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HNHPC, INC.

SUPERIOR COURT OF THE STATE OF CALIFORNIA

FOR THE COUNTY OF ORANGE

HNHPC, INC.,

Petitioner/Plaintiff,

vs.

CALIFORNIA DEPARTMENT OF TAX AND FEE ADMINISTRATION, a department of the California Government Operations Agency; THE CALIFORNIA OFFICE OF ADMINISTRATIVE LAW, a department of the California Government Operations Agency; and DOES 1-50, inclusive,

Respondents,

CASE NO. 30-2023-01369643-CU-WM-WJC

VERIFIED PETITION FOR WRIT OF MANDAMUS AND COMPLAINT

Assigned for All Purposes Judge Richard Lee

Petitioner HNHPC, INC. ("HNHPC" or "Petitioner"), by and through its attorneys, hereby complains, alleges, and avers as follows against Respondents CALIFORNIA DEPARTMENT OF TAX AND FEE ADMINISTRATION ("CDTFA"), CALIFORNIA OFFICE OF ADMINISTRATIVE LAW ("OAL") – both of which are departments within the California Government Operations Agency – and DOES 1-50 (collectively "Respondents"):

INTRODUCTION

1. This action arises because Respondent CDTFA, under the false guise of enacting "interpretive" regulations and using a contrived and non-existent "emergency" to do so shortly before its emergency powers ended, improperly promulgated Regulation 3802, *Gross Receipts from Sales of Cannabis and Cannabis Products,* ("Regulation 3802") and amended Regulation 3700, *Cannabis Excise and Cultivation Tax*, ("Regulation 3700") relating to the payment of excise tax on cannabis-related products in violation of the Administrative Procedures Act ("APA"). This action also arises because Respondent OAL improperly approved the enactment of Regulation 3802 and the amendment to Regulation 3700 in violation of the APA. Respondents' primary purpose in enacting such new/amended regulations was to improperly *expand the cannabis excise tax base* and to prevent HNHPC and other "Catalyst"-branded dispensaries from continuing to *properly* exclude "cannabis accessories" (*i.e.,* non-cannabis tangible personal property) from the cannabis excise tax. Excluding charges for "cannabis accessories" from excise taxation is in admitted compliance with both the provisions of the Revenue and Tax Code ("RTC") and the CDTFA's own existing interpretive regulations, which HNHPC accomplished by separately identifying on an invoice to its customers the price paid for items which constitute both taxable "cannabis" and "cannabis product" and non-taxable "cannabis accessories."

2. Why did Respondents do this? Because, currently, most cannabis retailers have either (i) failed to realize that "cannabis accessories" are *not* subject to cannabis excise taxation, and thus have been massively overpaying such taxes to the State's unjust benefit; or (ii) failed to properly exclude non-taxable "cannabis accessories" by segregating and "separately stating" such items on their invoices/receipts. As a result, the CDTFA and the State, thus far, have substantially benefited financially from the ignorance of those other dispensaries via the *massive overcollection of cannabis excise tax* on

items that legally are not subject to excise taxation. However, upon realizing that HNHPC and other "Catalyst"- branded dispensaries properly had excluded "cannabis accessories" for purposes of remitting cannabis excise tax to the CDTFA via procedures established under the CDTFA's own regulations and which the CDTFA agrees were proper – the CDTFA initiated "emergency regulation" procedures for the purpose of preventing HNHPC and others from continuing (or from implementing) such previously approved cannabis excise tax exclusion practices, and by retroactively rendering such practices ineffective.

3. Simply put, the CDTFA abused its emergency regulatory authority to "cram down" improperly *retroactive* and generally incoherent regulations on little or no notice that facially contravene the stated intent of Proposition 64 ("Prop 64"), the Cannabis Tax Laws implemented as part of Prop 64 (the "CTL"), commencing with RTC §34010 et seq., as well as their own previously promulgated regulations, all to force HNHPC and other retailers to pay (or continue to pay) cannabis excise tax on items that legally are *not subject to excise taxation*. And in doing so, Respondents: (i) purposefully disregarded the intent of Prop 64, (ii) contradicted the statutory language and history of the CTL (as enacted by Prop 64 and as subsequently amended), (iii) retroactively rendered its own existing and contradictory interpretive regulations "inoperative" without any notice, and (iv) blatantly violated and even ignored the APA's procedural requirements, including by fabricating a non-existent "emergency."

4. As such, via this Petition, HNHPC seeks a writ of mandate invalidating CDTFA's newly promulgated Regulation 3802 and amendment to Regulation 3700(i), prohibiting them from implementing or enforcing such regulations and the interpretations therein, and HNHPC also seeks a judicial declaration that, under the CTL, separately stated "cannabis accessories" are *not* subject to the cannabis excise tax – the same conclusion previously reached by both the Legislature and the CDTFA itself, but which the CDTFA improperly is now trying improperly to *reverse* under its newly promulgated "interpretive" regulations. *See Dyna-Med, Inc. v. Fair Employment & Housing Com.* (1987) 43 Cal. 3d 1379, 1389 ("An administrative agency cannot by its own regulations create a remedy which the Legislature withheld"; "Administrative regulations that alter or amend the statute or enlarge or impair its scope are void and courts not only may, but it is their obligation to strike down such regulations"); *Ellena*

v. Department of Ins. (2014) 230 Cal. App. 4th 198, 205 (where an ordinance defines the specific duties or course of conduct a governing body must take, that course of conduct becomes mandatory and eliminates any discretion); *Alameda Cnty. Deputy Sheriff's Assn. v. Alameda Cnty. Emps.' Ret. Assn.* (2020) 9 Cal. 5th 1032, 1060 (agencies have "no authority to act inconsistently" with governing legislation or to pursue a practice contrary to such legislation).

PARTIES AND VENUE

5. Petitioner HNHPC, INC. ("HNHPC") at all times was a duly licensed cannabis retail dispensary subject to the payment of California's cannabis excise tax on cannabis-related products. HNHPC is one of approximately 26 "Catalyst"-branded cannabis dispensaries licensed to operate in the State of California ("State"). HNHPC operates a retail dispensary in Santa Ana, California, which is located in the County of Orange, State of California. At all relevant times, HNHPC has incurred cannabis excise tax liability arising from retail sales transactions that occurred at its Santa Ana dispensary.

6. Respondents CDTFA and the OAL are departments within the State of California's Government Operations Agency ("GOA"), which HNHPC is informed and believes is an administrative agency whose director reports directly to Governor Newsom. As HNHPC understands it, the CDTFA drafted the challenged emergency regulations/amendments and purported to comply with (but did not actually comply with) the rules and procedures established by the APA and which are applicable to the promulgation of emergency regulations. Once CDTFA purportedly completed the emergency regulation process, it submitted its proposed regulations to the OAL, which is specifically charged with assessing whether there in fact is an emergency and whether the CDTFA's regulations "pass legal muster" and properly can be enacted. HNHPC is informed and believes that Respondents, during the OAL review process, colluded to alter and create new regulations outside of, and in violation of, applicable public notice requirements, and then attempted to "cover up" their misconduct. Because each of them acted improperly in the performance of their respective roles and duties, HNHPC has named both as Respondents herein. Notably, and ironically, both the CDTFA and OAL are housed within the GAO, which in effect creates a situation where the OAL reviews the proposed regulations of

a *sister agency* (the CDTFA) for legal compliance, while *both* departments are under the control and direction of a single agency (the GAO) and the same director who reports directly to the Governor. So in effect, the OAL acts as a "rubber stamp" and/or advocate for the CDTFA, rather than as an independent and objective agency charged with ensuring the provisions of the APA are strictly adhered to for proposed regulations.

7. HNHPC is ignorant of the true names and capacities of the Defendants/Respondents sued herein as DOES 1 through 50, inclusive, and therefore sues such Defendants/Respondents by fictitious names. HNHPC will amend its claims to allege the true names and capacities of DOES 1-50 when they have been ascertained. HNHPC is informed and believes, and on that basis, alleges each of the fictitiously named Defendants/Respondents are responsible in some manner for the acts, omissions, events and occurrences herein alleged, and that HNHPC's damages herein alleged were proximately caused in some way by such DOE Defendants/Respondents.

FACTS RELEVANT TO ALL CAUSES OF ACTION

STATUTORY AND REGULATORY FRAMEWORK

Proposition 64, a Ballot Initiative, Legalizes and Regulates Recreational Cannabis Use and Sale

8. On November 8, 2016, California voters passed Proposition 64 ("Prop 64"), a ballot initiative that, *inter alia*, legalized, regulated and taxed recreational marijuana sales in California. As stated in the ballot initiative, "it is the intent of the people in enacting this act to accomplish", among other things, " tax the growth and sale of *[cannabis]* in a way that drives out the illicit market for *[cannabis]* and discourages use by minors and abuse by adults." (Emphasis added). To that end, Prop 64 added the CTL – (RTC §§34010 et seq. – which established the framework for imposing a cannabis excise tax upon purchasers of cannabis and cannabis products and required cannabis retailers to collect and remit the cannabis excise tax to the CDTFA. (See RTC §34011 (all references to "marijuana" were ultimately changed to "cannabis" pursuant to SB-94)). In accordance with the intent of Prop 64, the voters added to the following language to RTC §34011:

> Effective January 1, 2018, a [cannabis] excise tax shall be imposed on purchasers of *[cannabis]* or *[cannabis] products* sold in this state at a rate of 15 percent of the gross receipts of any retail

> sale by [a dispensary or other person required to be licensed under the Business and Professions Code].

9. The voters also added RTC §34011(b) to further clarify that, for purposes of the cannabis excise tax, taxable "gross receipts" included *only* receipts from the sale of: (i) cannabis and cannabis products; (ii) any otherwise distinct and identifiable goods or services sold with cannabis and cannabis products, "if not itemized", and (iii) any goods or services if a reduction in the price of cannabis or cannabis products is contingent on the purchase of those goods and services. *See* RTC §34011(b) as enacted via Prop 64.

10. Significantly for purposes of this Petition, it is clear the drafters of Prop 64, when imposing the cannabis excise tax, expressly distinguished between the price a customer paid for "cannabis" and "cannabis products," on the one hand, and the price paid for "any otherwise distinct and identifiable goods or services" (*i.e.,* other non-cannabis property or services) on the other hand.

11. Specifically, for purposes of the CTL, RTC §34010 adopted and used the terms "cannabis" and "cannabis products" as defined in Health and Safety Code ("H&S") §§ 11018 and 11018.1 ("HSC"):

> "cannabis" means all parts of the plant Cannabis sativa L., whether growing or not; the seeds thereof; the resin extracted from any part of the plant; and every compound, manufacture, salt, derivative, mixture, or preparation of the plant, its seeds or resin. H&S § 11018.
>
> "cannabis products" means cannabis that has undergone a process whereby the plant material has been transformed into a concentrate, including, but not limited to, concentrated cannabis, or an edible or topical product containing cannabis or concentrated cannabis and other ingredients. H&S § 11018.1.

