Primer on MAUCRSA Co-Location Rules

Introduction

Note: *The following is intended as an information overview on current California law changes. It will become outdated as laws change, and you should consult with an attorney before acting on the information herein.*

On Thursday, June 15 as part of the state budget the California Legislature approved Senate Bill 94, which enacts the Medicinal and Adult-Use Cannabis Regulation and Safety Act (MAUCRSA). The new law reconciles the differences between the Adult Use of Marijuana Act (AUMA) and the Medical Cannabis Regulation and Safety Act (MCRSA), and unifies the adult-use and medicinal markets within the same regulatory regime.

MAUCRSA repeals all the vertical integration prohibitions in MCRSA. While operators are generally allowed to cross-license, there are some important rules and limitations. This paper outlines general issues and the relevant provisions of MAUCRSA those looking to co-locate should be aware of.

Vertical Integration Rules

Generally, there are no longer any restrictions on cross-licensure for both adult-use and medical licensees. There are two important exceptions:

- Testing licensees need to be independent. Those licensed in other categories cannot have an ownership interest in a testing license and vice versa.
- A Type 5 licensee (large scale cultivation for over one acre or over 22,000 square feet of canopy) may not hold a Type 8 (Testing), Type 11 (Distributor) or Type 12 (Microbusiness) license. We note that Type 5 licenses are not available until 2023.

Co-location

In September, the Governor signed Assembly Bill 133 to clarify that a licensee can co-locate multiple licenses within the same premises. The law allows a licensee to house multiple licenses within the same premise, but it is important to note that multiple licensees cannot co-locate on the same premises. For example, a cultivator licensee who is also licensed as a distributor would be able to locate both licenses within the same premises. However, a cultivator and distributor that are owned by separate entities would not be allowed to locate in the same premises. Licensing agencies will likely discourage different licensed activities on the same premises without walls or immovable barriers clearly distinguishing each activity.

Under MAUCRSA, a "premises" is currently defined as "the designated structure or structures and land specified in the application that is owned, leased, or otherwise held under the control of the applicant or licensee where the commercial cannabis activity will be or is conducted**. The premises shall be a contiguous area and shall only be occupied by one licensee**" (*emphasis added*).

Note: See Important Definitions and Provisions *section below.*

With the passage of AB 133, a licensee is now allowed to co-locate multiple licenses within the same premises, including medical and adult-use licenses, but most likely would need to have discrete units that are completely separated for each activity (e.g. manufacturing and cultivation) or a system to track products within each of the medical and adult-use regime. Further information and the specific rules associated with col-location will be specified in emergency regulations which are expected to be released in late November 2017. These emergency regulations would then be readdressed during 2018 with additional amendments expected.

Premises Diagram

As part of the license application process, applicants will need to submit a premises diagram. This is a critical component of the application as the premises diagram will determine what is and is not permissible in the same premises. For instance, while the Bureau of Cannabis Control (Bureau) has attempted to discourage multiple activities in the same space, there is a recognition that distribution and manufacturing in the same room makes sense.

On the issue of one applicant owning and occupying contiguous buildings, regulatory agencies have implied that only one application for licensure would be required if only one licensed activity was being conducted in the same general area, but that all buildings would need to be captured as part of the applicant's premise diagram and could not be separated by a public road.

While medical regulations proposed in May have been officially withdrawn, it can be assumed that the licensing entities will be using much of this language as a first draft for the regulations required to implement MAUCRSA. Under the proposed medical regulations, a premises diagram was described as follows:

> ***Section 5012. Premises Diagram***
>
> *An applicant shall submit to the bureau with his or her application a complete and detailed diagram of the proposed premises.*
>
> *(a) The diagram must show the boundaries of the property and the proposed premises to be licensed, showing all boundaries, dimensions, entrances and exits, interior partitions, walls, rooms, windows, doorways, and common or shared entryways. The diagram must show the areas in which all commercial cannabis activities will take place, including but not limited to, limited- access areas.*
>
> *(b) The diagram must be to scale.*
>
> *(c) The diagram shall not contain any highlighting.*
>
> *(d) If the proposed premises consists of only a portion of a property, the diagram must be labeled indicating which part of the property is the proposed premises and what the remaining property is used for.*

With the issue being in flux, it is difficult to say with certainty what the co-location rules will look like. We should have a better idea when emergency regulations are released in late November.

