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CONTENTS

CANNABIS LAW NEWS

REGULATORY DEVELOPMENTS

LEGISLATIVE DEVELOPMENTS

RECENT STATE DECISIONS

Continued on next page

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CANNABIS NEWS

PORTLAND, OREGON CITY COUNCIL COMMISSIONERS ADDRESS DIVESTMENT OF MARIJUANA TAX REVENUE FROM THE POLICE

In the past two months, the deaths of George Floyd and Breonna Taylor by police have produced national outrage and protests—but the dialogue from the fallout has produced widespread calls to defund law enforcement. In response, lawmakers are tackling the issue by considering the sources of the funding of police departments. On June 11, 2020 the Portland, Oregon, City Council approved an amendment to a proposed budget that would take cannabis tax revenue away from the city police.

The Portland Efforts to Defund Cannabis Tax Revenue

Commissioner Jo Ann Hardesty announced that $27 million in cuts were approved by lawmakers, combined with additional cuts put into place by the mayor. The cuts specifically include the halting the use of cannabis tax funds "to fill funding gaps for the Traffic Division." The other cuts include:

- Defunding the Gun Violence Reduction Team (GVRT)
- Defunding the School Resources Officers (SROs)
- Defunding the Transit Police unit
- Eliminating the 8 new positions in Special Emergency Reaction Team
- Reallocating $4.8 million from defunding the specialty units to fund Portland Street Response
- Reallocating $1 million from PPB funds for black youth leadership development
- Reallocating $1 million for houseless community participatory budgeting.

The Cannabis Community Agrees

Other organizations agree with the move. On June 10, 2020, the Minority Cannabis Business Association published a call for an end to funding Portland Police with cannabis revenue. The 2016 Recreational Marijuana Sales Measure 26-180 was supposed to give tax revenue funds to drug and alcohol treatment, public safety investments and support for neighborhood small businesses. "The city has failed to use these dollars as prescribed," the association asserted. The association pointed out that in 2019, the Portland City Auditor report showed 79 percent of cannabis tax revenue went into law enforcement every year since recreational cannabis was legalized in 2016.

Jason Ortiz, President of the Minority Cannabis Business Association and police accountability activist stated:

> We call on all cannabis justice activists to investigate their municipal finances, their local cannabis company investments, and discover if and how dollars meant for community uplift are being sent to law enforcement. This mockery of justice is a shameful moment in our history and we will not allow it to be our future.

"To delay this common-sense policy is to ensure the protests will continue," echoed Dr. Rachel Knox, Chair of the Oregon Cannabis Commission, member of Portland's Cannabis Policy Oversight Team, and Board member of Minority Cannabis Business Association. "Cannabis has historically—and continues to be to this day—a tool weaponized against communities of color," said Dr. Knox, who stated:

> It's really, in my opinion, paradoxical that we are now using the economy of cannabis to fund the very institution that continues to terrorize communities of color and continues to disproportionately police our communities for the enforcement of marijuana laws.

Jeanette Ward, Executive Director of NuLeaf, an Oregon Based non-profit, stated:

> Research has proven that training and transparency methods are not effective solutions. As we all continue to see black men and women die at the hands of police officers across this country, we have to take a stand now, and start by ensuring dollars meant for our community reach our community.

Conclusion and Implications

Many states that have sanctioned recreational cannabis have established programs and protocols to favor licensure in neighborhoods that were also hit the hardest by cannabis related convictions and by poverty. These communities often are predominantly made up of African Americans. Many states have also addressed expungement of past cannabis-related convictions. So, with the recent deaths of Floyd and Taylor—and the outcry against discrimination turning towards police departments, perhaps it's not surprising that communities are examining defunding. Portland may be one of the first cities to address defunding from cannabis tax revenue.

The city budget was not unanimously approved and it will be voted on again sometime later in June. Because the budget vote was an emergency item, it required all four votes to pass. City Commissioner Chloe Eudaly specifically voted against the package, stating that the budget did not make enough cuts to police. Commissioner Hardesty criticized Commissioner Eudaly's "no" vote. "While we are making strides in realigning our budget with our values, this 'no' vote does nothing to materially support our BIPOC communities," Hardesty said. "All this does is delay the much-needed relief for our communities and continues to allow these units to exist for that much longer."
(Brittany Ortiz)

UNIQUE ISSUES TO CONSIDER WHEN PLANNING TO FINANCE A CANNABIS BUSINESS IN ILLINOIS

With the federal government taking the position that cannabis is strictly illegal—and with several states taking the opposite position—the decision to finance a state-legal cannabis business raises unique concerns aside from the inherent risks associated with funding any business. What follows is a guide of the unique issues to consider for potential investors seeking to enter the industry in Illinois.

Background

In November 2015, Illinois saw its first medical cannabis dispensaries open for business. Almost four years later, on May 31, 2019, Illinois became the first state in the country to legalize adult use cannabis through its legislature. On January 1, 2020, Illinois began legal adult use cannabis sales. The industry is creating many new companies all seeking license to grow, manufacture or sell cannabis or cannabis-infused products.

Current federal law classifies all cannabis possession and sale as criminal. 21 U.S.C. §801, *et seq*. As a result, the cannabis industry must operate completely in cash even in states where it's sold recreationally.