12. Notably, as referenced under CDTFA Regulation 3700(a)(2) and (i), Prop 64 also added H&S Section 11018.2, which defined the term "cannabis accessories" as follows:

> Any equipment, products or materials of any kind that are used, intended for use, or designed for use in planting, propagating, cultivating, growing, harvesting, manufacturing, compounding, converting, producing, processing, preparing, testing, analyzing, *packaging*, *repackaging*, storing, *smoking, vaporizing, or containing marijuana or for ingesting, inhaling, or otherwise introducing marijuana or marijuana products into the human body*. (Emphasis added). H&S §11018.2

13. Upon even a cursory review the above HSC definitions, it is beyond legitimate dispute the terms "cannabis" and "cannabis product" are intended to include *only* such items derived directly

from the plant Cannabis sativa L., while "cannabis accessories" are intended to encompass all *other* things not derived therefrom, and which may be sold along with "cannabis" and "cannabis products." It is therefore generally understood that nearly all cannabis retail sales contain a combination of either: (1) "cannabis" and "cannabis accessories", (2) "cannabis product" and "cannabis accessories, or (3) "cannabis", "cannabis products", and "cannabis accessories." Regardless of what combination is involved, *only* cannabis and cannabis products by law (and also by pre-Regulation 3802 regulations) are subject to cannabis excise taxation.

14. A good illustration of how Regulation 3802 changes the application of the tax can be shown by examining the sale of a "vape pen" as referenced in HSC §11018.2. A cannabis "vape pen" consists of a small cartridge of cannabis oil (including the empty cartridge itself), a plastic pen mechanism, and packaging for the pen. Under a plain reading the CTL, with reference to the above-defined terms provided under the HSC, the cannabis excise tax would not apply to separately stated charges for the cartridge, the pen or its battery (which is used to assist inhalation), or the associated packaging, since all such items are expressly included within the definition of a "cannabis accessory." Assume a vape pen sold at retail for $40. If a retailer did not separately state and segregate charges for the cannabis oil (a "cannabis product") from charges for the pen's non-cannabis constituent parts, it would be required by law to collect and remit a 15% excise tax on the entire $40 price of the pen – or $6 in cannabis excise tax. If, however, the retailer "separately states" the charges for cannabis items and non-cannabis items and sufficiently substantiates that the cannabis oil in the pen cost only $5, it would be required by law to collect and remit only 75 cents in excise tax (15% of $5), not $6. *As discussed below,* ***Respondents herein are attempting to force retailers (or more accurately consumers) to pay $6 in excise tax when only 75 cents is actually owed***. Stated differently, to maintain or even expand excise tax revenues to the State, Respondents via regulatory coercion are attempting to force cannabis retailers and consumers to *massively overpay* excise tax and to *prevent them* from complying with the law, which clearly allows them to exclude cannabis accessories from cannabis excise taxation.

SB-94 - Amendments to CTL (as enacted by Prop 64)

15. In 2017, the California State Legislature ("Legislature") enacted Senate Bill No. (SB) 94 (Stats. 2017, ch. 27), which modified and made various amendments to the CTL, including transferring the remittance requirements from the cannabis retailer to the cannabis distributor. The amendments generally were limited to: (i) replacing the word "marijuana" with the word "cannabis"; and (ii) amending provisions of the CTL to require the distributor to collect the cannabis excise tax from the retailer and remit it to the CDTFA. To that end, the Legislature eliminated RTC §34011(b) and amended RTC §34011(a) to replace the term "gross receipts" with "average market price."

16. It is important to note the purpose of the SB-94 amendment was to change the point of remittance of the cannabis excise tax from the retailer to the distributor; it *did not* modify or amend the imposition of the cannabis excise tax, which has always been on "purchasers of cannabis and cannabis products . . . of any retail sale." Prop 64, SB-94; AB-195; RTC §34011(a); RTC §34011.2(a)(a); Regulation 3700(i); Regulation 3800(b). However, because distributors did not sell "cannabis" or "cannabis products" directly to consumers, the Legislature required the distributor to collect the cannabis excise tax from the retailer based on the computed "average market price" (which is intended to equal the retail selling price). In practice, the retailer would charge the consumer for the tax already collected by the distributor. For that reason, the "average market price" was nothing more than a calculation method to yield the expected "gross receipts" of the retail sale of the "cannabis" and "cannabis product" sold at retail. *See* RTC §§34010(b), (c).[1]

Promulgation of 18 CCR §3700

17. Although SB-94 eliminated the "separately stated" language previously set forth in RTC §34011(b), by mid-2019 the CDTFA promulgated Regulation 3700 which established the default rule

[1] Calculating the "average market price" turned on the relationship of the distributor and the retailer. In an arm's length transaction between disinterested parties, "average market price" meant "the average retail price determined by the wholesale cost of the cannabis or cannabis products sold or transferred to a cannabis retailer, plus a mark-up, as determined by the board on a biannual basis in six-month intervals". The "mark-up" was calculated by the CDTFA as the average markup charged by retailers to its customers in relation to the wholesale cost of the goods. In a non-arm's length transaction between related parties (i.e., vertically integrated), the "average market price" reverted back to "the cannabis retailer's gross receipts from the retail sale of the cannabis or cannabis products." See RTC §§34010(b)-(c)(2); §34011(b)(1).

that cannabis excise tax applies only to the sale of "cannabis" and "cannabis products", and not to "cannabis accessories", and also reinstated (and even "toughened") the separate statement requirement which had been removed by the Legislature. More specifically, during the rule making process, the CDTFA recognized that although "the CTL does not explicitly state how the cannabis excise tax applies to the sale of cannabis or cannabis product when sold with cannabis accessories," a review of the defined terms of RTC § 34010 made clear "cannabis accessories such as vaping devices are not considered cannabis or cannabis products and are therefore not subject to the 15 percent cannabis excise tax." With that analysis in mind, the CDTFA enacted Regulation 3700(i) to clarify that "the cannabis excise tax does not apply to cannabis accessories" *unless* the "distributor does not separately state the sales price of the cannabis or cannabis products from the cannabis accessories." Regulation 3700(i). To support this "separately stated requirement," the CDTFA relied on Prop. 64's RTC §34011(b) and determined "the proposed amendments are consistent with the intent of the CTL and California voters."

18. Importantly, Regulation 3700 provides in relevant part: (1) cannabis accessories shall have the same meaning as set forth in HSC §11018.2 (as established by Prop 64, Regulation 3700(a)(2)); and (2) the cannabis excise tax does *not* apply to cannabis accessories (including vape cartridges) if the distributor "separately states the price of the cannabis or cannabis products from the cannabis accessories." *See* Regulation 3700(i) (distributor that separately states must maintain supporting documentation used to establish the cost of the cannabis goods/ accessories, and must separately state such costs on the invoice, receipt or other documentation issued to the purchaser at the time of sale). In other words, via Regulation 3700, the CDTFA *expressly affirmed* that under the language and framework of Prop 64, SB-94 and the resulting CTL, cannabis accessories are *not* subject to cannabis excise tax if charges therefore are separately stated and sales are sufficiently documented.[2]

[2] While HNHPC is *not* challenging the propriety of enacting Regulation 3700, it does note the regulation (1) purports to reinsert and even toughen the prior "separately stated" language removed via SB-94; and (2) purports to add documentation and timing requirements not set forth in the original statutory framework. In other words, while reaffirming the legal distinction between cannabis products and cannabis accessories for purpose of excise tax liability (a distinction it improperly eliminated in the challenged "emergency" regulations), the CDTFA via "interpretive" regulation has tried to make it *much harder* than the drafters of Prop 64 intended for cannabis retailers to avoid payment of excise taxes on non-cannabis accessories.

AB-195 – Amendments to CTL (as enacted by Prop 64, and as Amended by SB-94)

19. On June 30, 2022, the Legislature enacted Assembly Bill No. ("AB") 195 which, as relevant here, modified the CTL to *again* shift the burden of remitting the cannabis excise tax – this time from the distributor *back* to the retailer (as originally envisioned in Prop 64). Specifically, AB-195 rendered RTC §34011 inoperative on April 1, 2023, and added RTC §34011.2(a)(1) to replace it. Significantly, RTC §34011.2(a)(1) is identical to its predecessor in all relevant respects, except the cannabis excise tax is – once again – measured by 15% of the "gross receipts" of any retail sale by a cannabis retailer, rather than the "average market price," since the retailer, not the distributor, is now responsible for remittance of the tax:

> Effective on or after January 1, 20~~18~~23, a cannabis excise tax shall be imposed on purchasers of cannabis or cannabis products sold in this state at a rate of 15 percent of the ~~average market price~~ gross receipts of any retail sale by a cannabis retailer. *See* Subdivision (a)(1) of RTC section 34011.2 (as compared to subdivision (a)(1) of RTC section 34011).

20. It is important to note AB-195 *did not*: (1) modify, amend, or expand any of the relevant definitions provided in RTC §34010, including cannabis, cannabis product and cannabis accessory; (2) amend the RTC to impose cannabis excise tax on "cannabis accessories"; or (3) amend any other provision of the CTL that would reasonably cause anyone (including the CDTFA) to believe RTC §34011.2(a)(1) should be interpreted as *expanding* the cannabis excise tax to include "cannabis accessories" or other non-cannabis tangible personal property. In essence, the Legislature simply reverted the CTL back to what existed when Prop 64 initially was enacted, and "put back" the original language set forth in RTC §34011 as set forth in Prop 64.

21. Although enacted as part of AB-195 in June 2022, RTC §34011.2 became effective on January 1, 2023. In response to the new provision, the CDTFA promulgated a series of emergency regulations, including amendments to Regulation 3700, that became effective January 30, 2023. As relevant here, the CDTFA promulgated Subdivision (b) of Emergency Regulation 3800, *Cannabis Excise Tax and Cannabis Retailer Excise Tax Permit* ("Regulation 3800") to clarify that under RTC §34011.2 the imposed cannabis excise tax is "15 percent of the cannabis retailer's gross receipts from the retail sale of the *cannabis* and *cannabis products* to the purchaser[.]" 18 CCR §3800(b) (Emphasis

added.). Furthermore, in the various amendments to Regulation 3700 initially made in response to RTC §34011.2, *the CDTFA neither modified nor altered* Regulation 3700(i). The CDTFA understood that, notwithstanding the AB-195 amendments, the CTL continued to impose cannabis excise tax *only on* receipts "from the retail sale of *cannabis* and *cannabis products*," and that Regulation 3700(i) properly describes the cannabis excise tax regime after enactment of RTC §34011.2.

