

# Cannabis and the Municipal Challenge: The Secrets to Successful Permitting

A ROUNDTABLE DISCUSSION

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*Sponsor Smith, Costello & Crawford represents technology, laboratory, dispensary, real estate, municipal and investment clients in both the medical and adult use cannabis industries, and offers a comprehensive array of services from regulatory and legislative advocacy to business consulting and legal services.*

## TOPIC 1: ZONING ISSUES

**SIRA GRANT, SMITH, COSTELLO & CRAWFORD:** I joined Smith, Costello & Crawford in November 2017, and it was about the same time that the draft adult use regulations were being released. Since the rollout of adult-use marijuana, we have worked with a number of different cities and towns with varying views on marijuana establishments. We have worked through the varying local processes with different clients and have learned a lot about Massachusetts over the past two years. We have 351 cities and

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— Sira Grant, Smith, Costello & Crawford

towns in Massachusetts, and we have 351 sets of zoning bylaws.

What we found is that the processes on the local level started taking multiple shapes and forms. The state [cannabis] application requires a certification page signed by both the operator and the city or town that says, “Yes, we’ve entered into a Host Community Agreement.” Some cities want you to get a special permit before they give you a Host Community Agreement. Some say, “No, we’ll give you a Host Community Agreement, and then we’ll worry about the special permit later.” Some have implemented a request for qualifications or proposals process, which is very similar to something you’d see in real estate as a management company.

Let’s say that a city or town wants to see a draft adult use application for an operator as part of that request for qualifications. I create a CIP login, I have to fill in information, I have to print each page individually. And maybe I don’t know the answers to questions like, “What is my plan to remain compliant with local zoning?” The process can take a long time. And then once you submit it, maybe there will be two selections out of 30 applications.

Also, finding property can be very difficult. At the very beginning, clients would come to us and they’d say, “Here’s an address I found of a commercial property for sale. Can you tell me if it’s zoned properly?” I have to take a look at their buffer zone. The statutory buffer zone is 500 feet from a preexisting K through 12 public or private school. That’s for adult use marijuana establishments. But for medical establishments, it’s a preexisting K through 12 public or private school and licensed daycares.

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That is still how the regulations are set up. When the regulations potentially change in the coming months, hopefully those get aligned so I’m not looking at two different buffer zones for an operator that wants a medical use, and an operator that wants an adult use.

[In addition,] some cities and towns may [require cannabis businesses] to be 500 feet from a funeral parlor, 500 feet from a playground, 500 feet from a baseball field or a recreational area. Cities and towns have passed this and that’s part of their zoning. It goes beyond what the state law says that you can do. But that’s just how it goes right now.

This hasn’t been litigated yet. So, let’s say that this property is 500 feet from a baseball field, and [the zoning provision] says “recreational areas.” Now I have to call the city or town and say, “Hey, is a baseball field a recreational area?” Or, “Is a dentist office that treats children a place where children commonly congregate?” “Is a karate studio?” These are the questions that we have to answer as we go through the buffer zone analysis.

## TOPIC 2: THE OPERATOR’S PERSPECTIVE

**CHRIS MITCHEM, DIEM CANNABIS:** Good counsel has been a godsend for us. We’re honestly fortunate that we found Smith, Costello & Crawford. Good counsel is incredibly important given this regulatory climate.

I’m going to talk a little bit about the process of getting an HCA, a Host Community Agreement. We operate out of Oregon. Massachusetts is an entirely different regulatory structure. It’s all new. I actually love what the state of Massachusetts did. They gave all the power to the municipalities to decide who gets to operate within their town or city. And I think that’s really smart. The local folks should be deciding which businesses they are going to host.

But it’s complicated [because] each municipality has set up unique rules. We’ve been working in four different municipalities in the state. There’s a different recipe for each one. And you go into each city with a smile on your face, understanding that it’s a startup for regulators along with us as operators.

You go into a town. Hopefully you find one that passed Question 4 in 2016. You do your research, target a few communities. [We said,] “We want to go to Worcester, we want to go to Springfield, we want to go to Lynn, we want to go to Orange.” Once we identify the communities that don’t have a ban, we go in and kind of feel out the planning department. We see if





they're open to it. There's a lot of passion both for and against cannabis, so we want to make sure that they're on board and they're not just saying that they're on board.

