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Staff Report for a Resolution Awarding the City of San Leandro's Second Medical Cannabis Dispensary Annual Permit Following the Effective Date of the Revised Medical Cannabis Dispensary Ordinance

SUMMARY AND RECOMMENDATIONS

The City Manager presents to the City Council the following analysis of the two applications that were received from business teams seeking to operate the second medical cannabis dispensary to assist the Council in selecting between the two teams to award the permit. The City Manager also presents for the City Council's adoption, should it so choose, a resolution representing the permit and conditions of approval written into said permit. The draft resolution awarding the permit, if approved, would be effective July 20, 2016, the effective date of the recently amended medical cannabis dispensary permits ordinance.

BACKGROUND

Following extensive dialogue with the community and numerous City Council discussions over several years, in December 2013, the City Council approved a medical cannabis regulatory ordinance to facilitate the approval, regulation, and operation of one medical cannabis dispensary in San Leandro. That ordinance, in conjunction with the Medical Marijuana Regulation and Safety Act of 2015, imposes strict zoning, security, and operational requirements on the operation of medical cannabis dispensaries.

To assist in developing a process to implement that ordinance, following a publicly announced Request for Proposals, the City contracted with ICF International, an independent third-party

consultant with expertise assisting governmental agencies across a wide range of subject areas, including medical marijuana program implementation, application review, business plan analysis, public health, safety and security. ICF also directly supported the statewide medical marijuana dispensary application review process for the Commonwealth of Massachusetts. As part of this work, ICF assisted the Massachusetts Department of Public Health in evaluating the most qualified applicants for registration as medical marijuana dispensary, cultivation, and processing facilities. ICF's related tasks included expert panel review of approximately 100 applications in technical areas that span corporate structure, financial management, cultivation, security, operations, drug diversion, patient access, as well as review of tax returns and credit reports for several hundred individual applicant team members, and score report development.

As part of its contract with the City, the ICF consultant team worked with an inter-departmental stakeholder group consisting of staff from various Departments, including the City Manager's Office, Community Development Department, Finance Department, and the City Attorney's Office. In 2016, this team was expanded to include representatives from the Police Department.

On December 15, 2014, a request for applications from parties interested in serving as San Leandro's first dispensary operator was publicly released and 15 teams ultimately applied for the first dispensary permit. Following a robust review of the 15 applicant proposals, the following three teams (in alphabetical order) were identified as having demonstrated the optimal combination of knowledge, expertise, experience, and alignment with the Council-adopted criteria:

- Blum San Leandro
- Davis Street Wellness Center
- Harborside San Leandro

On September 8, 2015, a recommendation from the City Manager was presented to the City Council, and the City Council unanimously voted to award the first dispensary permit to Harborside San Leandro.

Based upon City Council direction provided at subsequent Council meetings in late 2015 and early 2016, on June 6, 2016, the City Council adopted various amendments to the dispensary ordinance, including a provision that allows for the issuance of a second dispensary permit.

In late 2015, the City Council directed the City Council Rules Committee to develop a process to award the second permit. Following extensive discussions by the Rules Committee, its recommendations were presented to the City Council on February 16, 2016. At that meeting, the Council directed staff to limit the selection process for the second dispensary permit to only the two remaining teams from the list of three business teams provided above, i.e. Blum San Leandro (hereafter referred to as "Blum SL"), and Davis Street Wellness Center (hereafter referred to as "DSWC"). As part of its actions, the Council affirmed the Rules Committee's recommendation to allow these two teams to submit updated application materials, which would be scored using Council-adopted criteria. The criteria included Site Planning, Finance, Operations and Community Benefits.

Based upon this direction, on April 28, 2016, the City Manager's office distributed to the two teams a new Request for Applications, and invited the teams to provide responses to various questions, including questions related to their proposed financing, operations, security plans, proposed locations, and community benefits programs. Copies of those application materials are attachments to this report. With ICF's assistance, numerical scores were applied to the applications based upon

the quality of the team's responses to the various questions.