Summary of CTL from Prop 64 to AB-195

22. Briefly stated, the evolution of the CTL, from Prop 64 to AB-195, can be described as a series of shifts in the collection and remittance of the cannabis excise tax from the distributor to the retailer, while the non-taxable treatment of non-cannabis tangible personal property (such as cannabis accessories) has remained consistent.

23. Under the CTL, as enacted by Prop 64, non-cannabis tangible personal property was subject to the cannabis excise tax *only when*: (i) the sale of non-cannabis tangible personal property, if sold with cannabis or cannabis products, was "*not separately stated"* on an invoice or receipt given to the purchaser; and (ii) a reduction in the price of "cannabis" or "cannabis product" was conditioned on the purchase of non-cannabis tangible personal property. RTC §§34011(a), (b), as enacted under Prop 64 on November 9, 2016 (emphasis added). Thus, under Prop 64, "cannabis accessories" were not subject to cannabis excise tax.

24. Under the CTL, as amended by SB-94, the CDTFA recognized non-cannabis tangible personal property remained excluded from cannabis excise tax, promulgating a rule under Regulation 3700(i) that required charges for such items to be separately stated on the invoice when sold with cannabis or cannabis products. *See* Regulation 3700(i).

25. Under the CTL, as amended by AB-195, the CTL continued to exclude non-cannabis tangible personal property from the imposition of the cannabis excise tax. Indeed, HNHPC and the CDTFA both agreed (at least as of January 2023) that notwithstanding the change in the remittance point from distributor to retailer, RTC §34011.2 continued to impose cannabis excise tax *only* upon gross receipts from the sale of cannabis and cannabis products (as defined in Prop 64) and not on the

sale of separately stated cannabis accessories. The exclusion for separately stated charges on cannabis accessories has never changed from Prop 64 to now and there is no support to the contrary.

26. Yet, *in the twelfth month of 2023*, and on the eve of the expiration of its emergency regulatory authority (which ends December 31, 2023), Respondents enacted an emergency regulation – Regulation 3802 – that under the false guise of "clarification" of RTC §34011.2 directly contradicts its own interpretive Regulation 3800 (which ironically itself was promulgated to "clarify" RTC §34011.2) *and* also made improper "emergency" amendments to inactivate the CDTFA's prior interpretation in Regulation 3700(i) that directly contradict its "new" interpretation of the CTL's treatment of cannabis accessories.

27. This begs the obvious question – what happened between January 1, 2023 and December 2023 to cause CDTFA to do a "180-degree turn" and misuse the emergency regulation process to "jam through" amendments that flatly contradict the language and framework of the CTL and two of its own prior interpretive regulations? The answer is simple – HNHPC and the other Catalyst-branded dispensaries remitted excise tax payments in conformity with the CTL and those regulations, and the CDTFA was not happy with the amount paid or the fact they were able to properly distinguish between taxable cannabis/cannabis products and non-taxable cannabis accessories. Stated differently, when the CDTFA learned HNHPC and the other Catalyst-branded dispensaries had found a way to separately state cannabis accessories, thereby exempting them from excise taxation, Respondents engaged in a "mad scramble" to do anything and everything possible to *prevent* them from continuing to do so and to dissuade other retailers from even *thinking* of also doing so. In short, this action was made necessary by the CDTFA's legally improper "money grab" in violation of the CTL and its own regulations, and the OAL's legally improper approval of the CDTFA's legally invalid "emergency" regulations.

CDTFA'S MOTIVATION

Excise Tax Audit of HNHPC and Other "Catalyst" Entities by the CDTFA

28. For at least half the year in 2022, an affiliate of Catalyst was the distributor for most if not all of the Catalyst-branded dispensaries (the "Catalyst Distributor"), including HNHPC.

29. During that period, the Catalyst Distributor separately stated the price of "cannabis", "cannabis products," and "cannabis accessories" it sold to HNHPC and other Catalyst-branded dispensaries, and properly calculated and remitted the cannabis excise tax to the CDTFA based solely on "cannabis" and "cannabis products" it distributed to those Catalyst-branded dispensaries.

30. In or around March 2023, the CDTFA initiated an audit of the Catalyst Distributor for pre-January 1, 2023 cannabis excise tax payments – *i.e.,* during the period the Catalyst Distributor was still legally responsible under RTC §34011 for remitting cannabis excise taxes.

31. In connection with the audit, the Catalyst Distributor maintained that its calculation of the cannabis excise tax fully complied with, *inter alia*, RTC §34011 and Regulation 3700(i).

32. Eventually, the CDTFA acknowledged ***in writing*** that the Catalyst Distributor's interpretation of its excise tax obligations was correct, and that the "cannabis accessories" which had been separately stated on invoices provided to the Catalyst-branded retailers (including HNHPC) were *not* subject to cannabis excise tax. Specifically, in an emails dated September 8, 2023 and September 20, 2023, Joseph Ward of the CDTFA confirmed that separately stated and substantiated cannabis accessories distributed prior to January 1, 2023 were not subject to cannabis excise taxation. Thus, for the pre-2023 cannabis excise tax periods, the CDTFA conceded Catalyst *correctly* interpreted and applied the cannabis excise tax law, and more importantly, that cannabis accessories legally *were not* subject to cannabis excise taxation.

33. Beginning after January 1, 2023, the Catalyst-branded dispensaries, including HNHPC, applied the same procedures set forth in Regulation 3700(i) to maintain the proper collection of the cannabis excise tax from its customers. In so doing, the Catalyst-branded dispensaries, including HNHPC, separately stated on receipts provided to the customer the price of the "cannabis", "cannabis product", and "cannabis accessories" purchased in each retail sales transaction.

34. Under this practice, the Catalyst-branded dispensaries, including HNHPC, properly collected cannabis excise tax on "cannabis" and "cannabis products" sold in consumer transactions – in full compliance with RTC §34011.2, Regulation 3700(i) (which was then still in full effect), and the

CDTFA's newly promulgated Regulation 3800(b) reaffirming the interpretation in Regulation 3700(i) that only cannabis and cannabis products legally were subject to cannabis excise taxation.

35. However, in or around May of 2023, several Catalyst-branded dispensaries, including HNHPC, received notice the CDTFA was auditing their excise tax remittances for Q1 and Q2 2023.

36. In or around September 2023, HNHPC learned the CDTFA had rejected its position that cannabis excise tax does not apply to gross receipts of sales of "cannabis accessories" when they are separately stated and segregated out on a consumer invoice. More specifically, the CDTFA took the position that AB-195 amended the CTL to such an extent that, starting January 1, 2023, retailers were required to collect and remit cannabis excise tax on retail sales of "cannabis accessories." Notably, its position was the polar opposite of the interpretation contained in Regulation 3800(b), which the CDTFA promulgated in January 2023 to *interpret* the newly effective RTC §34011.2. In short, over a period of eight months, the CDTFA's "interpretation" on the taxability of cannabis accessories began to resemble a notable Katy Perry song – it was hot then cold, yes then no, in then out, up then down. Indeed, the only people that appeared to be "confused" on the subject was the CDTFA itself.

37. On September 14, 2023, the CDTFA issued a Notice of Determination to multiple Catalyst-branded dispensaries, including HNHPC, alleging its audit found a significant underpayment of cannabis excise tax. In response, the Catalyst-branded dispensaries, including HNHPC, informed the CDTFA auditors that they intended to appeal the CDTFA's audit determination. Notably, the alleged underpayment was based almost entirely on the CDTFA's newly-contrived position that cannabis accessories *legally were* subject to cannabis excise taxes, and Catalyst (including HNHPC) had failed to collect and remit excise tax on separately stated cannabis accessories.

38. ***On October 2, 2023, shortly after Catalyst/HNHPC informed the CDTFA of their intention to appeal, the CDTFA initiated "emergency" rulemaking proceedings for the purpose of enacting new "emergency" regulations to provide "bootstrap" support for its interpretation on cannabis accessories, and also (as HNHPC later learned) laid the groundwork to remove/de-activate "bad" interpretive regulations that fatally undermined its newly-contrived tax position – including both Regulations 3700(i) and 3800(b)***.

39. On October 11, 2023, HNHPC and the other Catalyst-branded dispensaries filed a formal notice of appeal of the CDTFA's audit determination. HNHPC contends the "rush" to promulgate Regulation 3802 and to deactivate 3700(i) was driven by CDTFA's desire to "beat" the Catalyst appeal, to prevent them from continuing to separately state and exclude cannabis accessories from cannabis excise taxation, and to dissuade other dispensaries from following Catalyst's lead.

CDTFA'S "EMERGENCY REGULATIONS"

The CDTFA Proposes Regulation 3802 Using its Emergency Rulemaking Authority

40. On October 2, 2023, the CDTFA distributed a Discussion Paper to interested parties seeking input on whether the CDTFA should, pursuant to its soon-expiring emergency rulemaking authority under RTC §34013, adopt Regulation 3802 to "clarify the meaning of 'gross receipts' from the sale of cannabis and cannabis products for purposes of the cannabis excise tax imposed by [RTC Section 34011.2]." The CDTFA held an interested persons meeting on October 12, 2023, and permitted interested parties to submit written comments by no later than October 20, 2023.

41. The consensus among the interested parties, including HNHPC, was that proposed Regulation 3802: (1) improperly expanded the cannabis excise tax and went far beyond the statutory parameters of the CTL, (2) conflicted with, and was contrary to, the CDTFA's own cannabis regulations, and (3) generally was incomprehensible. As far it could tell, not one interested party that meaningfully participated in the rulemaking process agreed with the CDTFA's "new" interpretation that cannabis excise tax could be imposed on items other than "cannabis" or "cannabis products."

42. Many of the interested parties also expressed their belief that the CDTFA sought without legal authority to promulgate emergency regulations relating to Sales and Use Tax Law ("SUTL") (RTC section 6001, et seq.) and to implement "long standing opinions" of its legal counsel.

43. In response to the comments, the CDTFA modified the proposed provisions of Regulation 3802 and – without additional input from the interested parties – submitted its Notice of Proposed Emergency Action ("Notice") to the OAL on December 5, 2023.

44. After carefully reviewing the Notice, HNHPC discovered that, not only did the CDTFA change the purported scope of Regulation 3802 – from "clarifying the meaning of 'gross receipts' from

the sale of cannabis and cannabis products for purposes of the cannabis excise tax imposed by [RTC Section 34011.2]" to "clarify[ing] the meaning of the phrase 'gross receipts from any retail sale by a cannabis retailer' as used in subdivision (a)(1) of RTC [S]ection 34011.2," the CDTFA also failed to remove many of the fatal flaws of the proposed provisions of Regulation 3802.