Cannabis Cooperatives

MAUCRSA allows cultivators who hold Type 1 or Type 2 cultivation licenses to form Cannabis Cooperative Associations. The purpose of these cooperative associations is to facilitate business cooperation between small cultivators and allow for these businesses to coordinate production, marketing, and sales. New cannabis businesses can no longer use "cannabis cooperative" within their corporate name unless they are structured pursuant to the rules for Cannabis Cooperative Associations under MAUCRSA.

Specifically, a Cannabis Cooperative Association may engage in any activity in connection with the growing, harvesting, curing, drying, trimming, packing, grading, storing, or handling of cannabis that is produced or delivered to it by its members; or any activity in connection with the purchase, hiring, or use by its members of supplies, machinery, or equipment, or in the financing of any such activities.

A cannabis cooperative would need to be made up of three or more people engaged in cultivation. Collectively, a cooperative would be prohibited from growing on more than four acres of total canopy. Cooperatives would also need to file articles of incorporation with the state and enact bylaws that set out rules and responsibilities for association members, stockholders, directors, and officers. The affairs of cannabis cooperatives would need to be managed by a board elected by members and stockholders.

***Note**: See Chapter 22 (commencing with Section 26220) of Division 10 of the Business and Professions Code for statutes relating to Cannabis Cooperative Associations*.

Potential Scenarios

MAUCRSA provides the broad framework that regulators and local governments will reference when developing state and local regulation. We will not know the specifics regarding the build-out of licensed premises, co-location, and other requirements until state regulators issue final regulations and local jurisdictions establish ordinances.

Some scenarios being contemplated by industry operators are discussed below considering the current rules in MAUCRSA. Ultimately, these interpretations may change as state and local regulations are developed and legislation is passed.

An individual buys 10 acres of land and subdivides it into 10 1-acre premises. There are no physical barriers that separate premises. The operator offers space in each premises to multiple companies.

- MAUCRSA would not prevent the acquisition of 10 acres or subdivision of the total property *if it was adequately divided with barriers into separate premises that complied with the size and operation requirements applicable to each individual license*. That does not necessarily mean the sale would be authorized. State and local laws relating to property acquisition and subdivision would still apply.
- To be compliant, the land would need to be divided into self-sufficient premises that complied with the state requirements for co-located premises and each had a site plan. Under MAUCRSA a premises would need to be a contiguous area only occupied by one licensee. Exactly how premises will need to be divided and secured will be provided in state regulations and local ordinances. For example, in their proposed manufacturing regulations the California

Department of Public Health would require "establishing physical barriers to secure perimeter access and all points of entry into a manufacturing premises." Physical barriers to separate different premises will most likely be required.

- Under MAUCRSA, a premises would be limited to one licensee. In the above scenario multiple licensees could not be housed within the same premises nor could multiple licensees share facilities.
- There could be no common space between each premises except for ancillary space such as parking or changing areas. So, for each license parcel all designated areas for cure, packaging, storage and trimming would need to be duplicated. This means that while the canopy limit for outdoor cultivation is 1 acre, with building duplication the 10-acre parcel will likely only be able to house approximately 5-7 licenses.

An operator wishes to hold multiple cultivation licenses of Type 1, 2 or 3 such that while the premises for each license falls within the applicable square footage requirements of such license, the total canopy such operator controls is much greater.

- Under the MCRSA, which was repealed by MAUCRSA, operators would have been limited to no more than four acres of total cultivation canopy. This four acre limitation was repealed by MAUCRSA, though Cannabis Cooperative Associations are still prohibited from growing on more than four acres of total canopy.
- MAUCRSA requires that the California Department of Food and Agriculture (CDFA) limit the number of Type 3, 3A, and 3B licenses allowed. Exactly how this limitation will be imposed is unclear. In draft CFDA regulations for medicinal cannabis that have been officially withdrawn, the Department limited operators to one Type 3, 3A, or 3B license unless the operator also held a Type 10A Producing Dispensary License, which no longer exists within the regulatory framework.
- While a limitation will be imposed on Type 3, 3A, and 3B licenses, there is no statutory requirement to impose limitations on the number of licenses issued for cultivation on 10,000 square feet or less of canopy.
- For example, say an operator is seeking 40,000 square feet of indoor cultivation canopy all within the same structure. MAUCRSA would allow the operator to obtain a Type 3A license for up to 22,000 square feet of canopy and two Type 2A licenses for the remaining 18,000 square feet of canopy. Canopy limitations are imposed per premises, but the statute allows for multiple premises to be located within the same structure or building. The operator will likely be required to establish barriers or physical separation between each cultivation license and have separated curing and storage rooms for each premises.