In June 2016, following completion of the numerical scoring, the stakeholder group conducted site visits to Blum's existing cannabis dispensary, cultivation facility and laboratory in Oakland. The City stakeholder group also visited a cannabis cultivation site operated by members of the Davis Street Wellness Center's management team. The City stakeholder group visited the Davis Street Family Resource Center, and Davis Street's Federally Qualified Health Clinic. Several days later, both teams were separately interviewed by the City Manager's stakeholder group to further assess the teams' capacities to effectively operate the second dispensary. Staff also conducted due diligence on each of the two teams, which included contacting references acquainted with cannabis facilities operated by members of the applicant teams.

Capacity to Operate a Successful Dispensary in San Leandro

Over the course of the past year and a half, each of the teams worked collaboratively with City staff as their applications were navigated through both the first and second permit award processes. Both teams provided detailed application materials that effectively responded to the questions posed, and each team proactively worked with City staff to address questions and concerns that were identified. Both teams also provided extensive documentation demonstrating that they had access to sufficient capital to start-up and operate their proposed dispensaries.

Using their experiences operating dispensaries and/or cultivation sites in other jurisdictions, both teams provided detailed security plans that include extensive measures designed to ensure a safe and secure facility that will sufficiently address public safety. High-definition cameras, around-the-clock security, and various other features are in their proposed plans to maximize security while also offering independent laboratory-tested medicine that work to ensure safe medicine for patient consumption. The teams also commit to providing their employees with wages that exceed the City's living wage and anticipated minimum wage requirements, as well as employee benefits packages that include retirement, vacation and sick leave benefits. Lastly, both teams offer robust community benefits programs that include financial contributions to local non-profit service providers as well as the City General Fund. As such, in staff's estimation, both teams demonstrate the knowledge, skills, and expertise that would be necessary to operate a successful dispensary in San Leandro.

Nevertheless, each team offers distinctly different proposals, which provide their own unique potential strengths and weaknesses, as staff further describes below.

Overview of Numerical Scores

The first step in the review of the application materials involved an assessment of the quality of each team's responses to the Request for Applications using a numerical scoring methodology. This effort was conducted by ICF International, Inc. due to its extensive experience analyzing these types of proposals. A summary of the scores is attached (with maximum possible points shown in parentheses).

As can be seen in the attached scores, each team demonstrated strengths and weaknesses that varied according to each of the categories to which scores were applied (with assessments of each team provided in alphabetical order).

Proposed Location

Blum SL proposes to purchase real property at 1925-1927 Fairway Drive. The property is currently in

escrow. The site complies with the distance requirements in the medical cannabis dispensary ordinance and is located in an industrial zone that is appropriate for the proposed use. In addition, Blum SL's proposed site would provide in excess of 30 parking spaces, which exceeds the minimum parking standards required by the San Leandro Zoning Code. In the first full year of operations Blum SL expects to have 14 employees, which will increase to 21 employees by Year 3. In the first quarter of operations Blum SL expects to have 60 patient visits per day, which will increase to 300 patient visits per day by Year 3. The dispensary operations are proposed to utilize approximately 5,000 square feet of the 13,300 square foot building. Blum SL is interested in either relocating its laboratory and manufacturing operations to San Leandro, or expanding into manufacturing edibles in the remaining 8,300 square feet.

DSWC identifies two potential locations for its proposed facility, and has secured both locations through lease options. The potential sites are: (i) 765-767 Marina Boulevard (the "Marina location") and (ii) 1244 Doolittle Drive (the "Doolittle location"). Of the two, DSWC prefers the Marina location. However, the Marina location does not comply with the distance requirements in the medical cannabis dispensary ordinance because the site is located approximately 970 feet from the northwestern corner of the Boys and Girls Club of San Leandro (the ordinance requires a minimum of 1,000 feet between a dispensary and a youth center, which is defined as a facility that serves youth 18 years of age or under).