Financial Issues Unique to the Cannabis Industry

Lending to cannabis businesses has created a volatile situation for the federal government. On February 14, 2014, the United States Department of Treasury Financial Crime Enforcement Network (FinCEN) issued guidance regarding compliance with the Bank Secrecy Act and the requirements for filing suspicious activity reports by any financial institution insured by the Federal Deposit Insurance Corporation. *See*, www.fincen.gov/statutes_regs/guidance/pdf/FIN-2014-G001.pdf

Transformation of Cannabis–From Farm to Retail Product

However, some lenders (often from private equity) provide financing for cannabis businesses, here are some issues to consider when financing cannabis businesses.

How is cannabis to be categorized under the Uniform Commercial Code? While growing, or in a grown stage, cannabis is a "farm product." 810 ILCS 5/9-102(a)(34)(A) ("crops grown, growing, or to be grown"). Products of crops in their unmanufactured

state are also farm products. 810 ILCS 5/9-102(a)(34)(D).

In Illinois, either a licensed Adult Use Cultivation Center or a Craft Grower turn the cannabis farm products into inventory by manufacturing cannabis or cannabis-infused products. 410 ILCS 705/1-10. In Illinois, the cannabis leaving the cultivator is transformed from a farm product into inventory ready for sale at a licensed dispensary. The Illinois Cannabis Regulation and Tax Act requires the farmers to prepare their crops into a packaged and sealed container prior to it leaving their farms.

Once cannabis is harvested, the first step is to hang it to dry for preserving flavor before the farmers separate its valuable flowers from its other plant material through a process called trimming. The cannabis plants are cured after manicuring and trimming of the cannabis flowers. When the manicured cannabis is less than ten percent moisture, it is packaged and sold by weight. The trimmings and other materials that shake free from the cannabis flowers are typically turned into extracts or edible products. This transformation of the cannabis farm products converts it into inventory under the UCC. Because the supply chain requires the producer to turn the farm product into inventory, a lender financing a cannabis grow should include both inventory and crops in their security agreements.

Much like federal restrictions placed on patented seed discussed in §7.15 above, Illinois law places restrictions on who may grow or sell cannabis. A licensed cannabis cultivator may only sell its cannabis farm products or inventory to a state licensed dispensary. 410 ILCS 705/15-10, 410 ILCS 130/105(e). In turn, an Illinois medical cannabis dispensary may only sell its inventory to registered qualifying patients. 410 ILCS 130/180(d).

Financial Security Interests

While the licensed cultivation center or dispensary could grant a security interest in its farm products or inventory, it cannot grant a security interest in its state license to sell cannabis. Illinois medical cannabis law does not expressly prohibit granting security interests in the state licenses to sell cannabis, but the restrictions imposed by the state on the licensing issuance and renewal creates the presumption they cannot be used as collateral. 410 ILCS 130/85, 130/90, 130/115, 130/130. Further, the adult use cannabis laws also prohibit assigning the license or transferring it without state approval. 710 ILCS 705/15-60, 20-30, 30-30. Generally state laws provide that no security interest may attach to a liquor license, explosive license, or patent license. Cannabis licenses will probably be treated the same.

Obviously, no lender is licensed to possess or sell cannabis. Whether a cultivation center or a dispensary is a borrower, who may sell cannabis is strictly regulated. Therefore, upon default by the borrower the value of the cannabis farm product, or inventory, is nontransferable. If the borrower defaults, the lender can repossess and liquidate all the real estate and equipment of the cannabis business, but not the cannabis without state approval. The cannabis business entirely depends on its unique statutory rights to possess and sell cannabis. The most significant value of the borrower to the lender is its cash flow.

Imagine if the cannabis business operates outside the state law and the Drug Enforcement Administration (DEA) seizes the cannabis inventory in a raid. With the cannabis taken as evidence, it cannot be liquidated. For this scenario, the bank financing the cannabis inventory should value it at zero. The bank could require the cannabis business to hold cash in a collateral pledge agreement at some percentage of the value of the cannabis inventory. When the DEA walks away with the cannabis inventory, the bank can declare a default and setoff the cash.

Another option widely used in the cannabis industry for the lender is the amount of interest charged for the extra risk of the cannabis business loan. The loan could be structured only on buildings and equipment, as if the inventory creating the cash flow could go up in smoke at any time.

Conclusion and Implications

Lending to cannabis businesses is not yet common, or technically allowed at federal law. While federal legalization may not be far in the future, one thing is clear: Cannabis businesses will continue to be strictly regulated like those selling alcohol, tobacco, or pharmaceuticals. Valuing the cannabis inventory or farm products provides a new challenge to prospective commercial lenders. Through proper planning, a financial institution has several creative options available for collateralizing its loans to licensed cannabis businesses.
(Thomas Henry)

REGULATORY DEVELOPMENTS

CALIFORNIA BUREAU OF CANNABIS CONTROL ANNOUNCES MULTI-MILLION DOLLAR GRANT PROGRAM

Recently, the California Bureau of Cannabis Control, together with the Governor's Office of Business and Economic Development jointly announced a new grant program for the state's cannabis industry.