45. HNHPC also discovered the CDTFA's alleged effort to "clarify the meaning of the phrase 'gross receipts from any retail sale by a cannabis retailer' as used in subdivision (a)(1) of RTC [S]ection 34011.2," was entirely devoid of any analysis or meaningful discussion of: (i) the framework of the CTL or its own prior interpretations, (ii) the relevant statutory language, (iii) any of the defined terms of the CTL, including the three (3) defined terms used in the phrase itself; (iv) any informative regulations or court decisions; or even (iv) the taxability of "cannabis accessories". In fact, the CDTFA mentions the relevant phrase *only once* in its analysis, where it proclaimed, without explanation, that "subdivision (a) of RTC Section 34011.2 . . . makes the 'gross receipts of any retail sale by a cannabis retailer' the measure of tax." The CDTFA then saw fit to promulgate, with no explanation at all, provisions of Regulation 3802 that subject all tangible personal property to the cannabis excise tax, *except* for "reasonable amounts charged for" "optional tangible personal property." In short, Regulation 3802 is nothing more than an expression of what the CDTFA now *wishes* the CTL said, but does not actually say and significantly has *never said*.

46. In an effort to prevent the promulgation of this dangerous and ill-conceived "dumpster fire" regulation, HNHPC joined other Catalyst-branded dispensaries in submitting a written comment to the OAL informing them it should disapprove Regulation 3802 on the grounds there was no emergency and the regulation failed (and continues to fail) to comply with (i) the clarity standard, (ii) the necessity standard, (iii) the consistency standard, (iv) the authority standard, and (v) reference standard as required in Government Code ("GC") section 11349.1 (the "Catalyst Written Comment").

47. The Catalyst Written Comment was submitted in compliance with 1 CCR §55(b) and OAL therefore legally was required to consider it.

48. Unfortunately, on December 15, 2023, the OAL Staff Attorney informed Catalyst via email that Regulation 3802 "was approved and filed with the Secretary of State" along with a copy of the filing submitted to the Secretary of State.

49. A review of the filing informed HNHPC that, for the first time, the CDTFA also sought to amend, and the OAL permitted it to amend, subdivision (i) of Regulation 3700 to add a new subsection (i)(3) that reads "Subdivision (i) is inoperative on and after January 1, 2023."

50. The CDTFA's intention to amend 3700 was never disclosed in its Discussion Paper, in the Notice, on its website, or in the rulemaking file it submitted to the OAL. In fact, it was not until the OAL Staff Attorney provided the Catalyst Group with a copy of the filing itself did the Catalyst Group discover Regulation 3700 had been subjected to a drastic amendment in complete violation of the notice and public participation requirements of the APA. Indeed, the fact Regulation 3700 had been amended was *handwritten in*to the approval form – evidencing the CDTFA submitted its amendments thereto *after* it submitted the package to the OAL for approval. Incredibly, and improperly, the OAL approved the amendments to Regulation 3700 despite being submitted at the 13th hour without any notice and without actually undergoing the rulemaking process, emergency or otherwise.

51. This surprise amendment prompted HNHPC to immediately make a Public Records Act Request ("PRA") on December 15, 2023 to both the CDTFA and OAL in order to better understand what the CDTFA submitted to the OAL (the "PRA Request"). The PRA Request asked for the entirety of the rulemaking file and the written communications, if any, between the CDTFA and the OAL related to the submission, and subsequent approval, of Regulation 3802 and the amendment of 3700. The OAL provided at least some of the requested documents and communications on December 22, 2023, and its revelations were *shocking* in that, for the first time, HNHPC learned the CDTFA had substantially modified Regulation 3802 after submission to the OAL, and the OAL had approved that substantially modified version of Regulation 3802, without informing the interested parties.

52. Specifically, the PRA Request revealed that immediately upon receiving the Catalyst Written Comment, the CDTFA and OAL engaged in a concerted *joint* effort to use the final days of the

OAL's regulatory review to "fix" some of the many fatal flaws in the proposed emergency regulation, included holding a "Teams" meeting on December 14, 2023 "to discuss [the OAL's] review".

53. Although the details of the meeting were not disclosed, the emails between the CDTFA and OAL reveal the OAL had concluded that the proposed regulations failed to satisfy at least the 'clarity' standard set forth in GC §11349.1(a)(3). In response, the CDTFA committed to "working on the revisions to Regulation 3700 and 3802 that [the OAL] suggested . . . so CDTFA does not need to withdraw the rulemaking file.". Pursuant to that commitment, the CDTFA began sharing revisions to Regulation 3802 and Regulation 3700 to see if "they are okay with [OAL] management."

54. Then, on December 15, 2023 (*i.e.,* the last day of the OAL's review period), the OAL confirmed it was satisfied the revised text and that it would "need the final version of the text with authorization to *swap* it out of the record" and to have the CDTFA " email [it] the *necessary fixes* by 10:30am so [the OAL] can get everything ready for filing." After the CDTFA complied, the OAL approved the modified provisions of Regulation 3802 and the amendment to 3700 and immediately filed the emergency regulations with the Secretary of State for publication.

55. In short, the OAL during its review period concluded that the emergency regulations did not comply with the APA. However, rather than disapprove the emergency regulation or forcing the CDTFA to withdraw them and to start the APA process over again (as it should have), the OAL instead worked directly with the CDTFA to: (i) amend Regulation 3700 and make substantial changes to Regulation 3802; (ii) "*swap*" the emergency regulations in the rulemaking file; and (iii) approve the modified emergency regulations and immediately submit the regulations to the Secretary of State. To add insult to injury, neither the CDTFA nor the OAL ever informed the public of the changes to Regulation 3802 or the amendment to Regulation 3700. In fact, HNHPC may be the only interested party aware that further changes were made to Regulation 3802. As far as the Notice is concerned, the CDTFA sought to enact Regulation 3802 as provided therein. Then, within 15 days, the OAL approved a substantially different version of Regulation 3802 *and* an amendment to 3700 that was never disclosed. Said differently, the CDTFA submitted A, the OAL approved B, did not tell the public what

they had done, and then incredibly they conspired to *alter the official rule making file* in an effort to cover up their misconduct.

FIRST CAUSE OF ACTION
PETITION FOR PEREMPTORY WRIT OF MANDATE
(AGAINST ALL RESPONDENTS)

56. HNHPC incorporates as though set forth herein in full the allegations contained in Paragraphs 1-55 above.

57. Via this Cause of Action, HNHPC challenges multiple different actions of Respondents. First, HNHPC challenges the promulgation of the emergency amendment to Regulation 3700 on the grounds there was no emergency, Respondents failed to provide any notice of their intention to amend that regulation, because it constitutes an improper retroactive amendment, and because it does not meet the legal standards necessary to promulgate or amend an emergency regulation. Second, HNHPC challenges the promulgation on emergency Regulation 3802 on the grounds no emergency existed, it fails to satisfy the legal standards for regulation promulgation (and discussed further herein), and because the "interpretation" advanced therein is nonsensical, defies the intent, express provisions and statutory framework of the CTL, cannot be reconciled with its prior interpretations as set forth in Regulations 3700(i) and 3800(b) and its audit of Catalyst Distributor, and cannot even be internally reconciled with the express language of RTC §34011.2 itself. Third, Respondents violated the APA by secretly changing the proposed amendment to Regulation 3700 and Regulation 3802 during the OAL review period, while withholding that information from the public then by altering the official file to conceal their misconduct. Fourth, HNHPC seeks an order compelling Respondents to comply with Prop 64, the CTL under a proper interpretation of the law, i.e., that cannabis accessories are not subject to cannabis excise tax, to prohibit them from interpreting and applying the governing law incorrectly or acting contrary to the controlling statutes, and to force them to comply with the APA and the controlling emergency regulation procedures.

58. HNHPC's challenges require the Court to determine whether the emergency rulemaking standards were satisfied, and to interpret and apply the language and framework of the CTL, as enacted by Prop 64 and the amendments made thereto, the APA, the CDTFA's own prior rulings and

interpretations, and the requirements of the OAL review process, the entirety of HNHPC's challenge is subject to *de novo judicial review* in connection with which little if any deference should be given to Respondents' newly contrived interpretations or applications of the relevant statutes and regulations. *Sims*, 216 Cal. App. 4th at 1080–81; *Yamaha Corp. of America v. State Board of Equalization* (1998) 19 Cal. 4th 1, 11; *State Farm Gen. Ins. Co. v. Lara* (2021) 71 Cal. App. 5th 148, 169 ("Interpretation of a statute or regulation is, of course, an issue of law for the court [citations], as is the question whether a regulation is consistent with the authorizing statute [citations]. Thus, we must review the interpretations of the [agency] and the trial court *de novo*, and come to our own independent conclusions on these issues"); *Dyna-Med,* 43 Cal. 3d at 1389 ("An administrative agency cannot by its own regulations create a remedy which the Legislature withheld"; "Administrative regulations that alter or amend the statute or enlarge or impair its scope are void and courts not only may, but it is their obligation to strike down such regulations"); *Alameda Cnty.*, 9 Cal. 5th at 1060 (agencies have "no authority to act inconsistently" with governing legislation or to pursue a practice contrary thereto).

REGULATION 3802 AND THE AMENDMENTS TO REGULATION 3700 MUST BE INVALIDATED FOR FAILURE TO IDENTIFY OR SUBTANTIATE THE EXISTENCE OF AN ACTUAL "EMERGENCY"

59. The CDTFA enacted Regulation 3802, and also amended Regulation 3700(i) to add subsection (1)(3), pursuant to its grant of emergency rulemaking authority under RTC §34013(e):

> **Until January 1, 2024**, the department may prescribe, adopt, and enforce any emergency regulations as necessary to implement, administer, and enforce its duties under this division. Any emergency regulation prescribed, adopted, or enforced pursuant to this section shall be adopted in accordance with Chapter 3.5 (commencing with Section 11340) of Part 1 of Division 3 of Title 2 of the Government Code, and, for purposes of that chapter, including Section 11349.6 of the Government Code, the adoption of the regulation is an emergency and shall be considered *by the Office of Administrative Law* as necessary for the immediate preservation of the public peace, health and safety, and general welfare. (Emphasis added.)

60. Under GC §11350(a), "[a]ny interested person may obtain a judicial declaration as to the validity of any regulation or order of repeal by bringing an action for declaratory relief in the superior court in accordance with the Code of Civil Procedure . . . The regulation or order of repeal may be declared to be invalid for a substantial failure to comply with this chapter, or, in the case of an emergency

regulation or order of repeal, upon the ground that the facts recited in the finding of emergency prepared pursuant to [GC §11346.1(b)] do not constitute an emergency within the provisions of [§] 11346.1."