An operator has multiple Type 2A cultivation and Type 7 manufacturing licenses throughout the state. The operator also obtains a single distribution license to be able to transport their products. The distribution license is tied to a manufacturing facility in Los Angeles, but the operator is also conducting full-scale distribution services out of a cultivation facility in Sacramento.

- Nothing in MAUCRSA would prevent a Type 2A cultivator and/or Type 7 manufacturer from obtaining a distribution license. This contemplates an independent distribution license.

- A distribution licenses is necessary to transport cannabis and cannabis products. A distribution licenses also authorizes the license holder to collect cannabis taxes, conduct quality assurance checks, and store, package, and label cannabis and cannabis products. A distribution licensee may not use independent contractors but instead must use employees of the licensee.
- The distribution license would have to be tied to a single premises. In the above scenario, the operator may transport goods to his/her other licensed premises, and even the licensed premises of other operators. However, since the distribution license is tied to a facility in LA, the operator may not conduct full scale distribution activities from his/her Sacramento facility – the Sacramento products would either (i) need to be transported via the distribution license to the LA distribution facility, (ii) transported by employees (not contractors) of the LA distribution facility (or a third part distributor) to the dispensaries that will sell the products or (iii) the operator would need to obtain a distribution license for the Sacramento facility to run full-scale distribution directly out of that premises.

An operator runs a retail business on the same premises as a cultivation facility.

- Provided the operator has both a retail and cultivation license and the appropriate local authorization, MAUCRSA does not prevent this. While specific rules have not yet been prescribed, areas where different commercial cannabis activities are occurring will likely need to be separated, most likely by a physical barrier or wall with separated security systems, into distinct designated areas.
    - For example, the CDFA proposed regulations would require that all cultivation canopy be "separated by an identifiable boundary such as an interior wall or by at least 10 feet of open space."
- To the extent the operator wishes to operate as a microbusiness (less than 10,000 sq. ft. cultivation, distribution and retailing) this would be a Class 12 license.

Several licensed operators owned by distinct entities share hallway and storage space.

- Under MAUCRSA, multiple companies could not share a single premises. Premises must also be contiguous and belong to a single licensee, so shared storage space or hallways may conflict with the requirements of MAUCRSA.
- A storage space that is separated from a licensed premises and shared by multiple licensees would likely not be allowed. The space would not be contiguous and would not belong to single licensee.
- It is likely that a bathroom or employee lounge or other space in a shared complex would be allowed if it was separate from the handling of cannabis operations (i.e. no cannabis or cannabis products ever entered this space).

Can distribution, cultivation and manufacturing operations be placed in one facility? If yes, can product be moved between them normally and then distribute from the distribution license?

- Other than Type 5 large scale cultivation and Type 8 testing licensees, there are no restrictions on obtaining a distribution license.
    - A distribution license would allow for self-distribution and distribution for other licensees.

  - The premises would need to meet all the requirements for a distribution license as well as any other categories the operator is licensed in.
- With respect to moving product for vertically integrated licensees, all rules for moving product between the distribution chain still apply.
  - All the different stages of commercial activity need to be recorded in the state track and trace system, including, but not limited to, cultivation, harvest, processing, distribution, inventory, and sale.
- **Only those with distributor licenses may transport cannabis and cannabis products on public roads.** If a licensee is cultivating and manufacturing in the same building a distributor license will likely not be required to move raw flower from a cultivation area to a manufacturing area. What would be considered "transport" will likely require the use of a public road. This issue will be clarified further in the emergency regulations.
- Taxes would also need to be collected in accordance with MAUCRSA.

Will the definition of canopy include vegetative growth and drying/curing space?

- "Canopy" is not defined in MAUCRSA. The term will be defined in regulations.
- Under proposed regulations canopy only included designated areas for mature plant growth. The proposed definition also included the following:
  - Canopy shall be calculated in square feet and measured using clearly identifiable boundaries of all area(s) that will contain mature plants at any point in time, including all of the space(s) within the boundaries;
  - Canopy may be noncontiguous but each unique area included in the total canopy calculation shall be separated by an identifiable boundary such as an interior wall or by at least 10 feet of open space; and
  - If mature plants are being cultivated using a shelving system, the surface area of each level shall be included in the total canopy calculation.