Per the ordinance, in order for DSWC to operate a dispensary at this location, the City Council would have to make affirmative findings as part of the award of the dispensary permit that the site "will not impact the peace, order and welfare of the public." (San Leandro Municipal Code section 4-33-200(d) (1). The ordinance closely follows the California Attorney General's 2008 Guidelines for the Security and Non-Diversion of Marijuana for Medical Use. Under the Guidelines' Section III.B.1 "Enforcement Guidance," the Attorney General provides that medical marijuana may not be smoked at or within 1,000 feet of a school, recreation center, or youth center. Although the Attorney General's Guidelines are not law, similar to the Attorney General's opinions, courts routinely read both as persuasive authority when rendering decisions. Thus, it is the City Attorney's opinion that if the City Council approves the permit with the Marina site as proposed, the permit is subject to challenge, which may be successful given the site is within 1,000 feet of the Boys & Girls Club, a land use that is expressly identified as incompatible within 1,000 feet of a medical cannabis dispensary. Per the ordinance, although medicine may not be smoked or consumed on the premises, the ordinance does provide that medicine may be dispensed in a variety of ways, including edibles such as cookies, cakes, and candies. Given these factors, the site's proximity to the Boys & Girls Club (a youth center) raises substantive concerns.

The Marina location is also situated within 350 feet of the proposed Industrial Transitional zone, which will be considered by the City Council in September as part of the anticipated Zoning Code updates. If adopted by the City Council, this zone would allow for residential development due to its proximity to the Downtown San Leandro BART station. Should the proposed zoning code changes ultimately be adopted in September, staff recommends that the Council consider updating the cannabis dispensary eligible locations map accordingly.

In addition, this property is located in a prominent location with frontage directly on Marina Boulevard, within the City's automotive dealer row, and in close proximity to other prominent retail uses. In 1997, the City established the Marina Boulevard Special Overlay District, which includes additional criteria for evaluating new uses in this area. The Marina location is part of the Regional Retail/Auto Mall area, which provides that new uses should fall into one of the following three categories: regional

retail, new auto sales, or other uses that are compatible with regional retail or auto sales uses. The proposed medical cannabis dispensary use does not meet these criteria.

Based on the factors detailed above, staff does not see sufficient evidence to support a finding by the City Council that a dispensary at this location “will not impact the peace, order and welfare of the public.”

The alternative Doolittle location complies with the setback requirements contained within the ordinance. Under the Zoning Code, the 2,600 square foot facility would be required to provide a minimum of 10 parking spaces. Although the application materials state that the proposed site provides 17 on-site spaces, staff is unable to verify these figures because the application materials do not provide a traditional site plan demarcating where those spaces would be located. This site appears small for the proposed level of activity and the parking appears insufficient to meet the needs of the 17 full-time employees and anticipated 250 customers per day upon start up, which will increase to 22 employees and 765 customers per day by the fourth quarter of Year 3 according to the applicant’s projections. Parking is a concern since there is no on-street parking near the proposed location at the southeast corner of Davis Street and Doolittle Drive.

Nevertheless, if the City Council were to issue the dispensary permit to DSWC at the Doolittle location, the Council would retain the authority to impose a condition of approval on the permit stating that the applicants would be required to mitigate any parking issues that might arise, or identify an alternative location that fully complies with the dispensary ordinance.

Finances

Blum SL and DSWC use different approaches in their financial projection models.

Blum SL uses a “bottom-up” approach for its financial modeling, based on current registered Blum Oakland patients who live in San Leandro or nearby communities. Using this approach, Blum SL conservatively expects to begin serving approximately 60 patient visits per day in the first quarter of operations, gradually increasing over the next three years to approximately 300 patient visits per day. According to its pro forma, Blum SL will generate approximately \$2.6 million in revenue in its first full year of operation; approximately \$5.4 million in Year 2, and approximately \$7.3 million in Year 3.

DSWC uses a “top-down” approach that projects its patient base assuming the potential patient pool to be 3% of the total population who lives within a 30-minute drive of San Leandro. Further assuming a 50% share of San Leandro’s market, DSWC’s application predicts approximately 250 patients per day on average upon initial start-up during its first quarter of operations, with 15% quarterly growth. This methodology results in DSWC forecasting significantly larger annual revenues than Blum SL. More specifically, according to its pro forma, DSWC forecasts that it will generate approximately \$1.27 million in revenue in Year 1 (assuming operations for only the 4th quarter), approximately \$6.94 million in year 2, and approximately \$11.67 million in Year 3.

