

Cannabis Legal Update Series – Municipal Oversight of Private Retail

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With a final Senate vote on Bill C-45 scheduled for June 7, 2018, municipalities, landlords and retailers are working feverishly to prepare for retail sales upon commencement of legalization of cannabis for adult-use non-medical purposes, particularly in provinces that will permit private retailer sales.

The separation of federal, provincial and municipal authorities within this entirely new regulatory framework can be a cause of some confusion for both market participants and governments.

Municipalities face crucial decisions that will have profound effects on the local competitive landscape. Key questions facing many municipalities include how closely cannabis retail stores may be located to each other, and how to choose between competing applicants for a retail business permit/license, especially at the outset. This article will examine municipalities' role in the new regulatory framework, and available policy options.

Some municipalities are considering a random lottery process and others a first-come/first-served race.

When designing processes for deciding who can operate a private retail business and where, municipalities would be well-advised to heed the AGLC's warnings to gamblers: "Know Your Limits. Play Within Them." If an unbridled lottery process is adopted, investors and speculators should be similarly warned.

1. Municipalities' Role re Cannabis Legalization

Municipalities serve an important and powerful role in determining where and how products may be produced, sold and consumed within communities. As with any consumer product, the "last mile" of the distribution chain will form a key aspect of the product-consumer relationship.

Municipalities' oversight of land use and zoning by-laws serves an important barrier to entry for federally licensed production businesses and provincially licensed retail businesses.

Municipalities also have a function in respect of regulating signage, which directly impacts businesses' ability to advertise and *Charter* rights to freedom of expression.

Municipalities will also serve important roles in the monitoring and enforcement of compliance with both existing and new by-laws. Strict zoning restrictions on separation from other cannabis

businesses and sensitive uses will be meaningless if a black market is allowed to continue operating with impunity.

For a detailed review of legal considerations facing municipalities, see the [Federation of Canadian Municipalities' Municipal Guide to Cannabis Legalization](#).

2. Zoning and Land-use Regulation

Municipalities are likely most familiar with their roles as regulator of the location, development and business licensing of cannabis businesses within their local communities – this is a function they routinely perform for all other businesses.

In the absence of express restrictions on cannabis businesses within certain areas, cannabis businesses could potentially have a legal right to operate in certain areas without discretion or approval of local government. This is the case where existing zones authorize permitted uses that would, on a plain reading, include cannabis businesses following implementation of federal Bill C-45 and provincial Bill 26, such as horticultural, agricultural, commercial greenhouse uses for commercial cannabis production facilities or general, commercial or convenience retail uses for cannabis retail stores.

As a result, many municipalities began the process of amending their zoning and land-use by-laws in 2013 to permit or prohibit legal commercial cannabis production activities in connection with the introduction of the *Access to Cannabis for Medical Purposes Regulations*.

Further work is now required to amend land-use and zoning bylaws in light of the pending legalization of private retail sales, as well as the federal government's proposal to introduce new regulations allowing commercial micro-cultivation, micro-processing and nursery facilities.

Fair and effective regulation will require a careful balancing of many considerations, including:

- Whether to dictate a cap or quota on the number of licenses to issue within a municipality.
- Whether to encourage concentrated cannabis districts within a municipality.
- Whether to conduct any subjective review of the fitness or good character of applicants.
- How to prevent the illicit market from dominating or manipulating the licensing process.
- How to protect youth, including their access to cannabis businesses and cannabis consumption.

Specific legal issues that municipalities are considering include:

- Whether to require a minimum separation distance between cannabis retail stores.
 - While not mandated by the province or AGLC, the creation of minimum separation distances would be consistent with the treatment of liquor sales. In general,

separation distances between stores are intended to avoid excess concentration of a particular business type in any one area to ensure an appropriately diverse mix of uses. In practice, separation distances are the greatest potential distortion of market forces as they effectively grant recipients a government-backed exclusive territory.