Background

The California Bureau of Cannabis Control (Bureau) is the lead agency in regulating commercial cannabis licenses for medical and adult-use cannabis in California. The Bureau is responsible for licensing retailers, distributors, testing laboratories, microbusinesses, and temporary cannabis events. Lori Ajax is the Bureau Chief.

The Governor's Office of Business and Economic Development (GO-Biz) serves as the State of California's:

> . . .leader for job growth and economic development efforts. GO-Biz offers a range of services to business owners including: attraction, retention and expansion services, site selection, permit streamlining, clearing of regulatory hurdles, small business assistance, international trade development, assistance with state government, and much more. (https://business.ca.gov)

GO-Biz also represents the cannabis industry.

California has continued to modify regulation of the cannabis industry—but recognizes that different parts of the state face a less than even playing field due to historic negative and disproportionate impacts due to previous cannabis criminalization. The program is aimed at addressing these impacts in the form of grants.

The Cannabis Grant Program

The April 21 announced a $30 million "California Cannabis Equity Grants Program" which provides for funding for local jurisdictions. The program:

> . . .focuses on the inclusion and support of individuals in California's legal cannabis marketplace who are from communities negatively or disproportionately impacted by cannabis criminalization. This is done through small business support services like technical assistance to individuals, reduced licensing fees or waived fees, assistance in recruitment, training, and retention of a qualified and diverse workforce, and business resilience such as emergency preparedness.

The program plans on:

> At least $23 million of the funding, in the form of low/no-interest loans or grants, will be directly allocated to applicants and licensees specifically identified by local jurisdictions as being from communities most harmed by cannabis prohibition. To date, jurisdictions seeking to create this inclusive regulatory framework represent roughly a quarter of the state's population

Governor Newsom's Senior Advisor on Cannabis, Nicole Elliott, addressed in a press release recently the program as follows:

> These Cannabis Equity Grants reflect California's desire to lead our legalization efforts with equity and inclusivity. . . .We applaud these jurisdictions for not only embracing the challenge of creating pathways to participate in a legitimate cannabis marketplace, but for doing so in a thoughtful way that seeks to uplift all communities. It is our hope that these efforts lead to the creation of a truly diverse industry and that these programs serve as a blueprint for others who share in our commitment to address systemic discrimination and create real prosperity for all.

Equity Assessment and Program Development

In terms of grant money to assist in addressing equity assessment and program development, the

grant program with allocate money as follows, totaling $1,149,038:

- Lake County: $150,000
- Monterey County: $150,000
- Nevada County: $149,999
- City of Palm Springs: $149,397
- City of San Jose: $149,300
- City of Santa Cruz: $147,666
- City of Clear Lake: $98,783
- City of Coachella: $93,783
- City of Stockton: $60,000

Licensure

In terms of funding for licensure, the program provides as follows, totaling $28,850,961:

- City of Oakland: $6,576,705
- City of Los Angeles: $6,042,104
- City and County of San Francisco: $4,995,000
- City of Sacramento: $3,831,955
- City of Long Beach: $2,700,000
- Humboldt County: $2,459,581
- Mendocino County: $2,245,704

Conclusion and Implications

Many states that have sanctioned recreational cannabis have established regulations that address their perception that licensure will not be a level playing field in areas that were hit the hardest in terms of past criminal conviction for cannabis related crimes. They also frequently address measures to expunge or otherwise mitigate past criminal convictions for cannabis possession. California is no different and with the announcement of the $30 million grant program, the Bureau is trying to better level the playing field for cannabis business in the state.

For more information regarding the Bureau of Cannabis Control's grant program, *see:* https://www.bcc.ca.gov/about_us/documents/media_20200421.pdf

CALIFORNIA CANNABIS CULTIVATORS TAKE NOTE: STATE WATER RESOURCES CONTROL BOARD ADOPTS PERMANENT MONTHLY WATER USE REPORTING REQUIREMENTS

Building upon its emergency regulations imposed during the incredible drought years of 2014 and 2017, the California State Water Resources Control Board (SWRCB) recently made permanent regulations mandating urban water suppliers to track and report monthly water usage. This may impact cannabis cultivators.

Background

During California's recent historic drought, the SWRCB adopted emergency regulations that required California's largest water suppliers—those with more than 3,000 connections or supplying more than 3,000 acre-feet of water annually—to track and report monthly water usage. These urban water suppliers collectively represent the state's 400 largest water suppliers and serve approximately 90 percent of the state's population. The regulations were put into effect generally from July 2014 through November 2017, in an effort to maximize water conservation throughout the state. Many considered those efforts largely successful. Between June 2015 and March 2017 California's urban water suppliers collectively conserved 22.5 percent water use compared to prior years, enough to supply approximately one-third state's population for one year.

In late 2017, the SWRCB modified the reporting mandates and generally transitioned toward voluntary reporting. Notwithstanding that transition, more

than 75 percent of water suppliers have continued to report their monthly water usage voluntarily. In May 2018, the Governor signed into law water efficiency legislation that authorized the SWRCB to issue permanent mandatory monthly water use requirements on a non-emergency basis.

