Nurseries (cloning and seed propagation) and Processors (trimming, drying, curing, grading, or packaging).

Testing Laboratories: All cannabis goods must meet certain health and safety standards before they can be sold to consumers. To ensure that cannabis goods meet those

standards, a representative sample of the cannabis goods must be tested by a licensed testing laboratory. The regulations provide the minimum laboratory-operation requirements, which would include requirements such as sampling procedures, personnel qualifications, standard operating procedures, and recordkeeping requirements.

Ownership – License “owners” must submit fingerprints (via the Department of Justice’s Live Scan service) and background information including any past criminal convictions. An “owner” includes the CEO, a board member, a person holding 20% or more ownership interest and any person participating in the direction, control, or management of the person applying for a license. Individuals that are employed by the State of California or district attorney’s offices and law enforcement agencies are prohibited from holding a license when the duties of their employment have to do with enforcement of cannabis regulations.

Financial Interests – The license application must disclose the holders of “financial interests” (any investment, loan or any other equity interest), including the holder’s name, birth date and a government issued ID. Holders of financial interests that are not required to be listed: (a) a bank or financial institution whose interest constitutes a loan; (b) individuals whose only financial interest in the commercial cannabis business is through an interest in a diversified mutual fund, blind trust, or similar instrument; (c) individuals whose only financial interest is a security interest, lien, or encumbrance on property that will be used by the commercial cannabis business; and (d) individuals who hold a share of stock that is less than 5 percent of the total shares in a publicly traded company.

Labor and Employment – License applicants with more than 20 employees must attest that they have entered into a labor peace agreement (in which the employer agrees not to resist organizing attempts by its workers) and provide a copy to the Bureau of Cannabis Control. If no such agreement exists, the license applicant will have to provide a notarized statement indicating that the company *will* enter into a labor peace agreement.

Surety Bond – License applicants must obtain a surety bond of \$5,000, payable to the State as obligee, to ensure payment of cost incurred for the destruction of cannabis product necessitated by violation of the MAUCRSA or regulations.

For a more complete summary of the regulations visit:

www.dorsey.com/newsresources/publications/client-alerts/2017/11/ca-emergency-cannabis-regulations

Federal Law Warning: The United States federal government regulates drugs through the Controlled Substances Act (21 U.S.C. § 811), which places controlled substances, including cannabis, in a schedule. Cannabis is classified as a Schedule I drug. A Schedule I controlled substance is defined as a substance that has no currently accepted medical use in the United States, a lack of safety for use under medical supervision and

a high potential for abuse. The Department of Justice defines Schedule 1 controlled substances as “the most dangerous drugs of all the drug schedules with potentially severe psychological or physical dependence.” The United States Federal Drug Administration has not approved the sale of marijuana for any medical application. State laws regulating cannabis are in direct conflict with the federal Controlled Substances Act, which makes cannabis use and possession federally illegal.