- How far must cannabis retail stores be separated from other sensitive uses, such as schools, parks, and what constitutes a sensitive use?
- The AGLC Retail Cannabis Store Handbook mandates a minimum separation distance of 100 metres from a provincial health care facility, school, or school reserve or municipal and school reserve.[\[1\]](#)
- Municipalities may extend those distances, or add further restrictions from other sensitive uses – e.g. separation from liquor stores, bars or cannabis lounges (once legalized)?
- Municipalities must also define what areas fit within the AGLC’s restrictions – for example, what is a “park”?
- Should cannabis stores be separated from liquor stores/bars?
- How will separation distances be calculated (i.e. site-to-site, use-to-use, or site-to-use)?
 - These legal distinctions can have a profound impact on where a store may be located and the scope of exclusivity granted by an initial licence.
 - For example, does a store located in a shopping centre preclude any other store from opening in that centre or in adjacent parcel?
- Should commercial micro-cultivation, micro-processing and/or nursery facilities be permitted outside of industrial zones?
- How to determine who receives a license in cases of conflict between applicants at the initial stage of licensing?
 - Whether discretion should be exerted to expressly “pick winners”.
 - If discretion is not to be exerted, how to design a fair, efficient and transparent process to select between competing applicants.

Each municipality will be making these decisions within the context of their own local community’s needs. In doing so, municipalities should be careful to consider both the intended and unintended effects that may result from their policy decisions.

Failure to do so could empower a black market and frustrate the goals of legalization at great administrative and financial expense to municipalities.

3. AGLC Application Process

Amendments to the *Gaming and Liquor Regulation* were declared by Order in Council on February 16, 2018. On February 22, 2018, the Alberta Gaming and Liquor Commission (now responsible for administering distribution and retailing of cannabis for non-medical purposes in Alberta) held a province-wide town hall to discuss details and answer questions regarding the AGLC licensing processes. Applications for an AGLC license to operate a non-medical cannabis retail business opened on March 6, 2018, and are being accepted and reviewed on an ongoing basis. The AGLC

has continued its province-wide outreach to ensure public awareness of its process.

The [AGLC application](#) requires detailed information regarding the applicant (including its directors, officers, shareholders, manager and associated businesses), the proposed location (including site and floor plans), undertakings regarding supply of legal cannabis, and application fees of \$4,100 (consisting of a .

The AGLC application process may be commenced in reliance upon an unsigned or conditional offer to lease; however, approval will not be issued until an applicant has delivered a signed, unconditional offer to lease or lease, or certificate of title in the name of the applicant.

All completed applications are posted publicly on the AGLC's website for a 21-day period in which impacted businesses or citizens may register their objection.

The AGLC conducts extensive due diligence investigations of all applicants, including a detailed review of any past criminal conduct. While non-violent drug possession charges do not automatically disqualify an applicant, the AGLC reviews each application on a case-by-case basis to determine fitness and good character and maintain the integrity of the legal cannabis regime.

Following such review, the AGLC has issued Phase 1 conditional approvals to many entrepreneurs that have satisfied the AGLC's requirements, subject to receipt of required municipal approvals.

Media reports have indicated up to ~450 applicants have been submitted to the AGLC. Of those, slightly more than 300 have been posted for public notification; however, that likely includes duplicate notifications where an applicant's name or location has changed requiring re-notification. It is not known precisely how many of those applicants have received Phase 1 Approval, though it is safe to assume that at least some of those applications have been rejected in light of the AGLC's appropriately rigorous standard for review.

The AGLC approval process is expected to take two – four months, subject to compliance with the AGLC's [review policies](#). This is a commendable target in light of the detailed, fact-specific review exercise that must be engaged to properly weed out ineligible applicants.

4. Picking Winners

Conflict Areas - Overview

The allocation and timing of issuance of initial cannabis retail developments and businesses licenses is perhaps the most commercially sensitive decision to be made by municipalities.

A review of the AGLC's published notifications of applicants shows several areas where applications have been submitted in close proximity that will likely require municipalities to decide

which applicant receives the initial permit (and therefore exclusivity within the mandatory set-back areas).

Based on the AGLC notification data, such conflict areas are the exception, not the norm. The relatively small number of conflict areas is likely due to market forces at work in the course of lease negotiations for suitable, available commercial real estate. Nevertheless, the conflicts in these areas will need to be resolved fairly, with inevitable winners and losers as a result.

The design of a selection process among those applicants in conflict could unintentionally cause the number of applications to expand drastically. In our view, the means for resolving conflicts should not incentivize the creation of further conflicts. Care should be taken to design a fair, efficient and open process for resolving the few conflicts that exist.