Monthly Reporting Requirements

The new SWRCB regulation requires water suppliers to report residential water use, total potable water production, measures implemented to encourage water conservation and local enforcement actions. Specifically, the regulation requires reporting of the following:

- The urban water supplier's public water system identification number(s);
- The urban water supplier's volume of total potable water production, including water provided by a wholesaler, in the preceding calendar month;
- The population served by the urban water supplier during the reporting period;
- The percent residential use that occurred during the reporting period;
- The water shortage response action levels.

The SWRCB considers these measures as part of the state's long-term plan to prepare California for future droughts. The regulation increases transparency and access to important and timely water data, and in a format consistent with reporting provided since 2014.

In adopting the regulation, the Chairman of the SWRCB stated:

> As we continue to see, the quality, timeliness, and gathering of data are critical to managing California's water in the 21st century. Urban monthly water use data have driven enduring, widespread, public awareness and understanding of water use, conservation and efficiency in our state.

The regulation now moves to the Office of Administrative Law for review and is expected to take effect October 1, 2020.

Conclusion and Implications

The recently adopted regulation will likely assist policy makers in making important and better-informed water resources management decisions moving forward. It will also help water managers and Californians working together to monitor statewide and local water usage conditions and improve effectiveness in responding to future water shortage challenges. Though reporting is once again mandatory, with more than 75 percent of water suppliers already voluntarily reporting water usage during the past three years, many are observing what appears to be a post-drought culture change among stakeholders who have taken greater ownership and responsibility in achieving water conservation. This recent move could potentially strengthen that dynamic and continue to yield increased conservation results. For more information, *see:* https://www.waterboards.ca.gov/press_room/press_releases/2020/pr04212020_swrcb_adopts_water_conserv_rpt_req.pdf
(Chris Carrillo, Derek R. Hoffman)

LEGISLATIVE DEVELOPMENTS

HOUSE DEMOCRATS URGE COLLEAGUES TO PURSUE MARIJUANA REFORM IN SUPPORT OF RACIAL JUSTICE VIA THE MARIJUANA OPPORTUNITY, REINVESTMENT, AND EXPUNGEMENT ACT

While Congressional Democrats are pushing for broad policing reform legislation, Repsentatives Earl Blumenauer (D-OR) and Barbara Lee (D-CA) circulated a sign-on "Dear Colleague" letter urging fellow lawmakers to "consider another crucial issue toward criminal justice reform: eliminating the failed prohibition on cannabis."

Democratic Efforts to Move the Federal Government on Cannabis

The criminalization of marijuana has long contributed to the disproportionate incarceration of minorities, particularly African Americans. The letter states:

> We have all seen the pernicious effects of selective enforcement of cannabis prohibition across the country, and it is not just in red states or rural Republican America. We have seen for the last 50 years the cannabis prohibition used disproportionately against people of color, especially young Black men. The use of cannabis is fairly uniform across different racial groups, but the people caught up in the net of cannabis enforcement are heavily skewed towards these young Black men. In Manhattan, until recently, Black people were eight times more likely to be arrested than white people, even though, as stated, the rate of use is the same. This placed too many under the pressure of selective and discriminatory enforcement, the threat of mandatory minimums, and overly punitive three-strikes and you're out sentencing laws.
>
> This often resulted in innocent people pleading guilty with district attorneys in order to avoid being prosecuted under much more stringent terms with harsh penalties almost assured.
>
> It is time that we as Democrats take a stand against this pernicious hold-over from Richard Nixon's blatant attempt at criminalizing the behavior of African Americans. These policies have resulted in an explosion of the American prison population. The prison population in 1970 was 372,000 people; this exploded by a factor of 300 [percent] by 1990, almost doubled again by the year 2000, and currently is 2.3 million. The statistics of racial disparities in the corrections system are appalling, known to us all, and driven by non-violent drug offenses coupled with selective enforcement.

The Marijuana Opportunity, Reinvestment, and Expungement (MORE) Act

Representatives Blumenauer and Lee stated that the simplest step toward tackling criminal justice reform through marijuana reform would be by passing the Marijuana Opportunity, Reinvestment, and Expungement (MORE) Act. The letter goes on to state:

> This carefully crafted legislation will legalize cannabis, provide restorative justice to communities of color torn apart by the failed War on Drugs, stop the nonsense of not being able to research it, remove the barriers to people getting medicine, and eliminate the impacts of cannabis prohibition on educational funding and access to public housing.

The MORE Act was sponsored by Judiciary Committee Chairman Jerrold Nadler (D-NY) and currently awaits floor action.

The policing reform bill filed by Democratic leaders contains no language addressing marijuana legality and instead focuses on more direct items, such as banning no-knock raids in drug cases. The bill is expected to be voted on in the House Judiciary Committee this week. However, Representative Blumenauer released a police accountability plan that specifically focuses on cannabis decriminalization in

order to effectuate a reduction of over-policing communities of color.

States that Have Legalized Cannabis Have Included Social Justice Provisions

Other state leaders also recognize the role marijuana criminalization plays in racial injustices. California Governor Gavin Newsome echoed the call to legalize marijuana, describing it as a "civil rights" issue. Virginia Governor Ralph Northam noted that the passage of cannabis decriminalization legalization in his state is representative of the efforts to address racial inequities.