Then we get into the community. Securing real estate is incredibly hard. The hardest part about this business is finding real estate. Each municipality has its own regulatory structure that starts with zoning. Some communities break it down to specific streets that you can operate on. From an operator's perspective, usually the zoning's pretty restrictive. We have to go to a specific part of the town. And the landlords in that zone know that they have something really special there. So when you're negotiating a contract, that becomes a huge factor.

It's the worst one-sided negotiation process, because they're charging double, triple, quadruple market rates for rent. They don't want to sell you the building, even though you're going to have to invest hundreds of thousands of dollars to retrofit it. It [is really challenging] from an operator's perspective.

Our strategy has been we try to secure multiple properties and throw multiple options at a city, which we did in Worcester and it turned out to be a successful strategy for us there. We were able to give Worcester the

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luxury of choice for us as operators, and we were lucky enough to get an HCA there.

The process is typically long. I think you can expect at least six months before you get an HCA, sometimes up to a year. As an operator, I have overhead. I have investors that I'm reporting to, I have budgets, I have a P & L. If I'm paying heavy rent on a piece of property for a year, before I even get the HCA, and once I get the HCA then I apply at the state level and that takes another year. We're talking about securing a property for two years without generating any revenue from it.

**JAMES SMITH, SMITH, COSTELLO & CRAWFORD:** Everybody in the communities that we deal with, and I think most folks in the public, think this is a goldmine, that nobody can possibly lose money in the cannabis industry. But I tell every client, "You want to be in this industry? Take your money, go to Vegas, put it on red. [You'll get] far better odds."

We tell clients, "You walk in the door, you won't see a nickel for 18 months." This is a hard industry. You've got a lot of people with passion who want to get into this industry. But there are no banks, there are no loans, there are no breaks. The rents are higher. Nothing is market [rate] in this industry, because everybody is convinced you're on your way to millions.

Some folks are going to make some serious money. But [you have to have] the capital, the ability to put millions of dollars on the table without a bank and let it sit out there for as long as 24 months.



### TOPIC 3: NEGOTIATING HOST COMMUNITY AGREEMENTS

**SMITH:** Host Community Agreements have become incredibly controversial. Ultimately, [what the words in the statute mean is going to] have to be adjudicated. We spend a lot of time negotiating [HCAs] — an inordinate amount of time. And you should have a question in your mind: Why would anybody in their right mind sign one of these things?

There are some key words in this statute. It says [that a HCA] "may" include a community impact fee. It's not "shall," it's "may." The Legislature thought, "There may be some costs here." [The statute says that fee should be] "reasonably related to the cost imposed upon a municipality."

There is a local tax of 3% that's in the statute. There's a total tax of 20%. The state gets 17%, the host community gets 3%. [But now, there's an addi-

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tional fee] up to 3%, and naturally, every community is at 3%, the maximum regardless of costs.

As this industry normalizes, an average store might do \$5 million [in revenue]. If you do less than \$5 million, you're probably not going to make it. You might do \$10 million in a good store. Today, because there are only 23 or 24 stores open across the commonwealth, they're doing much more than \$5 or \$10 million. But as this normalizes, \$10 million will be a pretty good store, \$5 million a barely OK store, \$15 to 20 million a phenomenal store. [If] you've got a \$20 million store, you're paying \$1.2 million in taxes and fees to the communities over and above the property taxes. And we have to fight our way into these communities.

Beyond the 3% tax, communities ask for charitable donations. And "ask" is really a misused verb. They'll want \$20,000-25,000. They might want more. They want a hundred man hours or person hours, annually, [for] volunteer [work]. You've got to use local vendors. You've got to hire local employees. Imagine anybody telling Dunkin' Donuts, Wal-Mart, or even maybe a bicycle repair shop, any of these things. This is language that should not be in these agreements. The statute says nothing about any of this, yet it's in most of the agreements.