Many entrepreneurs have already made significant investments in developing business plans, obtaining leases, and conducting engineering and construction due diligence in order to be ready to serve the private retail market as soon as possible after legalization. However, uncertainty over the issuance of a development permit or business license would likely cause most prudent entrepreneurs to halt further investment or development. Given the tight timelines involved to commence retail sales in August/September 2018, any such delay could be expected to result in a significant gap in the market once legalization occurs.

Designing a Selection Process

Broadly speaking, municipalities face of choice of whether to exert (1) discretion in choosing who receives a permit/licence in conflict areas, or (2) implement a non-discretionary rules-based system.

Consciously exercising discretion in issuing permits/licenses may be the most effective option for weeding out black market participants or other “bad actors”, but is otherwise rife with potential for abuse. At a minimum, legal challenges by rejected applicants would be expected to ensue.

Assuming municipalities will instead implement a non-discretionary rules-based system for resolving conflicts, they must each decide what rules will apply, communicate them openly to market participants, and apply them consistently.

Many commentators have split the options available to municipalities into two categories: (1) first-to-file; and (2) random lottery.

Oversimplification of either option could result in significant unintended consequences – many choices remain within either option.

In particular, municipalities should consider what entry criteria will be applied to either system, and

what rights will be granted to the initial winners in respect of renewal and transfer (and the municipality's ability to prohibit same).

Entry criteria that are purely financial in nature will incentivize speculative applications as a form of gambling on an opportunity to obtain a government-authorized right to exclude competitors within a prescribed area. At a minimum, such criteria would benefit any applicant willing and able to "play the numbers" by maximizing the number of applications made. It would also likely benefit more sophisticated or powerful market participants able to negotiate binding offers to lease with early termination provisions, or applicants with owned real estate. In any event, rent-seeking behaviour should be viewed as a negative consequence of introducing new highly regulated market which should be limited as much as possible, and not a legitimate government objective of itself.

Municipalities should also give due regard to the necessary interaction between their roles and those of the AGLC and Health Canada. Issuing provisional permits to applicants that will not meet the rigorous provincial review will, at best, result in increased administrative burden, confusion and uncertainty and, at worst, could provide the black market a way of extending their existing dominant position beyond legalization.

Municipalities should also be aware of the potential bias they face in favour of maximizing the number of applications (and corresponding fees) that are submitted, particularly since a disorderly application process would likely have significant harmful consequences (and be more costly to administer over the longer term).

Accordingly, we believe that **the entry criteria to any selection process should include a requirement to have obtained Phase 1 AGLC approval.**

While this may exclude some late applicants that might ultimately be successful in obtaining Phase 1 AGLC approval from participating in the initial permitting process, this is greatly preferable to the alternative where applicants who have been or will be rejected by the AGLC are granted an initial advantage in the municipal permitting process.

Whether a municipality chooses to submit properly pre-qualified applicants to a first-to-file or random lottery process, or any other review or subjective criteria, remains a topic for each municipality to determine in consultation with its stakeholders. The current state of the City of Edmonton's deliberations on Cannabis Retail Sales is addressed below.

Edmonton

On May 7, 2018, Edmonton City Council closed its public hearing and passed at second reading amendments to the City of Edmonton's Zoning Bylaw which would allow Cannabis Retail Sales as a permitted use within nine commercial zones, three mixed use zones and one industrial zone. Third and final reading is scheduled for June 12, 2018.

Cannabis Retail Sales will not be authorized in direct-control zones and special areas by the proposed Zoning Bylaw amendment. Applicant-driven bylaw amendments would be required to permit Cannabis Retail Sales in those zones/areas.

The Zoning Bylaw amendments will implement the provincially-mandated separation distances of 100 metres from provincial health care facilities, public parks and public recreation facilities, and to increase the minimum separation distance to 200 metres from schools and public libraries.

The Zoning Bylaw amendments will also introduce a minimum separation distance of 200 metres from another cannabis store. No separation distance from a liquor store use would be required.

The Zoning Bylaw amendments proposes to delegate authority to administer a selection process for applicants to the Development Officer. City Council would not directly be deciding how the process for selecting among competing applicants would be administered; however, Council should be aware of the proposed process and its likely effects when delegating such authority.