Operations

DSWC and Blum SL also offer distinctly unique visions and stated approaches for how their facilities will operate.

Blum SL proposes a tested, more traditional model of dispensing medical cannabis that is informed by its four years of experience operating a dispensary in Oakland, and more recently in Las Vegas. Blum SL’s application includes photos of the Las Vegas location, which will be the model for the San

Leandro dispensary. Blum SL will be structured as a new community collective, although managed by many of the same executive team members who manage Blum Oakland. Since the time of its initial application as part of San Leandro's first dispensary award process in 2015, Blum Oakland merged with a publicly traded parent company -- Terra Tech Corporation. As a result of this merger, Blum SL states that it will have greater access to "working capital, state of the art equipment, grow technology, human resources services, community partners, and industry expertise." Terra Tech is a publicly traded company; as such Blum SL states that the merger increased levels of transparency through more stringent financial and performance auditing requirements, which resulted in stricter operating standards (Blum SL has indicated, for example, that product and cash diversion has decreased to 0.0005% since the merger).

Blum SL proposes that it will employ 21 employees in year 3 and operate up to 10 patient stations to handle 300 patients per day. All employees at Blum SL would be offered access to a health medical plan, dental, vision, employee assistance, 401(k) retirement match, and various other employee benefits upon hiring. Similar to Harborside San Leandro, Blum SL plans to handle vendor purchases at its Oakland location and transport product to San Leandro as needed. Blum SL would also like to relocate its laboratory and manufacturing operations for its IVXX brand to the remaining 8,300 square feet of the site.

DSWC states that it will offer an innovative new approach to dispensing medical cannabis. According to DSWC's application materials, its facility will dispense medical cannabis in a clinical setting that will include an "advisory board of doctors and specialists to offer panel reviews of individual patients, observing symptoms and recommending treatment accordingly." When applicable, DSWC also proposes to refer patients to its partner facility, the Davis Street Family Resource Center (hereafter referred to as "DSFRC"), for "additional consultation, assistance, or treatments." However, because DSFRC is a federally qualified healthcare provider and because cannabis continues to be classified as a Schedule 1 substance at the federal level, DSWC is clear that DSFRC doctors would not be able to provide formal written recommendations for medical cannabis treatments to patients.

DSWC proposes to employ 17 employees in years 1 and 2, which would increase to 22 employees by the second half of Year 3. DSWC will provide vacation time for all full-time employees who have worked for the company for at least two continuous calendar years, and employees will be able to take sick leave following their first 90 days of employment. DSWC will also offer continued education, health insurance, dental plan, 403(b) retirement match and various other benefits. DSWC anticipates 250 patients per day upon initial start-up, which would increase to 765 patients per day by the end of Year 3. DSWC's proposed operations include a vendor area with a separate entrance for the purchasing of cannabis from approved vendors on an appointment only basis.

Community Benefits

As part of its community benefits program, Blum SL offers to self-impose a five percent (5.0%) gross receipts fee that it will voluntarily provide to the City's General Fund. Blum SL further states that if and when San Leandro voters adopt a cannabis business tax, that it will fully comply with the tax in lieu of the voluntary gross receipts percentage contribution. Blum SL also offers to create a community grants program that will "provide grants to programs and institutions in which the City of San Leandro has already invested." Blum SL identifies seven program areas it plans to fund via grants in its first five years of operations. Each individual award will not exceed \$25,000 so that Blum SL may "impact as many program areas as possible". Blum SL also anticipates that grant amounts will increase in the second and subsequent years. As part of its proposal, Blum SL also offers to provide financial support for re-entry and jobs training programs, domestic violence prevention

programs, youth development, local community revitalization efforts, substance abuse education, foreclosure prevention, housing rehabilitation, and support for the San Leandro Homeless Compact. Blum SL also offers to subsidize the cost of medical cannabis to qualified low-income patients.