How should square footage limitations for cultivation licenses be interpreted?

- Exactly how square footage limitations must be interpreted will depend on regulations.
- The square footage limitations applied to the various cultivation licenses apply to square footage of total canopy size on premises, not the aggregate square footage of the premises.
- MAUCRSA provides for 14 cultivation licenses as well as a Microbusiness license which allows for cultivation, manufacturing, retail sale, and distribution. An explanation of each license type is provided below:
- **Type 1 "Specialty" Licenses:**
  - **Type 1-specialty outdoor:** for outdoor cultivation using no artificial lighting of less than or equal to 5,000 square feet of total canopy size on one premises, or up to 50 mature plants on noncontiguous plots.
  - **Type 1A-specialty indoor:** for indoor cultivation using exclusively artificial lighting of between 501 and 5,000 square feet of total canopy size on one premises.
  - **Type 1B-specialty mixed-light:** for cultivation using a combination of natural and supplemental artificial lighting at a maximum threshold to be determined by the CDFA, of between 2,501 and 5,000 square feet of total canopy size on one premises.

- **Type 1C-specialty cottage:** for cultivation using a combination of natural and supplemental artificial lighting at a maximum threshold to be determined by the CDFA, of 2,500 square feet or less of total canopy size for mixed-light cultivation, up to 25 mature plants for outdoor cultivation, or 500 square feet or less of total canopy size for indoor cultivation, on one premises.
- **Additional rules for Type 1 Licenses:**
  - Only cultivators who hold a Type 1 or Type 2 license may become members of a cannabis cooperative.

- **Type 2 "Small" Licenses:**
  - **Type 2-small outdoor:** for outdoor cultivation using no artificial lighting between 5,001 and 10,000 square feet, inclusive, of total canopy size on one premises.
  - **Type 2A-small indoor:** for indoor cultivation using exclusively artificial lighting between 5,001 and 10,000 square feet, inclusive, of total canopy size on one premises.
  - **Type 2B-small mixed-light:** for cultivation using a combination of natural and supplemental artificial lighting at a maximum threshold to be determined by the licensing authority, between 5,001 and 10,000 square feet, inclusive, of total canopy size on one premises.
  - **Additional rules for Type 2 Licenses:**
    - Only cultivators who hold a Type 1 or Type 2 license may become members of a cannabis cooperative.
- **Type 3 "Medium" Licenses:**
  - **Type 3-outdoor:** for outdoor cultivation using no artificial lighting from 10,001 square feet to one acre, inclusive, of total canopy size on one premises.
  - **Type 3A-indoor:** for indoor cultivation using exclusively artificial lighting between 10,001 and 22,000 square feet, inclusive, of total canopy size on one premises. The
  - **Type 3B-mixed-light:** for cultivation using a combination of natural and supplemental artificial lighting at a maximum threshold to be determined by the licensing authority, between 10,001 and 22,000 square feet, inclusive, of total canopy size on one premises.
  - **Additional rules for Type 3 licenses:**
    - The Department of Food and Agriculture is required to limit the number of licenses allowed of this type.
- **Type 4-nursery:** for cultivation of cannabis solely as a nursery.
  - A Type 4 license may only produce clones, immature plants, seeds, and other agricultural products used specifically for the propagation and cultivation of cannabis.
- **Type 5 "Large" Licenses:**
  - **Type 5-outdoor:** for outdoor cultivation using no artificial lighting greater than one acre, inclusive, of total canopy size on one premises.
  - **Type 5A-indoor:** for indoor cultivation using exclusively artificial lighting greater than 22,000 square feet, inclusive, of total canopy size on one premises.
  - **Type 5B-mixed-light:** for cultivation using a combination of natural and supplemental artificial lighting at a maximum threshold to be determined by the licensing authority, greater than 22,000 square feet, inclusive, of total canopy size on one premises.
  - **Additional rules for Type 5 licenses:**
    - Type 5 licenses will not be issued before January 1, 2023.

    - Type 5 licensees may also hold Type 6 and Type 7 manufacturing licenses and Type 10 retailer licenses.
    - Type 5 licensees may not hold Type 8 testing laboratory, Type 11 distributor, or Type 12 microbusiness licenses.
- **Type 12 "Microbusiness" License:**
    - Microbusinesses may cultivate on an area less than 10,000 square feet and act as a licensed distributor, Level 1 (nonvolatile) manufacturer, and retailer (including delivery). Microbusiness licenses will be issued by the Bureau of Cannabis Control and applicant must demonstrate compliance with all the rules specified for the various commercial activities a microbusiness license authorizes.