61. GC § 11346.1(b)(1) further provides a regulation "may be adopted as an emergency regulation or order of repeal" only if "if a state agency makes a finding that the adoption of a regulation or order of repeal is necessary to address an emergency." GC § 11346.1(b)(2) provides that "[a]ny finding of an emergency shall include . . . a description of the specific facts demonstrating the existence of an emergency and the need for immediate action, and demonstrating, by substantial evidence, the need for the proposed regulation to effectuate the statute being implemented, interpreted, or made specific and to address only the demonstrated emergency." And GC §11346.1(b)(2) provides that "[t]he enactment of an urgency statute shall not, in and of itself, constitute a need for immediate action" and "[a] finding of emergency based only upon expediency, convenience, best interest, general public need, or speculation, shall not be adequate to demonstrate the existence of an emergency."

62. Finally, even the acknowledged existence of an emergency requires additional supporting disclosures: "[i]f the situation identified in the finding of emergency existed and was known by the agency adopting the emergency regulation in sufficient time to have been addressed through nonemergency regulations . . . the finding of emergency shall include facts explaining the failure to address the situation through nonemergency regulations." GC §11346.1(b)(2).

63. In the present case, the Notice's *Statement of Emergency* does nothing more than regurgitate the statutory requirements contained in RTC §§34013(c) and (e) and is *entirely devoid* of "a description of the specific facts demonstrating the existence of an emergency and the need for immediate action," as required by GC §11346.1(b)(2). In addition, nowhere in the Notice did the CDTFA demonstrate "by substantial evidence, the need for the proposed regulation to effectuate the statute being implemented, interpreted, or made specific and to address only the demonstrated emergency" as required by GC §11346.1(b)(2). In fact, the CDTFA provided *no evidence whatsoever* demonstrating the proposed regulations were even narrowly tailored to "to address only the demonstrated emergency."

64. Simply put, when acting, it is clear Respondents relied on the language of GC §11349.6(c) that "the adoption of the regulation is an emergency and shall be considered by the Office of

Administrative Law as necessary for the immediate preservation of the public peace, health and safety, and general welfare." However, their blind reliance thereon was/is legally improper and deficient, since by law "[t]he enactment of an urgency statute shall not, in and of itself, constitute a need for immediate action" and that "[a] finding of emergency based only upon expediency, convenience, best interest, general public need, or speculation, shall not be adequate to demonstrate the existence of an emergency."

65. Furthermore, although GC Section 11349.6(c) requires the OAL to treat the regulation "as necessary for the immediate preservation of the public peace, health and safety, and general welfare," GC §11346.1(b)(2) nevertheless requires, at a minimum, a disclosure of facts necessary and sufficient to establish when the CDTFA became aware of the "emergency" and that CDTFA did not have "sufficient time to [address the emergency] through nonemergency regulations," which would require it to provide specific "facts explaining the failure to address the situation through nonemergency regulations". As stated before, *the Notice is devoid of any such facts or information* – and, absent such facts, it should be presumed (if a presumption is required) the "emergency" commenced as of June 20, 2022, the date AB-195 was enacted (*i.e., 18 months prior to the promulgation of the emergency regulations*).

66. In short, a judicial declaration invalidating the emergency regulations is proper, warranted and legally required under GC §11350(a) because the Notice (i) is devoid of facts identifying or substantiating an actual "emergency," (ii) relied solely and improperly on the existence of an urgency statute in its *Statement of Emergency*, and (iii) failed to provide *any details whatsoever* identifying when the CDTFA became aware of the emergency and whether the "emergency" could have been resolved via the ordinary rulemaking process, as opposed to requiring emergency rule making powers.

THE EMERGENCY REGULATIONS FAIL TO SATISFY THE CENTRAL "NOTICE" AND "PUBLIC PARTICIPATION" REQUIREMENT OF THE APA AND MUST BE INVALIDATED

67. The CDTFA enacted Regulation 3802, and also amended Regulation 3700, pursuant to its grant of emergency rulemaking authority under RTC §34013(e).

68. Pursuant to GC §11350(a), "[a]ny interested person may obtain a judicial declaration as to the validity of any regulation or order of repeal by bringing an action for declaratory relief in the

superior court in accordance with the Code of Civil Procedure . . . The regulation or order of repeal may be declared to be invalid for a *substantial failure* to comply with this chapter."

69. Under the APA, the "adoption, amendment, or repeal of an emergency regulation" are required to "substantially comply" with GC §§11346.1, 11349.5, and 11349.6.

70. GC §11346.1(a)(2) requires that, unless "the emergency situation clearly poses such an immediate, serious harm that delaying action to allow public comment would be inconsistent with the public interest", then "[a]t least five working days before submitting an emergency regulation to the [OAL], the [CDTFA] shall . . . send a notice of the proposed emergency action to every [interested party]. The notice shall include both of the following: (A) The specific language proposed to be adopted and (B) The finding of emergency required by subdivision (b)."

71. Here, not only did CDTFA fail to provide the requisite notice mandated by GC §11346.1(a)(2) within "five working days before submitting an emergency regulation to the [OAL]," it was the OAL who informed HNHPC of the emergency amendment *after the OAL had submitted the filing to the Secretary of State.* Furthermore, although GC §11346.1(a)(3) provides an exception to the notice requirement in the case of "immediate, serious harm," the fact the CDTFA provided the Notice with respect to Regulation 3802 clearly demonstrates the non-existence of such a heightened emergency sufficient to dispense with the notice requirement vis-à-vis the amendment to Section 3700.

72. Moreover, although the CDTFA issued the Notice related to the enactment of Regulation 3802, the Notice, itself does not satisfy the requirements of GC §11346.1(a)(2) for purposes the amendment to Regulation 3700(i), since the Notice did not include "the specific language [of Regulation 3700(i)] proposed to be adopted."

73. In addition, and as a natural consequence of failing to provide *any notice* as required by GC §11346.1(a)(2), the CDTFA also failed to comply with GC §11346.1(b)(2), which requires that the notice include the information set forth in GC §11346.5(a)(2)-(a)(6) – namely: (2) reference to authority; (3) the informative digest; (4) other matters as prescribed by statute; (5) the local mandate determinations; and (6) the necessary financial estimates.

74. Moreover, during its review period, the OAL revealed via PRA Request responses that Regulation 3802, as submitted to it, failed to satisfy the 'clarity' standard under GC §11349.1(a)(3). But rather than disapprove it on that basis, OAL instead worked directly with the CDTFA to substantially modify the provisions of Regulation 3802 so it would allegedly comply with the 'clarity' standard. Importantly, the modifications made to the provisions of Regulation 3802 during the OAL process are: (i) substantial because they operate to bring Regulation 3802 into alleged compliance with the 'clarity' standard; and (ii) were never provided to the interested parties pursuant under the procedures set forth in GC §11346.1(a)(2).

75. As previously mentioned, the Court may declare Regulation 3802 and the amendment to Regulation 3700 invalid for "*substantial failure* to comply with the [APA]." Case law provides that "substantial compliance with a statute is dependent on the meaning and purpose of the statute." *Freeman v. Vista de Santa Barbara Associates LP* (2012) 207 Cal.App.4th 791, 793. Furthermore, "noncompliance [with the APA] is insubstantial, or 'harmless,' *only where it* does not compromise any 'reasonable objective' of the APA." *Sims*, 216 Cal.App.4th at 1073. The objectives of the APA are " 'to provide a procedure whereby people to be affected may be heard on the merits of the proposed rules' " and ensure " 'meaningful public participation in the adoption of administrative regulations by state agencies.' " *Id.*

76. Here, both the CDTFA and OAL *purposefully and knowingly* ignored the APA, and did so with the intent of depriving interested parties (including HNHPC) of notice and any reasonable opportunity to be "heard on the merits of the proposed rules' " and to ensure " 'meaningful public participation in the adoption of administrative regulations by state agencies." *Id.* As such, a judicial declaration invalidating the emergency regulation is not only proper under GC §11350(a), but is both warranted and legally required.

77. And to be crystal clear, the CDTFA's failure to provide the required notice and permit "meaningful public participation" cannot remotely be characterized as *harmless*. First, Regulation 3700(i) is a critical regulation that sets forth the CDTFA's own understanding that "the cannabis excise tax does not apply to cannabis accessories." Although the CDTFA claims AB-195 rendered Regulation 3700(i) inoperable, that position ignores that the provisions of Regulation 3700(i) are untethered to any

specific statute of the CTL. Furthermore, the CDTFA was fully aware HNHPC and the Catalyst-branded dispensaries intended to rely on Regulation 3700(i) as part of their legal arguments in the impending tax appeal with the CDTFA. In addition, the modifications to the provisions of Regulation 3802 are substantial because they seek to bring Regulation 3802 into compliance with the 'clarity' standard without participation of the interested parties, even though the 'clarity' standard is intended to benefit the interested parties. Not only is this *harmful*, but it is an unquestionable abuse of the CDTFA's rulemaking authority, emergency or otherwise.

78. The amendment to Regulation 3700(i) also must be invalidated because Respondents improperly "jammed through" via a no-notice "emergency" regulation an amendment as of December 15, 2023 that purported to *retroactively rescind* the CDTDFA's own excise tax interpretation contained in Section 3700(i) as of January 1, 2023 (nearly a year prior to the emergency amendment). The Legislature did not expressly or implicitly authorize Respondents to promulgate or enact such retroactive regulations, and therefore the amendment to Section 3700 was legally improper and exceeded the scope of Respondents' legal authority. *See California Medical Assn v. Lackner* (1981) 117 Cal. App. 3d 552, 564; *McClung v. Employment Dev. Dept.* (2004) 34 Cal. 4th 467, 475 (strong presumption *against* retroactive application of *statutes* absent express language of retroactivity or a clear and unavoidable implication that the Legislature intended retroactive application"). Here there is no language even remotely suggesting that the voters or the Legislature authorized Respondents to promulgate emergency retroactive interpretive regulations or retroactively rescind an interpretation it promulgated a year before.

79. On this issue, Respondents' stated reason for the need to retroactively amend/rescind Section 3700(i) is at best contrived given the factual and procedural history preceding the amendment. As noted above, until *Catalyst/HNHPC expressed an intention to appeal the CDTFA's excise tax determination for Q1 and Q2 2023*, the CDTFA clearly did not believe any amendment to Regulation 3700 was required, or that Section 3700(i) had become obsolete in light of the enactment of RTC §34011.2. Indeed, the CDTFA made amendments (not relevant here) to Section 3700 *after* enactment of RTC §34011.2, but tellingly did not amend or seek to render "inoperative" Regulation 3700(i) until *after* HNHPC stated its intent to appeal. Rather, when it became clear HNHPC would cite Section 3700(i) in

support of its appeal, the CDTFA initiated *secret and expedited* emergency actions (without notice to anyone) to effectively rescind Section 3700(i) so it could not later be used against it by HNHPC or others. That is neither a valid emergency nor the proper use of the rulemaking authority given to the CDTFA. And to the extent that the OAL required CDTFA during the approval process to amend Regulation 3700(i) because it conflicted with Regulation 3802, it acted improperly as its recourse in that instances was to disapprove Regulation 3802 and required CDTFA to "go back to the drawing board." Yet instead it colluded with the CDTFA to approve the two amendments without public notice or input, and even agreed to *alter* the official rulemaking filed to try to conceal what they had done.