DSWC offers to provide a voluntary contribution of 9% of its gross receipts to the City's General Fund. DSWC further states that if and when San Leandro voters adopt a cannabis business tax, that it will comply with the tax in lieu of the voluntary gross receipts percentage contribution. DSWC also offers to create a community benefits package consisting of several primary elements, which are further augmented through its proposed partnership with the Davis Street Family Resource Center ("DSFRC"). More specifically, DSWC offers to provide a contribution to the DSFRC for its basic needs program that will provide families and seniors with emergency food, clothing and other resources. DSWC estimates approximately \$115,000 will be contributed annually as part of this effort, which will "free up funds that can help grow the Bill McCammon Community Health Center Homeless Medical Clinic". The application materials also highlight various other DSFRC programs that will benefit financially from DSWC, including: community counseling, substance abuse prevention, as well as an annual community dialogue on medical cannabis. DSWC also offers a sliding fee scale to low-income patients and it offers to ask DSFRC to recommend additional benefits partners through an annual vetting process that will donate up to 5% of revenues. During its first year of operations, DSWC commits to providing the following one-time contributions to the City of San Leandro: \$50,000 towards the Cherry Festival, \$50,000 towards planning and business development, and \$50,000 for use by the Arts Commission. These contributions would decrease to \$10,000 annually in future years.

Future Tax Discussion

It is important to note that the City's first dispensary permit that was awarded to Harborside San Leandro (HSL) contained a provision that HSL's community benefits commitments would be nullified if San Leandro voters approved a measure to impose a medical cannabis business tax. A similar condition of approval is incorporated into the attached resolution. The permit awarded to HSL also contains a provision that if the City were "to award more than one medical cannabis dispensary permit, all subsequent medical cannabis dispensary permits awarded or approved by the City shall include no less than that which is required or conditioned by this resolution." Given that both teams offered robust community benefits packages that meet or exceed the community benefits package offered by HSL, this condition is addressed through the following condition of approval that is included in the attached draft resolution:

"Permittee shall comply with, effect, and further all of the commitments, statements of intent, and promises, including but not limited to its community benefits commitments, contained in its application to operate a medical cannabis dispensary, which are incorporated herein and made a part hereof as an attachment to this resolution."

Additional Considerations

At tonight's Council meeting, the City Council is also considering the placement of a revenue measure on the November 8, 2016 ballot that would ask San Leandro voters to consider a local cannabis business tax of up to 10% of gross receipts. There is also a statewide measure (Proposition 64) that will appear on the November ballot, which could legalize the adult use of cannabis throughout California without the need for a doctor's recommendation. The approval of this latter measure could have significant impacts upon the industry statewide and in the City because it would open up various opportunities for the expansion of the cannabis industry throughout the state.

Additionally, members of both applicant teams currently operate cannabis cultivation, processing and THC extraction facilities in other jurisdictions, which could similarly produce revenue for the City's General Fund if they were allowed to operate such facilities in San Leandro.

Conclusion

Both of the applicant teams demonstrate the knowledge, skills, expertise, and access to capital to operate a successful dispensary in San Leandro. In addition, both teams demonstrate a commitment to provide extensive benefits to the San Leandro community. Nevertheless, each application brings its own unique strengths and weaknesses, as outlined above and in the attached documents.

Given the rapidly evolving legal and regulatory environment relative to the cannabis industry, coupled with the cannabis industry's potential to meet medical needs and generate financial benefits for the community, staff recommends that the City Council explore the possibility of allowing additional cannabis dispensaries and/or ancillary cannabis businesses to operate in the City of San Leandro in the future.

Fiscal Impacts

The City will collect a \$60,000 annual dispensary permit fee 30-days after opening. The permit fee is designed to off-set the City's costs in regulating the dispensary's operations.

The facility will also generate annual sales tax receipts, of which the City will receive 1.5%, as well as voluntary contributions to the City's General Fund that will vary depending on which applicant team is awarded the permit.

ATTACHMENTS

- Application Scoring Sheet
- Blum San Leandro Application Materials and Overview of Proposal
- Davis Street Wellness Center Application Materials
- Copy of Request for Applications to Operate the Second Cannabis Dispensary

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