Even Nora Volkow, Director of the National Institute On Drug Abuse (NIDA) recently acknowledged racial disparities in drug enforcement, to which she admitted is more harmful than marijuana itself. "Whites and Black/African Americans use drugs at similar rates, but it is overwhelmingly the latter group who are singled out for arrest and incarceration. This use of drug use and addiction as a lever to suppress people of a particular race has had devastating effects on communities of color," Volkow stated.

Conclusion and Implications

To date, Congress has achieved little traction in decriminalization of cannabis. The Farm Bill was the most traction to date. The linkage to cannabis convictions and discrimination might indeed be pushing the federal government towards decriminalization. But most certainly, with the light shining bright on the alleged discrimination-motivated deaths of George Floyd and Breonna Taylor by the police, Congress may be ready to move forward on the Marijuana Opportunity, Reinvestment, and Expungement Act.

While most lawmakers continue to note the importance of directly reforming policing in order promote racial justice, the push toward improving other areas of the law that systemically perpetuate racial injustice is clearly not without consideration. As the Dear Colleague letter states in closing, "It's not all about chokeholds and the police, it's about blatant, discriminatory, irrational drug laws that have destroyed so many lives. We urge you to join us." (Brittany Ortiz)

JUDICIAL DEVELOPMENTS

CALIFORNIA SUPERIOR COURT ORDERS SHERIFF'S DEPARTMENT RETURN OF OVER $600,000 IN CASH AND $1,000,000 IN CANNABIS TO LICENSED BUSINESS TAKEN DURING RAID

Eagle Bay Enterprises, Inc., DBA Procan Labs v. State of California,
Case No. 2-cv-00590 (Santa Barbara Super. Ct. 2020).

On January 22, 2020, the Santa Barbara County, California Sheriff's Department served a search warrant and raided Arroyo Verde Farms Inc. (Arroyo Verde). According to a January 31, 2020 press release from the Santa Barbara County Sheriffs, the raid on Arroyo Verde yielded $620,998 in cash related to black market cannabis transaction, a small extraction lab, 20 pounds of illegally stored cannabis, and 1,800 pounds of cannabis oil worth about $1,000,000 belonging to Eagle Bay Enterprises, Inc. dba Procan Labs (Procan). According to a May 15, 2020 order from Santa Barbara County Superior Court Judge Thomas Anderle, Arroyo Verde is a licensed cannabis grower and transporter in Carpinteria, California and Procan is licensed to manufacture cannabis oil from cannabis biomass, which it then sells to licensed distributors. Consequently, Judge Anderle ordered the seized property to be returned by the Santa Barbara County Sheriff's Department.

Background

The Sheriff's Department conducted the search because of suspicions that Arroyo Verde and its owner, Barry Brand, were growing and processing cannabis outside the permitted parcels, as well as storing and selling cannabis oil without a valid license. According to an industry survey by Cannabiz Media, 398 cultivation licenses have been issued in Santa Barbara County and last year, more cultivation licenses were issued in Santa Barbara County than in Humboldt County and Mendocino County

According to Cannabiz Media, Santa Barbara has issued 398 cultivation licenses since the legalization of marijuana. Last summer, the county obtained more state licenses for growers than Humboldt county and Mendocino county. Some indications existed that the raid was at least in part due to Brand's involvement in promoting the cannabis industry within Santa Barbara County, including donating $10,000 to the campaigns of two pro-cannabis county supervisors.

The cannabis oil seized in the raid is packaged in 323 bottles that were sent by Procan to Arroyo Verde in six shipments between December 18, 2019 and January 14, 2020. These shipments were inputted into METRC, the state's "seed-to-sell" cannabis tracking system. Procan provided the cannabis oil to Arroyo Verde for transport to a cannabis distributor, Kanna Kingdom, LLC ("Kanna") that was interested in the product.

Legal Proceedings

Following the raid of Arroyo Verde and seizure of Procan's cannabis and cash, the State of California filed a petition for forfeiture in the aptly named case of *The People of the State of California v. Six Hundred Twenty Thousand Nine Hundred Ninety Eight Dollars ($620,998.00) U.S. Currency*, Case No. 20CV00590.. The forfeiture was filed on the basis that the cannabis product and cash being the product and proceeds from unlicensed cannabis activity.

In opposition to the forfeiture, Procan filed a motion to compel the return of the cannabis oil on the basis that it is a licensed manufacturer of cannabis oil and was the legal owner of the cannabis oil seized by the Sheriff's Department in its raid of Arroyo Verde. Procan subsequently amended its motion to also seek the return of the cash seized in the raid. The state argued that in addition to being the product of illegal activity, the cannabis oil should not be returned to Procan because it was part of an ongoing criminal case involving Arroyo Verde and Mr. Brand. To date there is no pending criminal proceeding against Arroyo Verde or Mr. Brand.

In arguing that the seized property should not be returned to Procan, one argument put forth by the state was that Procan knew that Arroyo Verde would

store the product at its facilities. Procan denies this claim. The reason this fact is relevant is that transport licenses "shall not engage in the wholesale packaging, labeling, or storing of cannabis goods."

The Superior Court's Decision

Judge Anderle ultimately ordered that Procan "committed no crime, much less intentionally committed a crime" and ordered the seized property to be released to them.