80. Finally, the enactment of RTC §34011.2 – the stated reason for the need to retroactively nullify Regulation 3700(i) – objectively had no factual or legal bearing on the applicability or interpretation of Regulation 3700(i); nor did RTC §34011.2 establish, discuss or authorize (explicitly or implicitly) any change in substantive cannabis excise tax policy. For instance, RTC 34011.2(a)(1) expressly provides "a cannabis excise tax shall be imposed upon purchasers of cannabis or cannabis products" at "15 percent of the gross receipts of any retail sale by a cannabis retailer." *See* RTC §34011.2(a)(1). This sentence is fully consistent with Regulation 3700(i), and notably has two express limitations which are significant to the present case.

81. The voters and the Legislature both made clear the CTL was imposing a *cannabis* excise tax, not a general excise tax on all retail sales by cannabis retailers. As such, the cannabis excise tax was imposed *solely* on purchasers of "cannabis and cannabis products" (both expressly defined terms) and *not* on purchasers of cannabis accessories (also a defined term). When RTC §34011.2(a)(1) is read in context, "gross receipts of any retail sale" clearly is meant to refer *only* to the sale of cannabis or cannabis products, *not* the entire retail sale regardless of what is purchased. Significantly, and as discussed below, not even the CDTFA purports to interpret RTC §34011.2(a)(1) to impose a cannabis excise tax on *all items* purchased in a cannabis retail transaction. So if that section was *not* intended to impose an excise tax on *everything* – as admitted by the CDTFA in Regulation §3802 – that merely confirms the clear and unambiguous meaning of RTC §34011.2(a)(1) in that it imposes a 15% excise tax on the gross receipts ***from the purchase of any cannabis or cannabis product***s, and *nothing else*. *Webster v. Superior Court*

(2020) 51 Cal. App. 5th 676, 680 (If the statutory language is clear and unambiguous, the reviewer's task is at an end, since there is no need for judicial construction); *Skidgel*, 12 Cal. 5th at 10-11 (where administrative interpretations are contrary to clear statutory language, they must be rejected).

82. In this regard, immediately after RTC §34011.2 went into effect, the CDTFA promulgated a new interpretive regulation specifically addressing how the excise tax regime would work begining January 1, 2023 – 18 CCR §3800 ("Regulation 3800"). Therein, the CDTFA stated the following:

> A cannabis excise tax is imposed upon purchasers of cannabis or cannabis products sold at retail in this state on and after January 1, 2023, pursuant to Revenue and Taxation Code section 34011.2. ***The tax is 15 percent of the cannabis retailer's gross receipts from the retail sale of the cannabis and cannabis products to the purchaser on or after January 1, 2023***, and the cannabis retailer is responsible for collecting the cannabis excise tax from the purchaser and remitting that tax to the Department. (Emphasis added).

In short, between January 1, 2023 and October 12, 2023, Respondents *agreed* with HNHPC/Catalyst that even under RTC §34011.2, excise tax applied *only* to gross receipts from the retail sale of cannabis and cannabis products – which *does not include* the sale of cannabis accessories, as CDTFA now claims.

83. The purported need to retroactively rescind Section 3700(i) in light of RTC Code §34011.2 also is not supported by any other statutory provisions of Prop 64. RTC §34011(e), as originally enacted under Prop 64, RTC §34011(d) as amended by the Legislature, *and* Section 34011.2(f) *all* make clear that cannabis excise taxation is limited to "gross receipts" upon "the sale of cannabis or cannabis products," and not on *all* sales made in a cannabis retail transaction. *See* RTC §34011.2(f) ("***Gross receipts from the sale of cannabis or cannabis products*** for purposes of assessing the sales and use taxes . . . shall include the tax levied pursuant to this section") (emphasis added). Simply put, if excise taxation was *not* intended to be limited to sales of cannabis and cannabis products, as Respondents now claim, these sections would not have been necessary, and certainly would not have been worded as they were.

84. The structure of Prop 64, as amended over time, also demonstrates the enactment of RTC §34011.2(a)(1) was not intended to alter longstanding law and *for the first time* subject cannabis accessories to excise taxation. As originally enacted, Prop 64 made the retailer responsible for the remitting the excise tax, and did so using the same "gross receipts" language contained in RTC §34011.2(a)(1). No one disputes that as originally enacted, separately stated and segregated cannabis

accessories were not subject to excise tax. Later, the Legislature amended Prop 64 to change the remittance point from the retailer to the distributor. That change necessitated an amendment to RTC §34011 to reflect the distributor's need in certain cases to use a formula to reach anticipated gross receipts of the retail sales – and so "gross receipts" in that instance was replaced with "average market price."

85. When the remittance point statutorily was transferred back to the retailer as of January 1, 2023, the Legislature not surprisingly replaced the "average market price" language with the *original* "gross receipts" language. Nothing more, nothing less. The CDTFA itself did not interpret the phrase "15 percent of the average market price of any retail sale by a cannabis retailer" in the original RTC §34011 to include everything purchased; rather, it properly interpreted that phrase as being limited to cannabis or cannabis products as defined in Prop 64 and the CTL. That interpretation not only is correct, but also clearly survived the enactment of RTC §34011.2. The Legislature was certainly aware of the language and structure of Prop 64 and the CTL prior to enacting RTC §34011.2. It also was certainly aware of the CDTFA's interpretation (in Regulation 3700(i)) that cannabis accessories were *not* subject to cannabis excise tax. Yet nothing in RTC §34011.2 even remotely suggests the Legislature intended to alter the longstanding law excluding cannabis accessories from cannabis excise taxation.

86. Based on the foregoing, any claim by the CDTFA that it needed to rescind Section 3700(i) on an emergency basis in light of RTC §34011.2 going into effect on January 1, 2023, is baseless, contrived, and its conduct were arbitrary, capricious, in excess of its authority, in violation of required notice and procedures, and fundamentally was legally improper.

EMERGENCY REGULATION 3802 MUST BE INVALIDATED

87. As alleged above, in September 2023, the CDTFA twice acknowledged in writing that prior to January 1, 2023, if they were separately stated and substantiated, cannabis accessories legally were not subject to the cannabis excise taxation, and HNHPC's and Catalyst's interpretation of that issue under both Prop 64 generally and RTC Code §34011 specifically was legally correct.

88. In or around May 2023, with full knowledge of HNHPC's and Catalyst's interpretation, the CDTFA initiated an audit of their Q1 and Q2 2023 sales and excise tax calculations. In or around September 2023, the CDTFA rejected their interpretation for post-January 1, 2023 sales, notwithstanding

the fact HNHPC's interpretation was fully consistent with Prop 64, RTC §34011.2, and the CDTFA's own interpretive regulations 3700(i) and 3800. When HNHPC and Catalyst notified the CDTFA it intended to appeal its excise tax determination, the CDTFA, realizing it would *lose* under the clear statutory language and its own *existing* interpretive regulations, fabricated a non-existent "emergency" in order to eliminate its own problematic regulations and advance and replace them with a new and baseless interpretation of the CTL's excise tax provisions in order to defeat Catalyst's expected appeal.[3]

89. More specifically, the CDTFA purported to seize on a non-existent ambiguity in RTC §34011.2's use of the phrase "gross receipts" to materially alter the CTL, to contravene the intent and express language of RTC Code §34011.2(a)(1), and to establish via emergency regulation an entirely new excise tax regime that far exceeds the CDTFA's legal authority or discretion. Dispensing entirely with the *statutory distinction* for excise tax purposes between cannabis and cannabis products, on the one hand (taxable), and cannabis accessories on the other hand (non-taxable), the CDTFA via Regulation 3802 purported to make *everything purchased at a cannabis retail store subject to excise tax*, including items wholly unrelated to cannabis as well as items expressly defined as non-taxable "cannabis accessories." *See* Regulation 3802(a). As the CDTFA purposefully and intentionally expanded the scope and applicability of the statutory excise tax, altered the longstanding statutory provisions for calculating the excise tax, and created an entirely new category of "property" not mentioned in or even remotely suggested in the governing statutes, the CDTFA grossly overstepped, exceeded its authority and its own prior regulations, and therefore Regulation 3802 must be invalidated. *Dyna-Med,* 43 Cal. 3d at 1389.

90. Incredibly, Respondents did not stop there. Not content with eliminating the statutory exclusion for cannabis accessories *maintained and reaffirmed* in both the HSC and RTC §§34011 and 34011.2, and realizing any interpretation imposing excise tax on *everything and anything sold* would summarily be rejected, Respondents purported *via emergency regulation* to invent an entirely new category of property for purposes of assessing the cannabis excise tax – "Optional tangible personal property." See Regulation 3802(b). The apparent purpose was to ensure cannabis accessories *would be*

[3] On no notice and in violation of the APA and statutory emergency rulemaking procedures, Respondents retroactively rescinded the interpretations contained in Regulation 3700(i). HNHPC is informed and believes the CDTFA also is now undertaking similarly improper efforts to amend Regulation 3800(b) because it too is fatal to its newly-contrived "interpretation" of the cannabis excise tax provisions.

subject to excise tax, without saying so directly. Stated differently, Respondents "butchered" the clear and unambiguous intent *and* language of the CTL (as enacted by Prop 64 and subsequently amended) to try to render illegal HNHPC's and Catalyst's *righteous* conduct and to *expand* the cannabis excise tax far beyond their legal authority or the governing statutes and to effective subject non-taxable items to cannabis excise taxation.

91. After Regulation 3802 was submitted to the OAL for review and approval, the Catalyst Written Response was submitted to the OAL on behalf of Catalyst/HNHPC explaining the deficiencies and improprieties of that regulation and urging the OAL to disapprove it. The OAL improperly rejected and/or disregarded the matters raised in the OAL Letter, as well as numerous public comments submitted to the OAL by the general public (including HNHPC/Catalyst). In the OAL Letter, HNHPC addressed in detail the invalidity and impropriety of the CDTFA's claim it was required to promulgate Regulation 3802 because the enactment of RTC §34011.2 changed the manner in which excise tax was assessed and/or calculated. HNHPC refuted that contention by noting "gross receipts" had been part of the governing law since the passage of Prop 64, and the statutory treatment remained unchanged even after the passage of SB-94, AB-194, and enactment of RTC §34011.2 – and thus, contrary to the CDTFA's claims, there was no change in the governing law that would call into question the *uniformly accepted* premise that cannabis accessories were *not* subject to excise tax so long as they were separately stated from taxable cannabis and cannabis products. Simply stated, the CDTFA *invented* a non-existent emergency to try to address, via a new "interpretive" regulation, an imaginary change in the law.