[One provision] that you absolutely cannot sign is when [towns] have local health departments and want the ability to come in and say, "Well, that product is dangerous. You can't sell that." You can't have that. Nobody can walk into Dunkin' Donuts and say, "Don't sell the coconut doughnuts. I don't like coconut; it's dangerous." Yet this language is in agreements where local health departments can walk in.

The Cannabis Control Commission is extraordinarily aggressive when it comes to regulations. They show up unannounced, they bring in six, eight, nine people; they inspect all the time. They've approved every single product many times over. [You can't] allow a health department with no background, no experience, and potentially someone who is not a cannabis advocate, saying, "Those are dangerous, those edibles. We can't have those sold in our town." That can essentially shut your business down. These products are very expensive. You just can't simply not sell them.

So why sign one of these things? We have no leverage. These are not equal negotiations. Your client comes to you and says, "Well, Jim, I've had this property now for about a year. It's costing me \$10,000 a month. I'm





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paying you. I've got a whole team. I've got an architect. I've got an engineer. I've surveyed. I've spent all that money. I'm now finally through the city process. I probably hired local counsel to get through the zoning process locally, and now [this is] the final step before I can go to the CCC. You're telling me it's not legal. It doesn't meet the statutory requirements, but I have [no choice but to] sign it."

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Another issue is that once the city or town says, "Hey, the guy down the street signed this and you have to sign the same thing," it's really hard to argue with that. Everybody thinks there is a goldmine here, [and] they'll sign anything. Then your client walks in with good counsel, and you say, "There are eight or 10 violations of the statute here. I can't have this signed." [And the municipality says,] "We don't need your client. We'll get somebody else." It's really hard to negotiate with that.

#### TOPIC 4: PUBLIC POLICY ISSUES

**SMITH:** There are three basic cannabis licenses. There's cultivation. You've got to grow this product, and that's frankly where there's some serious profit margin. There's manufacturing. You process it, you turn into something. Cultivation and manufacturing ... are typically zoned in the industrial area of town -- it's an industrial or light manufacturing facility. [But even though] there's no retail operation there, there's no traffic, [communities] want 3% of your sales.

I don't think anybody [on the legislative side] really intended the industrial side of this business, the cultivating and the manufacturing, to also have a Host Community Agreement for 3%. The real goal from a public policy

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perspective is to defeat the illicit market. Estimates tell us that 85% of all cannabis sold in Massachusetts is sold illicitly. You have no idea what's in that product. You have no idea where it came from. You don't know if the kid down the street grew it or it came out of a foreign country and who knows what's inside that product. But 85% of all cannabis consumed today in this state is that product.

We're the other 15%. Our product is tested. You know what's in it. It's a safe product. The goal here is really to defeat the illicit market. But if [for example] we add to the 20% state tax the 3% local Host Community fees in three communities, now you're at 9% on top of 20%. Our product is so much more expensive than what the street corner is selling it for that we can't compete. Our product is safer, but it's more expensive.

So if the public policy goal here is to eliminate the illicit market or at least do harm to it, Host Community Agreements are really a critical component in my mind.

#### TOPIC 5: SOCIAL EQUITY IN THE CANNABIS INDUSTRY

**GRANT:** We have worked with some economic empowerment applicants on a pro bono level. We have negotiated some Host Community Agreements for them. But we've been approached by a few that we don't want to take their money because there's no path.

**SMITH:** It goes back to this is not an inexpensive industry. There are no banks; there are no lending resources. People come in with a couple hundred thousand dollars — which is a lot of money — and say, "I want to get in the cannabis business." Well, you can't. You're at about a million dollars to open a simple retail store, which is the least profitable segment of the market. So the folks on the poorer side of the equation can't open one retail store. Without capital, you really can't have social equity. It's tragic.

**MITCHEM:** I just want to make a quick comment from an operator's perspective to that. This is an issue we're passionate about. We chose cannabis, in part, because of the social mission. We know that last year 600,000 people got put in jail for carrying small amounts of marijuana, and each one of those people cost us as taxpayers \$50,000 a year. Most of them were black or Latino men. They get out of jail, they have a felony on their record, they can't get an apartment, they can't get a job. It's a nightmare, and that's a big reason why we do this.