Can an operator be licensed as a cultivator and retailer and have canopy space openly viewable to the public? Can harvested plants be sold in the cultivation/retail establishment like a winery?

- Cultivation and retail sales will be allowed on the same premises and the cannabis grown by the dually licensed operator may be sold to consumers and patients. However, to what degree these operations will need to be separated from each other on premises depends ultimately on regulations and local ordinances. While it is possible that the grow space could be viewable, at best it would only be through a secure glass partition where people on the premises of the dispensary could see into the premises of the cultivator. Most likely, "walk-throughs" or tours would not be allowed.
- While regulations are still being drafted, proposed regulations require a physical or spatial barrier that separates canopy space. In conversations with stakeholders, licensing agencies have indicated that each activity should generally occur in a designated area separated by a barrier. To what extent and how activities need to be separated from each other is unclear, but err on the side of caution and be prepared to have physical barriers between each licensed activity.
- State law requires retail operators to establish "limited access areas" that only authorized personnel can access which, in cases where the retailer is also licensed as a cultivator, will likely include cultivation canopy. Other than items for immediate sale, display, or samples cannabis and cannabis products also need to be stored in a secure and locked location.
- Many local governments prohibit canopy space from being viewable from outside of the premises or by unauthorized personnel. This may be an issue if there are clear sightlines into dually licensed retail and cultivation establishment.
- It should also be noted that free samples are prohibited, so winery style free tasting or samplings would not be allowed. Specifically, Business and Professions Code Section 26153 states "a licensee shall not give away any amount of cannabis or cannabis products, or any cannabis accessories, as part of a business promotion or other commercial activity."

Important Definitions and Provisions

Proposed Medical Cannabis Cultivation Regulations. Section 8000 (d): "Canopy" means all of the following:

(1) The designated area(s) at a licensed premises that will contain mature plants at any point in time;

(2) Canopy shall be calculated in square feet and measured using clearly identifiable boundaries of all area(s) that will contain mature plants at any point in time, including all of the space(s) within the boundaries;

(3) Canopy may be noncontiguous but each unique area included in the total canopy calculation shall be separated by an identifiable boundary such as an interior wall or by at least 10 feet of open space; and

(4) If mature plants are being cultivated using a shelving system, the surface area of each level shall be included in the total canopy calculation.

Note: This definition "canopy" is from medical cannabis regulations proposed by the CDFA. This is only a draft proposed definition of canopy. The definition may ultimately change when regulations are finalized.

Business and Professions Code (BPC) Section 26001 (y): "License" means a state license issued under this division, and includes both an A-license and an M-license, as well as a testing laboratory license.

BPC Section 26001 (z): "Licensee" means any person holding a license under this division, regardless of whether the license held is an A-license or an M-license, and includes the holder of a testing laboratory license.

BPC Section 26001 (ap): "Premises" means the designated structure or structures and land specified in the application that is owned, leased, or otherwise held under the control of the applicant or licensee where the commercial cannabis activity will be or is conducted. The premises shall be a contiguous area and shall only be occupied by one licensee.

BPC Section 26053: (a) All commercial cannabis activity shall be conducted between licensees, except as otherwise provided in this division.

(b) A person that holds a state testing laboratory license under this division is prohibited from licensure for any other activity, except testing, as authorized under this division. A person that holds a state testing laboratory license shall not employ an individual who is also employed by any other licensee that does not hold a state testing laboratory license.

(c) Except as provided in subdivision (b), a person may apply for and be issued more than one license under this division.

(d) Each applicant or licensee shall apply for, and if approved, shall obtain, a separate license for each location where it engages in commercial cannabis activity.

BPC Section 26055 (c): A licensee shall not change or alter the premises in a manner which materially or substantially alters the premises, the usage of the premises, or the mode or character of business operation conducted from the premises, from the plan contained in the diagram on file with the application, unless and until written approval by the licensing authority has been obtained. For purposes of this section, material or substantial physical changes of the premises, or in the usage of the premises, shall include, but not be limited to, a substantial increase or decrease in the total area of the licensed premises previously diagrammed, or any other physical modification resulting in substantial change in the mode or character of business operation.