92. As noted above, the *only* changes of significance here via SB-94 and AB-195 were the transfer of remittance point duties from the retailer to the distributor (SB-94) and then later transfer *back* of those duties to the retailer. At all times, cannabis accessories, if segregated and separately stated, were *not subject to cannabis excise tax*, and any claim to the contrary is false, contrived, and made in bad faith.

93. To add insult to injury, in its campaign to materially alter the CTL, CDTFA simply refuses to conduct any legal analysis to substantiate its "interpretation" of RTC §34011.2(a)(1). That is, the Notice is entirely devoid of any analysis or meaningful discussion of: (i) the framework of the CTL and its own prior interpretations, (ii) the relevant statutory language, (iii) any of the defined terms of the CTL

that are used in RTC §34011.2(a)(1); (iv) any informative regulations or court decisions; or even (iv) the taxability of "cannabis accessories". Nevertheless, the CDTFA saw fit to promulgate the provisions of Regulation 3802 that subjects tangible personal property to the cannabis excise tax, except for "reasonable amounts charged" for" "optional tangible personal property" with no explanation at all.

94. Because the CDTFA failed, in spectacular fashion, to even feign a legitimate attempt at interpreting the statutory provisions of the CTL, the provisions of Regulation 3802 can only be classified as "arbitrary, capricious [and without] reasonable or rational basis." Moreover, Regulation 3802 not only upends the uniform historical application of the CTL, it goes so far as to suggest the plain reading of RTC §34011.2(a)(1) imposes cannabis excise tax on everything except for "reasonable amounts charged" for "optional tangible personal property," even though such terms are entirely foreign to both the CTL and the RTC. For that reason, Regulation 3802 impermissibly alters and amends the CTL and unjustifiably enlarges the scope of the statute it seeks to clarify without legislative authority. It is therefore the court's "obligation to strike down" Regulation 3802 in its entirety. See *Morris v. Williams* (1967) 67 Cal.2d 733, 748 ("Administrative regulations that alter or amend the statute or enlarge or impair its scope are void and courts not only may, but it is their obligation to strike down such regulations").

Regulation 3802 Fails to Satisfy the Legal Requirements of Government Code Section 11349.1

95. In addition to being founded on a non-existent emergency and a knowingly false claim of a change to the excise tax law under RTC §34011.2, Regulation 3800 also must be struck down because Respondents failed to establish, and cannot establish, compliance with the six regulatory standards set forth in GC §11349. Specifically, with respect to emergency regulations adopted pursuant to GC §11346.1(b), such as here, GC §11349.6(b) states the "[OAL] *shall* disapprove the emergency regulation if it determines the agency fails to meet the standards set forth in [GC §11349.1.]" Although the language of GC §11349.1(a) directs the OAL to review the regulation for compliance with the six substantive standards, courts have held that such language "does not defeat the authority of the superior court to review regulations promulgated by an agency for compliance with those requirements." *Sims*, 216 Cal. App. 4th at 1080–81. As such, a court "may declare [a regulation] to be invalid" if it determines the regulation "fails to meet the standards set forth in §11349.1."

Regulation 3802 Fails the Clarity Standard

96. GC §11349.1(a)(3) requires regulations to comply with the "clarity" standard, which means it is "written or displayed so that the meaning of the regulations will be easily understood by those persons directly affected by them." Gov. Code §11349.1(c). In determining whether a regulation meets this standard, a court may rely on provisions of OAL's regulatory guidelines set forth in Cal. Code Regs., tit 1, §16, which in relevant part that "[a] regulation shall be presumed not to comply with the 'clarity' [requirement of Government Code §11349.1]" if, among other things:

(1) the regulation can, on its face, be reasonably and logically interpreted to have more than one meaning; or

(2) the language of the regulation conflicts with the agency's description of the effect of the regulation; or

(3) the regulation uses terms which do not have meanings generally familiar to those "directly affected" by the regulation, and those terms are defined neither in the regulation nor in the governing statute. *Sims v. Dep't of Corr. & Rehab*. (2016) 216 Cal. App. 4th 1059, 1080.

97. First and foremost, Regulation 3802 is riddled with "terms which do not have meanings generally familiar to those 'directly affected' by the regulation, and those terms are defined neither in the regulation nor in the governing statute." One such term is "tangible personal property," which is a term neither defined in Regulation 3802 nor mentioned in the CTL. In addition, the term "tangible personal property" has different meanings across different California statutes, including the Business and Professions Code, the Sales and Use Tax Law, and the Probate Code[4]. Since the term "tangible personal property" has multiple statutory meanings, and since the term is not defined in Regulation 3802 or in the CTL, Regulation 3802 fails to comply with "clarity" standard under GC §11349.1.

98. In addition, Regulation 3802(a) states "'gross receipts' from the retail sale of cannabis or cannabis products does not include a reasonable amount charged for optional tangible property."

[4] *See Business and Professions Code §21627; Probate Code §6132(h); RTC §6016 (under the Sales and Use Tax).*

However, the term "reasonable amounts charged" is not defined in Regulation 3802 nor mentioned in the CTL and, by its nature, is inherently subjective and ambiguous. Furthermore, although Regulation 3802(b)(3) was modified (without notice) to establish "factors [the CDTFA] *may consider* in determining whether the amount charged for optional tangible personal property is reasonable," nothing in the provision limits the CDTFA's ability make arbitrary conclusions. Because the term "reasonable charge" is vague, ambiguous, and inherently subjective, and because those "directly affected" would not understand what constitutes a "reasonable amount charged" for purposes of imposing the cannabis excise tax, Regulation 3802 fails to comply with the "clarity" standard under GC §11349.1.

99. Moreover, in the Notice, Regulation 3802(a) and (a)(1) provided that "gross receipts," for purposes of the cannabis excise tax, includes "[s]ervices that are part of the sale of cannabis and cannabis products." However, the phrase "services that are part of the sale of cannabis and cannabis products" is neither defined nor clarified in Regulation 3802, the CTL, or the SUTL and provides no clarity as to when services are subject to the cannabis excise tax. The OAL understood this and worked with the CDTFA to modify Regulation 3802(a)(2) to include an example that would provide 'clarity' to the provisions of Regulation 3802(a)(2) without input from the interested parties. The example added dealt with the charging of a fee charged to the customer to reimburse the retailer for processing a credit card payment for the purchase of cannabis. However, had the CDTFA actually provided notice to interested parties of this modification, the interested parties would have informed the CDTFA that the example does little to clarify the meaning of the phrase since it conflicts 18 CCR §1641 (Credit Sales) and 18 CCR §1643 (Debit Card Charges), which are regulations that govern when credit card and debit card charges are subject to the sales and use tax. Not only does the phrase "services that are part of the sale of cannabis and cannabis products" inherently unclear as it is neither defined nor clarified in Regulation 3802, the CTL, or the SUTL, the *13th hour* modification to Regulation 3802 makes matters worse as it is an example that directly contradicts 18 CCR §1641 (Credit Sales) and 18 CCR §1643 (Debit Card Charges). For that reason, Regulation 3802(a)(2) fails to comply with the "clarity" standard under GC §11349.1.

100. Furthermore, Regulation 3802 fails to satisfy the 'clarity' standards because it uses language in a way that "can, on its face, be reasonably and logically interpreted to have more than one

meaning." For instance, Regulation 3802(a) provides that "gross receipts," for purposes of the cannabis excise tax, include "tangible personal property . . . the purchaser is required to purchase as a condition of the sale of the cannabis or cannabis products". (Emphasis added). The phrase "condition of the sale" is neither defined nor clarified in Regulation 3802 or the CTL and has multiple interpretations. One interpretation is that "condition of the sale" means the retailer will not sell the customer the cannabis or cannabis product unless the customer also purchases the tangible personal property. Alternatively, "condition of the sale" reasonably and logically could mean the customer does not benefit from a discounted price – i.e. "*sale*" – if they fail to satisfy the condition of the sales promotion. Under the former, the customer cannot purchase cannabis and cannabis products without also purchasing the "tangible personal property", while the latter the customer could purchase the cannabis or cannabis product without also purchasing the "tangible personal property," but in that scenario would not benefit from the promotional sale.

101. Because the phrase "condition of the sale" causes Regulation 3802 to "be reasonably and logically interpreted to have more than one meaning," Regulation 3802 fails to comply with the "clarity" standard under GC §11349.1.

102. Finally, "[a] regulation shall be presumed not to comply with the 'clarity' standard" if "the language of the regulation conflicts with the agency's description of the effect of the regulation." In the Notice, the CDTFA claims Regulation 3802 "clarifies the meaning of the phrase 'gross receipts of any retail sale by a cannabis retailer' as used in [RTC §34011.2(a)]." However, the phrase "gross receipts of any retail sale by a cannabis retailer" does not appear in any of the provisions of Regulation 3802. Instead, Regulation 3802 repeatedly uses the phrase "'gross receipts' from the retail sale of cannabis or cannabis product."

103. Although the CDTFA's description of the effect of the regulation was to clarify the meaning of the phrase "gross receipts of any retail sale by a cannabis retailer," the phrase, itself, never appears in Regulation 3802. Moreover, absent the use of the phrase "gross receipts of any retail sale by a cannabis retailer" in the provisions of Regulations 3802, it would be impossible for Regulation 3802 to have the effect of clarifying the meaning of the phrase "gross receipts of any retail sale by a cannabis

retailer" for purposes of RTC §34011.2(a). For that reason, Regulation 3802 fails to comply with the 'clarity' standard because "the language of Regulation 3802 conflicts with the [CDTFA]'s description of the effect of the regulation" as required by GC §11349.1(a)(3).

Regulation 3802 Also Fails the Consistency Standard

104. In order to comply with the APA, GC §11349.1(b) requires that all regulations satisfy the 'consistency' standard set forth in GC §11349.1(a)(1), which is defined as "being in harmony with, and not in conflict with or contradictory to, existing statutes, court decisions, or other provisions of law." GC §11349(d). Here, the provisions of Regulation 3802 provide that "gross receipts," for purposes of the cannabis excise tax, (i) includes "amounts the purchaser is required to pay to purchase the cannabis or cannabis products, regardless of how the amount is denominated or labeled on the invoice, receipt, or other document provided to the purchaser," but excludes (ii) "a reasonable amount charged for optional tangible personal property purchased with cannabis or cannabis products."

