



INSTITUT C.D. HOWE INSTITUTE

C.D. Howe Institute Submission - Legalization of Cannabis in Canada

- The most important, and government-articulated, goals associated with the legalization of marijuana are the protection of public health and the minimization of the black market. Minimization of the black market should be the first priority of government at the outset of legalization, as its continued existence will only serve to undermine efforts to control and regulate the substance to the detriment of public health goals.
- As long as a functioning black market exists, the government will not be able to effectively enforce minimum-age requirements and cannot guarantee the product does not contain harmful contaminants or pesticides. All regulations related to distribution and sale of marijuana in Canada need to keep this in mind. Prohibitively high prices or inconvenient access will not serve the best interests of public health and will simply serve to further entrench the black market.

Recommendations

- Ensuring that consumers have access to legal regulated product should be a public health priority. The federal government should be prepared to supply consumer demand in the event that provinces do not have retail and distribution regulations in place by July of next year. If marijuana becomes legal for consumption but consumers do not have access to legal product, it will simply entrench the existing black market.
- The complexity of the market means that federal and provincial governments should not enact excise taxes and instead rely only on ad valorem sales taxes. There are many different strains of marijuana and determining an optimal excise tax rate for each becomes a complicated administrative process.
- To ensure that the black market is effectively minimized, the federal tax rate should not exceed the current GST rate (5 percent). Assuming a pre-tax price of \$7.50 per gram, a 5 percent sales tax results in about 88 percent of the market shifting to legal consumption and \$216 million in federal tax revenues (Figure 1).
- While it should be a priority to restrict youth access to marijuana, policymakers ought to prioritize restricting youth access to the illicit market as well. Setting a prohibitively high

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minimum age will only maintain the black market, as a large portion of consumers would not have access to legal supply.

- The proposed federal minimum age of 18 is compatible with the objective of restricting youth access to marijuana. It also allows provinces to increase the minimum age to be comparable to their current policies surrounding minimum ages of consumption for other controlled recreational substances.

Access to Retail Outlets and Regulated Supply

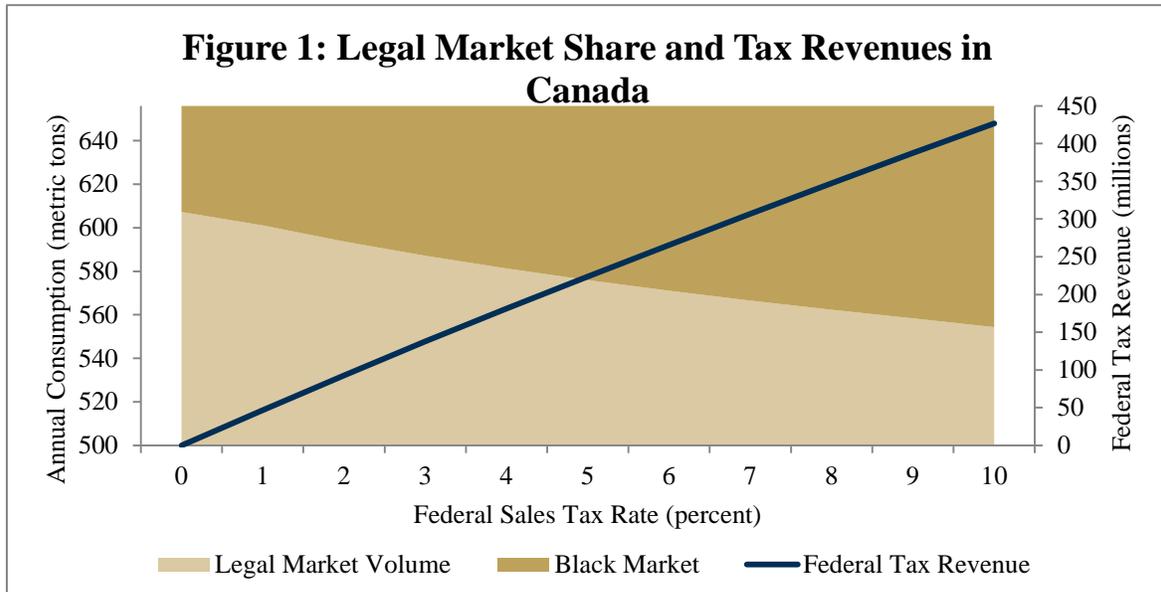
- There can be no doubt that there is a prolific and functional black market supplying market demand for marijuana in Canada.
 - There are more than 75 delivery services and more than 50 dispensary storefronts in the [Toronto area alone](#).
- Ensuring that consumers have access to legal regulated product should be a public health priority.
 - In a sample of products from 9 dispensaries in Toronto tested to the guidelines prescribed by Health Canada, [3 did not pass federal guidelines](#).
 - Following recalls and failed inspections due to the use of prohibited pesticides, Health Canada requires all licensed producers now also [test for the presence of unauthorized pesticides](#).
 - Ensuring that licensed growers supply uncontaminated product is the first step towards protecting cannabis consumers from unrelated negative health effects. To be effective, however, consumers will need safe and convenient access to legal product. This requires functional, regulated distribution networks and retail outlets.
- The federal government should be prepared to supply consumer demand in the event that provinces do not have retail and distribution regulations in place by July of next year. If marijuana becomes legal for consumption but consumers do not have access to legal product, it will simply entrench the existing black market.
 - Governments should take note of the recent experience in Nevada, where sales of recreational marijuana began on July 1 of this year, with no licensed distributors to ship product from producers to retailers. This logistical problem arose because, for 18 months following legalization, Nevada state law has granted alcohol distributors exclusive rights to licences to distribute recreational marijuana unless “an insufficient number of marijuana distributors will result from this limitation.” Thus far, the state does not have any determination of what would be “sufficient” and [Nevada courts have sided with liquor distributors](#) by granting an injunction that protects their exclusive rights to distribution licences. Meanwhile stores are running short as sales boom and there is no shortage of opportunity for the black market to supply Nevada consumers with unregulated, potentially contaminated, product.