In coming to this conclusion, the court noted a number of factors weighing in favor of the return of this product. First, the lack of charges against Arroyo Verde, Mr. Brand, or Procan weighed in favor of the product being returned. This was further reinforced by the state's ability to prove that the property was seized at any future criminal proceeding even without the physical evidence but instead through the use of photographs, stipulations, and the testimony of the Sheriff's Deputies who took part in the raid.

Second, the court looked to the harms suffered by Procan as a result of the raid. The cannabis oil seized by the Sheriff's Department represents approximately 65 percent of Procan's inventory. In the wake of the raid, Procan was forced to cut 40 percent of its staff. In looking at that reduction in staff, the court further noted that it was necessary prior to, and therefore unrelated to, the COVID-19 outbreak. The court found that this seizure could force Procan to shutter its business and that the Procan's interest in having the seized property returned weighed much more strongly than the state's "claimed need" to retain the property as evidence.

Key Takeaway for Cannabis Licensees

Procan claims it was unaware that Arroyo Verde was intending to store its product at its facilities in violation of its licenses. While this seems like an innocent mistake in this case where an interested buyer for the product, Kanna, had already been found and Arroyo Verde (a licensed transporter) was hired to transport the product, this situation is avoidable. Cannabis licensees should ensure that in addition to carefully following the procedures of the track and trace system, they are closely monitoring the license status, requirements, and limitations of their business partners. While this type of administrative detail seems onerous, especially for smaller licensees, it would go a long way towards limiting the type of situation Procan found itself in.

Does Seizure of Cannabis 'Adulterate' the Product?

One additional argument the state made in favor of it retaining the seized cannabis oil was that the oil was adulterated and therefore unsaleable once the chain of custody was broken by the seizure. The court did not rule on this issue and instead stated that it was up to Procan and state cannabis regulators to determine whether the cannabis oil can be lawfully sold once returned to Procan.

Conclusion and Implications

While the court did not opine on this issue and state regulators have not addressed this concern, the result of concluding as the state argued that any cannabis product that is seized in a law enforcement action becomes tainted should be troubling to all lawful operators. This conclusion would mean that any lawful inventory could at any point be tainted by law enforcement, even if as was the case here its seizure was ultimately found to have been in error by a court. In the wake of this case, this issue is likely to be something that California's cannabis regulators will address in refining the track and trace system to account for these situations where lawful operators find themselves and their inventory in a situation much like Procan.

(Andreas L. Booher, Nataliya Shtevnina)

MICHIGAN SUPREME COURT HOLDS MUNICIPAL LAND USE AUTHORITY ADDRESSING CULTIVATION OF MEDICAL MARIJUANA WAS NOT PREEMPTED BY THE STATE'S MEDICAL CANNABIS ACT

Deruiter v. Township of Byron, Case No. 158311 (Mich. Apr. 27, 2021).

Recently, the Michigan Supreme Court was faced with the apparent conflict between the state's medical marijuana act, which authorized medical cannabis cultivation by a registered primary caregiver and a municipality's zoning ordinance that added permitting requirements before cultivation would be deemed legal. The state Court of Appeals affirmed the trial court judgment that state law preemption trumped the municipal ordinance for home-occupation permitting. The Supreme Court overturned the judgment, finding that legal concepts of state preemption did not take away the inherent authority of the municipality to regulate land use pursuant to state law.

Factual Background

Christie DeRuiter, a registered qualifying medical marijuana patient and a registered primary caregiver to qualifying patients, cultivated marijuana in an enclosed, locked facility at a commercially zoned property she rented in Byron Township. She did not obtain a permit from the township before cultivating the medical marijuana as a primary caregiver. At the township's direction, DeRuiter's landlord ordered her to stop cultivating medical marijuana at the property or face legal action. When the township attempted to enforce its zoning ordinance, DeRuiter filed the instant action, seeking a declaratory judgment regarding the ordinance's legality.

Legal and Procedural Background

The case centered on the apparent conflict between the township's zoning ordinance authority that required primary caregivers to obtain a permit and pay a fee before using a building or structure within the township to cultivate medical marijuana. The ordinance further specified that the caregiver wishing to cultivate cannabis must do so within a dwelling or garage in a residentially zoned area within the township as part of a regulated home occupation at a full-time residence.

Michigan has a statute that regulates medicinal cannabis cultivation: the Michigan Medical Marihuana Act (MMMA), MCL 333.26421, *et seq*. Under MCL 333.26424(b)(2), primary caregivers and qualifying patients must keep their plants in an enclosed, locked facility in order for those individuals to be entitled to the MMMA protections in MCL 333.26424(a) and (b).

The argument of alleged state law preemption was based on the apparent conflict between the MMMA and the zoning ordinance authority regarding occupancy requirements for cultivation.

The Michigan Court of Appeals [325 Mich. App 275 (2018).] affirmed the trial court judgment, concluding that the MMMA preempted defendant's home-occupation zoning ordinance because the ordinance directly conflicted with the MMMA by prohibiting what the MMMA permitted and because the ordinance improperly imposed regulations and penalties upon persons who engage in the MMMA-compliant medical use of marijuana.

