



BOARD OF SUPERVISORS
AGENDA LETTER

Agenda Number: 2020-09-22

Clerk of the Board of Supervisors
105 E. Anapamu Street, Suite 407
Santa Barbara, CA 93101
(805) 568-2240

Department Name: County Executive Office
Department No.: 012
For Agenda Of: September 22, 2020
Placement: Administrative
Estimated Time: N/A
Continued Item: No
If Yes, date from:
Vote Required: Majority

TO: Board of Supervisors
FROM: Department Director (s) Contact Info
Mona Miyasato, County Executive Officer
Harry Hagen, Treasurer-Tax Collector, Public Administrator, Public Guardian
Bernard Melekian, Assistant County Executive Officer
SUBJECT: Agreement for Cannabis Tax Compliance Services from Hinderliter, de Llamas & Associates

Digitally signed by Mona Miyasato
DN: cn=Mona Miyasato, o=County of Santa Barbara, ou=County Executive Office,
email=mmiyasato@countyofsb.org, c=US
Date: 2020.09.11 13:43:16 -0700
Mona Miyasato
H. Hagen
B. Melekian

County Counsel Concurrence

As to form: Yes

Auditor-Controller Concurrence

As to form: Yes

Risk Management Concurrence

As to form: Yes

Recommended Actions: That the Board of Supervisors:

- a) Approve and authorize the Chair of the Board of Supervisors to execute the Agreement for Services of Independent Contractor with Hinderliter, de Llamas & Associates (HdL) to deliver Cannabis Tax Compliance Services, for the period of 9/22/2020 through 6/30/2023, in an amount not to exceed \$300,000 (Attachment A); and
- b) Determine that the above actions are organizational or administrative activities and fiscal activities that will not result in direct or indirect physical changes in the environment and are not a project under the California Environmental Quality Act (CEQA) pursuant to Section 15378(b)(4) and (5) of the CEQA Guidelines.

Summary Text:

The County Executive Office recommends entering into a Board contract with HdL for quarterly cannabis tax analysis and monitoring of cannabis businesses operating under the County’s regulatory program. This will shift the burden of analysis and monitoring from in-house staff with limited resources, to a firm that specializes in maximizing local government revenues by providing audit,

compliance, economic development, consulting service, and software products, as well as the establishment and implementation of cannabis regulatory programs that includes conducting compliance and financial audits. The contract amount of \$300,000 is based on \$100,000 per fiscal year for a term of three years to support the tax compliance audit services performed.

Background:

The County Executive Office uses cannabis tax revenue data for reporting and analyzes this data for budgeting and long term revenue planning. Pursuant to the County's Cannabis Tax Ordinance, County Code Chapter 50A, every person who engages in cannabis operations, including the cultivating, manufacturing, producing, processing, preparing, storing, providing, donating, selling, or distributing cannabis or cannabis products within the unincorporated area of the County is required to pay to the County Treasurer-Tax Collector a tax on the gross receipts of each of their operation's activities, based on the established tiered cannabis tax rate structure.

Furthermore, every person required to pay the cannabis operations tax is required to file with the Treasurer-Tax Collector a quarterly report that provides the number of units of cannabis or cannabis products sold or transferred, the total gross receipts of the cannabis operation, and the computation of the amount of the gross receipts tax for each such operation due the County. At the time of filing the report, the cannabis operation is required to pay to the Treasurer-Tax Collector any gross receipts tax which may be shown due.

Under the Ordinance, cannabis operators are permitted to self-report their gross receipts and associated taxes due. Consequently, it is critical to monitor and verify that tax reporting and the corresponding tax payments submitted are accurate with respect to the type of licensed cannabis activities conducted. To that end, the service objectives to be accomplished by HdL as part of this contract are twofold: 1) generation of Tax Analytical Remittance Reports (TARR) consisting of quarterly financial reviews with an annual preliminary onsite assessment for a sample set of 20 businesses, and 2) complete cannabis business tax audits for six cannabis businesses that include a full annual financial audit to verify the accuracy of revenues reported to the County.

HdL has developed a quarterly revenue-monitoring system that provides a risk-based assessment of each cannabis business to identify outliers or possible errors that may warrant further investigation. Their proprietary TARR uses specially designed algorithms to analyze confidential data from each cannabis business that will enable HdL to make recommendations to the County to address tax liability deficiencies or other financial compliance issues.

As part of HdL's business tax audits, one annual financial audit of each subject cannabis business will be conducted to verify the accuracy of the revenue reported to the County during the review period and will recommend a tax assessment should the audit reveal any unreported revenue. As part of this process, HdL will conduct a risk based analytical review of the business using the proprietary Cannabis Analytical Tracking Solution (CATS™) program to ensure there is no diversion of product or cash. Their unique audit approach identifies whether a cannabis operator is under-reporting its taxes or diverting product from its facility.

The outside resource, HdL, is a necessary component of an overall tax compliance program for a cannabis operations tax based on gross receipts. The tax compliance function decreases the risk that taxpayers will underreport taxes owed and will help ensure that taxes owed the County are reported. It is the primary mechanism for detecting and deterring noncompliance with the tax ordinance, which may

involve more in-depth review of the business’s financial records and other powers defined by code. The County Executive Office will work with the Treasurer-Tax Collector to provide the required resources to better serve the public and satisfy the goal of tax compliance.

Fiscal Analysis:

<u>Funding Sources</u>	<u>Current FY Cost*:</u>	<u>Annualized On-going Cost:</u>	<u>Total One-Time Project Cost</u>
Cannabis Tax Revenue	\$ 100,000.00		
General Fund			
State			
Federal			
Fees			
Total	\$ 100,000.00	\$ -	\$ -

* Annual fiscal year costs in the amount of \$100,000 will be appropriated for cannabis tax compliance services resulting in a total board contract amount not to exceed \$300,000 through 6/30/23.

Narrative:

Funding for Cannabis Tax Compliance Services is included in the FY 2020-21 Adopted Budget.

Key Contract Risks:

The contract risk assessment determined the contract to be of medium risk because of the complexity of the work involved as well as the visibility and sensitivity of the County’s cannabis programs. HdL has successfully performed other consulting services for the County for many years. Furthermore, HdL’s consultant staff has proven experience in the field of cannabis regulatory programs.

Staffing Impacts:

The services provided by HdL in this contract provide the necessary industry knowledge and expertise to help sufficiently guide the efforts of the tax compliance team. Additional staff are required to sufficiently meet the needs of a cannabis operations tax compliance program. One additional FTE is needed to lead the tax compliance function this fiscal year, and additional resources will be evaluated during the development of next year’s budget.

Attachments:

A – Cannabis Tax Compliance Services Contract

Authored by:

Bernard Melekian, Assistant County Executive Officer