To operate in Edmonton, a Cannabis Retail Sales business will require a Development Permit, Building Permit and Business Licence in addition to an AGLC licence.

In a series of public consultations held at the end of April, 2018, the City of Edmonton, Development Services, announced their proposal to conduct an Expression of Interest / Random Selection Process for reviewing Development Permit Applications. Expressions of Interest would be submitted commencing "late May".

Inconsistent announcements have been made as to long the window will remain open for submission of Expressions of Interest, or when the Random Selection Process would occur. Further clarity and consistent messaging should be encouraged.

The City of Edmonton has indicated that the Random Selection Process would "determine the order in which applications will be accepted and first reviewed". The ordering of applications would mostly, but not conclusively, determine who receives a Development Permit in a conflict area – if a Development Permit is approved, subsequent applications within a 200 metre distance from such location would be refused. However, applications may be found incomplete and re-ordered if subsequently completed within 5 days, leaving some faint hope for applicants in conflict areas that do not initially "win" the lottery.

At a minimum, substantial uncertainty would ensue, and most entrepreneurs can be expected to halt any development activities until the Development Permit process is completed. This is particularly true if there is no pre-qualification of applicants, as that could result in a large number of applications being submitted at a late stage for gambling or anti-competitive purposes, with Development Permits initially issued to entities that will ultimately be refused an AGLC licence.

The City of Edmonton should be commended for their efforts in consulting with the public, developing clear and reasonable rules regarding zoning and separation distances, and bringing forward amendments on a timely basis. To complete this good work, the City of Edmonton should be encouraged to:

1. Set pre-qualification criteria for entry into the Random Selection Process that discourages speculative or anti-competitive behaviour, prevents criminal actors from manipulating the process, and aligns with the AGLC's background checks and due diligence review. In this regard, we recommend requiring AGLC Phase 1 approval as a condition to entering the selection process.
2. Clearly and unambiguously communicate the criteria and timing for the Random Selection Process to the public.
3. Commence consultations for proposals to amend zoning bylaws to permit Cannabis Retail Sales in applicable direct-control zones and special areas as soon as practicable.

Council has requested a further report regarding the selection process be provided to the Urban Planning Committee on May 22, 2018.

Additional details regarding the issuance of permits and licences for micro-cultivation and micro-processing facilities and cannabis lounges are expected as and when the federal and provincial rules respecting them are clarified.

For further information, see the City of Edmonton's [Cannabis Legalization webpage](#).

Calgary

On April 5, 2018, Calgary City Council considered two sets of bylaw amendments to Cannabis Facility, Cannabis Store and Cannabis Counselling uses as discretionary uses within certain districts (i.e. commercial and industrial districts in which liquor stores are permitted), and in respect of minimum separation distances and other requirements of cannabis businesses. The definition amendments were carried, while the second set of amendments was reviewed and read twice, and referred for further reporting at a future Council meeting.

The proposed amendments included minimum separation distances from a Cannabis Store of 200 metres from a School, 20 metres from a Liquor Store, 150 metres from an Emergency Shelter, 10 metres from a Child Care facility and 300 metres from another Cannabis Store. However, these distances remain subject to debate and approval by City Council, and Council has also engaged in debate and requested further reports regarding potential other separation distances from pay day loan businesses, religious facilities, etc.

Although the actual separation distances remain uncertain, the City of Calgary has already opened applications for Development Permits on April 24, 2018. Applications could be submitted online or

in person, and the City engaged potential applicants through an online webinar and FAQ.

This process created a rush to file first to gain advantage over competing applicants, particularly within a known conflict area based on the proposed separation distances.

While a race to file avoids exercise of discretion by the City in deciding between competing applications at the outset, it does create an arbitrary distinction when applicants may be separated by mere seconds in submitting an online application. The timing of submission of applications while the actual separation distances remain uncertain also introduces substantial potential for confusion. Finally, the absence of an AGLC-based pre-qualification criteria again introduces the potential for Development Permits to be issued to businesses that have been or will be rejected by the AGLC following their criminal background check and related due diligence, which would increase the administrative burden and investor uncertainty.

For further information, see the City of Calgary's [Cannabis Legalization webpage](#) and [Cannabis Store Business Guide](#).

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[1] Section 3.2.2, [Retail Cannabis Store Handbook](#).