The Michigan Supreme Court's Decision

Cutting the chase, the Supreme Court reversed the decision of the Court of Appeals, finding no inherent conflict or state law preemption of the home-occupancy zoning ordinance.

The Land Use Authority and the MMMA

The Court found that:

> Under the conflict-preemption doctrine, the MMMA does not nullify a municipality's inherent authority to regulate land use under the Michigan Zoning Enabling Act (MZEA), MCL 125.3101 *et seq*., as long as (1) the municipality does not prohibit or penalize the cultivation of medical marijuana and (2) the municipality does not impose regulations that are unreasonable and inconsistent with regulations established by state law.

In addressing the zoning authority of a municipality, the Court stated that:

> Generally, local governments may control and regulate matters of local concern when that power is conferred by the state. However, state law may preempt a local regulation either expressly or by implication. Implied preemption can occur when the state has occupied the entire field of regulation in a certain area (field preemption) or when a local regulation directly conflicts with state law (conflict preemption). A direct conflict exists when the ordinance permits what the statute prohibits or the ordinance prohibits what the statute permits; there is no conflict between state and local law when a locality enacts regulations that are not unreasonable and inconsistent with regulations established by state law so long as the state regulatory scheme does not occupy the field.

The Court went on to state that:

> . . .while a local ordinance is preempted when it bans an activity that is authorized and regulated by state law, a local governmental unit may add to the conditions in a statute as long as the additional requirements do not contradict the requirements set forth in the statute.

Focusing on the immunity from prosecution portion of the MMMA, the Court pointed out that the act:

> provide[s] that qualifying patients and primary caregivers are immune from arrest, prosecution, or penalty in any manner, including, but not limited to, civil penalty or disciplinary action for the medical use of marijuana in accordance with the MMMA. In turn, MCL 333.26424(b)(2) provides that primary caregivers and qualifying patients must keep their plants in an enclosed, locked facility in order to qualify for the immunity. This requirement sets forth the type of structure marijuana plants must be kept and grown in for a patient or a caregiver to be entitled to the MMMA protections in MCL 333.26424(a) and (b), but the provision *does not* address where marijuana may be grown (Emphasis added).

Addressing the zoning ordinance and apparent conflict with and preemption by the MMMA, the Court found that the local ordinance conflicts with the MMMA when the ordinance results in "a complete *prohibition* of the medical use of marijuana; however, the MMMA does not foreclose all local regulation of marijuana"

The Court went on to focus on the zoning ordinance. In recognizing the scope of the local authority to regulate land within its borders, the Court found *this* zoning ordinance neither prohibited cannabis cultivation, nor did the Court feel the regulation unreasonable:

> . . .the [MMMA] does not nullify a municipality's inherent authority to regulate land use under the MZEA as long as (1) the municipality does not prohibit or penalize the cultivation of medical marijuana and (2) the municipality does not impose regulations that are unreasonable and inconsistent with regulations established by state law. Because an enclosed, locked facility may be found in various locations on various types of property, a local regulation limiting where medical marijuana must be cultivated within a locality does not conflict with the statutory requirement that marijuana plants be kept in an enclosed, locked facility.

In concluding that no conflict between the ordinance and the MMMA existed, and no argument as to state preemption applied here, the Court distilled its position as follows:

> In this case, the township's ordinance allowed for the medical use of marijuana by a registered primary caregiver but placed limitations on where the caregiver could cultivate marijuana within the township. The ordinance's geographical restriction added to and complemented the limitations imposed by the MMMA; it did not directly conflict with the MMMA. While the ordinance went further in its regulation than the MMMA, the township appropriately used its authority under the MZEA to craft an ordinance that did not directly conflict with the MMMA's provision requiring that marijuana be cultivated in an enclosed, locked facility. The township also had authority under the MZEA to require zoning permits and permit fees for the use of

buildings and structures within its jurisdiction. The township's ordinance requiring primary caregivers to obtain a permit and pay a fee before using a building or structure within the township to cultivate medical marijuana did not directly conflict with the MMMA because the ordinance did not effectively prohibit the medical use of marijuana, and DeRuiter did not argue that the requirements for obtaining a permit were so unreasonable as to create a conflict.

Conclusion and Implications

In this case, the Michigan Supreme Court affirmed the ability of municipalities within the state to layer on certain conditions for medicinal cannabis cultivation so long as those conditions didn't go so far as to prohibit cultivation rights guaranteed under the MMMA or rise to the level of highly burdensome. Here, the Court found that the occupancy requirement and the need for a permit established by the township was well within their zoning authority: "the township appropriately used its authority. . .to craft an ordinance that did not directly conflict with the MMMA's provision requiring that marijuana be cultivated in an enclosed, locked facility. The township also had authority under the MZEA to require zoning permits and permit fees for the use of buildings and structures. . . .[none of this]. . .directly conflict[ed] with the MMMA because the ordinance did not effectively prohibit the medical use of marijuana."