- The provinces should be encouraged to leverage the existing retail outlets by allowing for retail of marijuana through licensed establishments. Provinces can effectively enforce regulations through the revocation of licenses and imposition of fines if retail outlets fail to meet regulatory standards, similar to establishments licensed to sell alcohol or retail outlets authorized to sell cigarettes.
- The cognitive impairment associated with cannabis consumption may be [greatly increased when consumed along with alcohol or other drugs](#). To discourage co-consumption of alcohol and marijuana, establishments licensed to sell one substance should not be licensed to sell the other.

Prices, Taxes and the Market

- Despite some claims that the legal marijuana market could [exceed \\$20 billion](#), applying [results from Colorado](#) to Canada yields an estimate of roughly 637 to 763 tonnes, which is in line with Parliamentary Budget Office (PBO) estimates of a market size of about 655 tonnes. Employing a per-gram price range of \$7.50-\$8.50 (consistent with PBO estimates) implies [a \\$4.7 billion to \\$6.5 billion retail market](#), including both legal and illegal suppliers.
- If the government taxes marijuana heavily, it will ensure the continuation of the black market and undermine its efforts to control the substance (Figure 1). A newly accessible legal supply at a low price—made possible in part by low taxes—will result in a decrease of the black market and has the public health benefit on encouraging more consumers to use regulated product.



Note: Calculations assume a pre-tax price of \$7.50 per gram for legal marijuana and current provincial sales tax rates.

Source: Parliamentary Budget Office, author's calculations

- Estimates of prices in the black market range from \$7.60 to \$8.64 per gram (Parliamentary Budget Office, 2016 and Boucher et al. 2013). Meanwhile, the pre-tax price of marijuana from licensed medical producers is expected to be in the range of \$6.67 to \$8.33 per gram (before factoring in added costs associated with additional pesticide screening now mandated by Health Canada).
- The complexity of the market means that federal and provincial governments should not enact excise taxes and instead rely only on ad valorem sales taxes. There are many different strains of marijuana and determining an optimal excise tax rate for each becomes a complicated administrative process.
- To ensure that the black market is effectively minimized, the federal tax rate should not be in excess of the current GST rate (5 percent). Assuming a pre-tax price of \$7.50 per gram, a 5 percent sales tax results in about 88 percent of the market shifting to legal consumption and \$216 million in federal tax revenues (Figure 1). A tax rate of 10 percent results in only 84.5 percent of the market being regulated. Put another way, the increase in sales tax from 5 to 10 percent would shift about \$162 million to the black market and decrease provincial tax revenues by \$14 million while only gaining an additional \$203 million in federal tax revenues.
 - If provinces enact marijuana-specific retail taxes, both federal revenues and the legal share of the market would decrease relative to the above estimates.
 - Given that provinces will likely incur significant costs in transitioning to a legal and regulated market for recreational marijuana, the federal government should not tax marijuana heavily, effectively ensuring adequate fiscal room for provinces to raise their own revenues to offset their costs.

Health and Consumption

Minimum Age

- The minimum age for consumption should be set to encourage the maximum amount of consumers to use legal supply.
 - Over a third (36.4 percent) of consumption in Canada is projected to come from people in the 15-24 age group. In 2014-2015, 33 percent of grade 12 students reported using cannabis at least once in the last year.¹

¹ 2014-2015 Canadian Student Tobacco, Alcohol and Drugs Survey (CSTADS)

- If the legal age were set at 25, it would be putting these consumers at risk of interacting with the black market and potentially receiving product containing contaminants making their consumption more detrimental than it otherwise would have been.
- While it should be a priority to restrict youth access to marijuana, this includes restricting access to the illicit market as well. Setting a prohibitively high minimum age will only maintain the black market, as a large portion of consumers would not have access to legal supply.

Where Cannabis can be Consumed

- The consumption of cannabis causes cognitive impairment and, if consumed in public, may have negative impacts on others. As such, laws that limit the public consumption of cannabis should be considered. These can be modelled after those for other intoxicating or harmful legal products like alcohol and tobacco.
- The cognitive impairment associated with cannabis consumption may be [greatly increased when consumed along with alcohol or other drugs](#). To discourage co-consumption of alcohol and marijuana, establishments licensed to sell one substance should not be licensed to sell the other.
 - There is the possibility to license establishments to allow public consumption of cannabis; however these same establishments should not allow consumption of alcohol. This would be similar to policy in the Netherlands where “Coffee Shops” may sell marijuana and allow consumption on the premises. Alcohol cannot be sold or consumed in “Coffee Shops.” Conversely, marijuana cannot be sold or consumed in any establishment that sells alcohol.

Rosalie Wyonch
Policy Analyst
C.D. Howe Institute
Phone: 416-855-0388
Fax: 416-865-1866
Email: rwyonch@cdhowe.org