105. According to the Notice, the CDTFA promulgated the entirety of Regulation 3802 on the unsupported notion that "[RTC §34011.2(a)] . . . makes the 'gross receipts of any retail sale by a cannabis retailer' the measure of tax." However, the CTL and relevant regulations make clear that the measure of tax, for purposes of the cannabis excise tax, is found in the phrase "gross receipts from the retail sale of the cannabis and cannabis products."

106. As previously discussed, shortly after the enactment of AB-195, the CDTFA promulgated Regulation 3800(d) which provided in relevant part: "[the cannabis excise tax] is 15 percent of the cannabis retailer's gross receipts from the retail sale of the cannabis and cannabis products sold to the purchaser on and after January 1, 2023. (Emphasis added.)

107. In addition, a cursory review of RTC §34011.2 itself reveals it utilizes "gross receipts from the retail sale of cannabis and cannabis products" more frequently than "gross receipts of any retail sale by a cannabis retailer." RTC §34011.2(a)(3) (requiring the CDTFA to estimate the amount

of forgone cultivation revenue by projecting the estimated amount "as a percentage of gross receipts from the retail sale of cannabis and cannabis products by cannabis retailers"); RTC §34011.2(f) ("Gross receipts from the sale of cannabis or cannabis products" for purposes of assessing sales and use taxes).

108. Notably. the provisions of Regulation 3802 itself conspicuously ignore the phrase championed by the CDTFA. Instead – and perhaps ironically – the CDTFA chose to use the phrase "gross receipts from the sale of cannabis or cannabis products."

109. As a matter of construction, the phrases "gross receipts of any retail sale by a cannabis retailer" and "gross receipts from the retail sale of cannabis and cannabis products" are markedly different. On the one hand, "gross receipts of any retail sale by a cannabis retailer" suggests all sales of a cannabis retailer, including non-cannabis tangible property (whether or not "optional") is subject to cannabis excise tax. On the other hand, "gross receipts from the retail sale of cannabis or cannabis product" suggests only sales of "cannabis" and "cannabis product" are subject to cannabis excise tax.

110. Because the plain meaning of the two phrases stand in directly opposition to each other, a determination that "'gross receipts of any retail sale by a cannabis retailer' [is] the measure of tax" immediately calls into question the meaning of the phrase "gross receipts from the retail sale of cannabis and cannabis products" used in the CTL, Regulation 3800, and even Regulation 3802 itself. As such, Regulation 3802 "[lacks] harmony with, and [is in] conflict with [and] contradictory to, existing statutes, court decisions, or other provisions of law," and the court should therefore invalidate Regulation 3802 for failing to satisfy the 'consistency standard' of GC §11349.1(a)(4).

Regulation 3802 Also Fails the Necessity Standard

111. In the record of a rulemaking proceeding, an agency must state the specific purpose of each regulatory provision and explain why the provision is reasonably necessary to accomplish that purpose. The 'necessity' standard set forth in subdivision GC §11349(a) provides:

> "Necessity' means the record of the rulemaking proceeding demonstrates by substantial evidence the need for a regulation to effectuate the purpose of the statute . . . that the regulation implements, interprets, or makes specific, taking into account the totality of the record. For purposes of this standard, evidence includes, but is not limited to, facts, studies, and expert opinions.

112. In order to meet the 'necessity' standard of GC §11349.1, the record of the rulemaking proceeding must include:

> (1) a statement of the specific purpose of each adoption, amendment, or repeal; and
>
> (2) information explaining why each provision of the adopted regulation is required to carry out the described purpose of the provision. Such information shall include, but is not limited to, facts, studies, or expert opinion. When the explanation is based upon policies, conclusions, speculation, or conjecture, the rulemaking record must include, in addition, supporting facts, studies, expert opinion, or other information.

113. Regulation 3802 fails to satisfy the "necessity" standard because the CDTFA relies exclusively on its "policies" and "conclusions" in explaining why the subdivisions (a)(2) and (b)(2) of Regulation 3802 are necessary to carry out the described purpose of the provision.

114. To be sure, the Notice indicates Regulation 3802(a)(2) and (b)(2) are founded entirely on the CDTFA's "determinations" based on the "wording" of RTC §34011.2(a):

> "The [CDTFA] revised [] subdivision (a)(2) to clarify that for purposes of the cannabis excise tax "gross receipts" include any amount the purchaser is required to pay for tangible personal property, including packaging, the purchaser is required to purchase as a condition of the sale of the cannabis or cannabis products. This is because the [CDTFA] determined that those amounts are required to be included in gross receipts based upon the terms of the retail sale and the wording of subdivision (a) of RTC section 34011.2." (Emphasis added).
>
> "[T]he [CDTFA] revised renumbered subdivision (b)(1) of emergency Regulation 3802 so that it now clarifies that for purposes of the cannabis excise tax, "gross receipts" from the retail sale of cannabis or cannabis products does not include a reasonable amount charged for optional tangible personal property. . . [t]his is because the [CDTFA] determined that RTC section 34011.2 does not require charges for optional tangible personal property to be included in the gross receipts from retail sales by cannabis retailers." (Emphasis added).

115. Importantly, the words "tangible property", "optional tangible property", and "reasonable amounts charged" are *nonexistent* in the CTL and are solely the product of the CDTFA's unexplained "determinations". That is, the CDTFA does not even take the time or effort to analyze any other relevant statute or regulation in support of its "determination" and the rulemaking record is

devoid of any facts, studies, expert opinion, or other information to support the CDTFA's "conclusions" in violation of 1 CCR§10(b)(2). As such, the court should invalidate Regulation 3802 for failing to satisfy the 'consistency standard' of GC §11349.1(1).

HNHPC Has Legal Standing to Bring a Mandamus Action

116. There is no plain, speedy or adequate remedy in the ordinary course of law available to HNHPC, it has a substantial and direct beneficial interest in enforcing Respondents' mandatory and/or discretionary duties and/or correcting its abuses of discretion as it has been directly harmed by the offending conduct alleged herein, and HNHPC legally is entitled to performance by the Respondents of such duties and/or to the proper exercise of discretion under the correct legal interpretation of Prop 64, the CTL and the APA. *See* Cal. Civ. Proc. Code §§1085(a), 1086; *Save the Plastic Bag Coalition v. City of Manhattan Beach*, 52 Cal. 4th 155, 165 (2011) ("one who is in fact adversely affected by governmental action should have standing to challenge that action if it is reviewable"); *Braude v. City of Los Angeles*, 226 Cal. App. 3d 83, 87-88 (1990) (beneficial interest is assessed on a "common sense rather than a merely technical approach," and requires only that the petitioner have a "substantial interest" in the outcome of the proceeding).

117. Via this Cause of Action, HNHPC seeks the issuance of a writ of mandate: (1) invalidating the "emergency" amendment to Regulation 3700 and/or compelling the OAL to *disapprove* it; (2) invalidating Emergency Regulation 3802 and/or compelling the OAL to *disapprove* it; (3) prohibiting Respondents from formally implementing or taking any steps to enforce those emergency regulations; (4) invalidating Respondents' promulgation and approval of those emergency regulations as being violative of their respective mandatory ministerial and legal duties to comply with the law and governing legal authorities recited above; (5) compelling Respondents to act in conformity with the governing law and under the correct interpretation of the law, and invalidating all actions that might be considered discretionary on the grounds they were/are legally improper, violative of governing law, and/or were arbitrary, capricious, without rational, factual or legal basis and thus reversible abuses of discretion.

SECOND CAUSE OF ACTION

INJUNCTIVE RELIEF

(AGAINST ALL RESPONDENTS)

118. HNHPC incorporates as though set forth herein in full the allegations contained in Paragraphs 1-117 above.

119. HNHPC seeks a preliminary and permanent injunction (a) compelling Respondents to comply with their mandatory and/or discretionary legal duties vis-à-vis the formulation and promulgation of interpretive regulations relating to cannabis excise taxation; (b) prohibiting them from enforcing or acting in furtherance of the above-mentioned emergency regulations; (c) prohibiting them from imposing or seeking to collect cannabis excise taxes on separately stated cannabis accessories; (d) compelling the OAL to disapprove the challenged emergency regulations; and (e) compelling them to properly interpret and apply Prop 64 and the CTL so as to exclude from cannabis excise taxation separately stated and documented "cannabis accessories" as defined in HSC §11018.2; and (d) prohibiting them from engaging in any effort to amend or rescind Regulation 3700, and specifically 3700(i), whether pursuant to emergency rulemaking or otherwise.

THIRD CAUSE OF ACTION

DECLARATORY RELIEF

(AGAINST ALL RESPONDENTS)

120. HNHPC incorporates as though set forth herein in full the allegations contained in Paragraphs 1-117 above.

121. As noted above, an actual and justiciable controversy exists between HNHPC and Respondents over the validity and enforceability of the December 15, 2023 emergency amendment to Regulation 3700 and of Regulation 3802, as well as over whether "cannabis accessories" as defined in Prop 64 and the CTL legally are subject to the cannabis excise tax. As such, HNHPC seeks the following declaratory judgments from the Court: (a) that the emergency amendments to Regulation 3700, and Regulation 3802, are invalid and of no legal force or effect; (b) Respondent did not substantially comply with the APA and governing emergency rulemaking provisions with respect to the

emergency amendment to Regulation 3700 and emergency Regulation 3802, and thus the OAL legally was required to disapprove them; (c) under Prop 64 and the CTL, separately stated and documented sales of cannabis accessories are not subject to the cannabis excise tax; and (3) the proper interpretation and application of RTC §§34011 and 34011.2 vis-à-vis whether and under what circumstances (if any) cannabis accessories are properly the subject of cannabis excise taxation.

PRAYER FOR RELIEF

WHEREFORE, based on the foregoing, HNHPC prays for the following relief:

1. For the granting of its request for peremptory writ of mandate as set forth above;
2. For the granting of the requested preliminary and permanent injunction requested above;
3. For the declaratory judgments requested above;
4. For the recovery of reasonable fees and costs, to the extent permitted by law; and
5. For such other or different relief as deemed necessary or appropriate by the Court; an

DATED: December 26, 2023

LAW OFFICE OF JEFF AUGUSTINI

By: Jeff Augustini
JEFF AUGUSTINI

Attorneys for HNHPC Inc.

VERIFICATION

State of California, County of Fresno

I have read the foregoing **VERIFIED PETITION FOR WRIT OF MANDAMUS AND COMPLAINT** and know its contents.

I have been authorized by Petitioner and Plaintiff HNHPC, Inc., to make this verification for and on its behalf, and I make this verification for that reason.

I am informed and believe and on that basis allege that the claims, allegations and averments stated in the foregoing document are true based upon the information reasonably available to me.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct.

Executed on December 26, 2023, at Long Beach, California.

Elliot Lewis