Municipalities in Michigan will undoubtedly be emboldened by this decision in exploring zoning requirements and permit fees for medical cannabis cultivation in their jurisdictions. The Court's opinion is available online at: https://courts.michigan.gov/Courts/MichiganSupremeCourt/Clerks/Recent%20Opinions/19-20-Term-Opinions/158311.pdf
(Robert Schuster)

WASHINGTON STATE COURT OF APPEALS REJECTS VESTED RIGHT LAND USE ARGUMENT FOR CANNABIS GROW FACILITY

SEVEN HILL, LLC, et al. v. Chelan County, Washington,
Case No. 36439-9-III *Unpub.* (Wash.App. Apr. 23, 2020).

A Washington State limited liability company received a citation for operating a cannabis manufacturing facility in Chelan County without permits. The company was operating legally under the state's laws and regulations. Later in time, the county established a ban on such cannabis production. In what in essence was a land use law/zoning matter, the county deemed the activity a non-conforming us of the property. In an unpublished opinion, the Washington Court of Appeals affirmed the action of the county rejecting the argument that the business had the right to continue a non-conforming use after the county's moratorium was established because it established a vested right to do so.

Background

Washington State voters, in 2012, approved "Initiative 502." The initiative was sent to the Washington Secretary of State in the summer or 2011 with enough signatures to permit it appear on the November 2012 general state ballot legalizing recreational cannabis. The ballot measure passed by a margin of approximately 56 to 44 percent. The initiative:

> . . .legalized the production, possession, delivery and distribution of marijuana. The initiative regulated the sale of small amounts of marijuana to people 21 and older. According to reports, marijuana farms and food processors would be licensed by the Washington State Liquor Control Board (https://ballotpedia.org/Washington_Marijuana_Legalization_and_Regulation,_Initiative_502_(2012))

As is the case with many states that have legalized recreational cannabis, Washington gave municipalities the ability to ban recreational cannabis sales and production within their jurisdiction. In late 2014, Seven Hills, LLC wanted to establish a cannabis production facility in the county and at the time, no restrictions on such production existed. Production

began on land owned by co-appellant Water Works Properties. Seven Hills also applied for a license to allow cannabis production from the Washington State Liquor and Cannabis Board (WSLCB). That state license was granted to Seven Hills on January 26, 2016.

Two weeks later, Chelan County established a permanent ban on such production. The county had a temporary moratorium on the production but the parties disagreed when notice to the county was established but it is understood that the state license came four months after the county had established a temporary moratorium.

What was not disputed is that Seven Hills did receive a permit from the county in May 2015 to build a fence around the property. Greenhouses were built and the county approved installation of five propane tanks on November 2015 to heat the greenhouses. Seven Hills never sought final approval for the propane installations.

In July 2016 a county code enforcement officer observed the greenhouses and the county issued a notice of violation o September 16 for:

> 1) Production and/or Processing of Marijuana or Cannabis in Violation of Chelan County Resolution 2016-014.
>
> 2) Unpermitted Buildings in Violation of IBC [International Building Code] [2012] section 105.
>
> 3) Operation of a Propane Tank in Violation of Building Permit No. 150687 and the International Fire Code (IFC) [2012] [A]105.3.3.
>
> 4) Maintaining a Nuisance in Violation of CCC [Chelan County Code] 16.02.030. (*Seven Hills LLC*)

With the violation citations, Seven Hills was ordered to cease and desist production and processing of cannabis, and was further ordered to remove all plants, growing structures and propane tanks.

The Superior Court affirmed that actions of the county. This appeal followed.

The Court of Appeals Decision

There were procedural arguments the court addressed. But the crux of the decision addressed the claim made by Seven Hills that it had established under land use law a vested right that the county could not deny.

The Vested Nonconforming Use Claim

The court stated that the "one substantive issue is whether or not Seven Hill had established it was operating its production business as a nonconforming use prior to the moratorium"

The court espoused the law of such a right as follows:

> The right to continue a nonconforming use despite a zoning ordinance which prohibits such a use in the area is sometimes referred to as a 'protected' or 'vested' right. (Citations omitted) A nonconforming use is a use which lawfully existed prior to the enactment of a zoning ordinance, and which is maintained after the effective date of the ordinance, although it does not comply with the zoning restrictions applicable to the district in which it is situated. (Citations omitted) The landowner bears the burden of establishing that a valid nonconforming use exists. (Ibid)

As some production occurred before the state had licensed the grow, the court stated that:

> In light of this statutory scheme, we do not believe that anyone could have a valid right to produce marijuana prior to the time the WSLCB authorized the activity. Here, Seven Hills did not obtain a valid license to produce marijuana until January 26, 2016.

On January 26 the county's temporary moratorium was already in place, therefore "there could be no valid nonconforming use at that time."

As to the argument that the site preparations may have given Seven Hills a vested right. The court shot this argument down as well:

> Erecting a fence does not establish [that] one is producing marijuana. Constructing a temporary greenhouse likewise does not establish lawful production of marijuana.

Conclusion and Implications

This case presents some interesting issues of law in the cannabis/land use area. Here the court found the facts such that Seven Hills hadn't actually established cannabis production prior to the county's temporary moratorium on production. That might explain the court's order not to publish the decision. However, it begs the question: in a state that allows for cannabis grows, if one begins production in a county without a moratorium on such grows, which later enacts a moratorium, would there be a valid argument of a land use vested interest?

The court's decision is available online at: http://www.courts.wa.gov/opinions/pdf/364399_unp.pdf
(Robert Schuster)

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