

Opportunities and Risks Arising from the Legalization of Recreational Cannabis

October 17, 2017

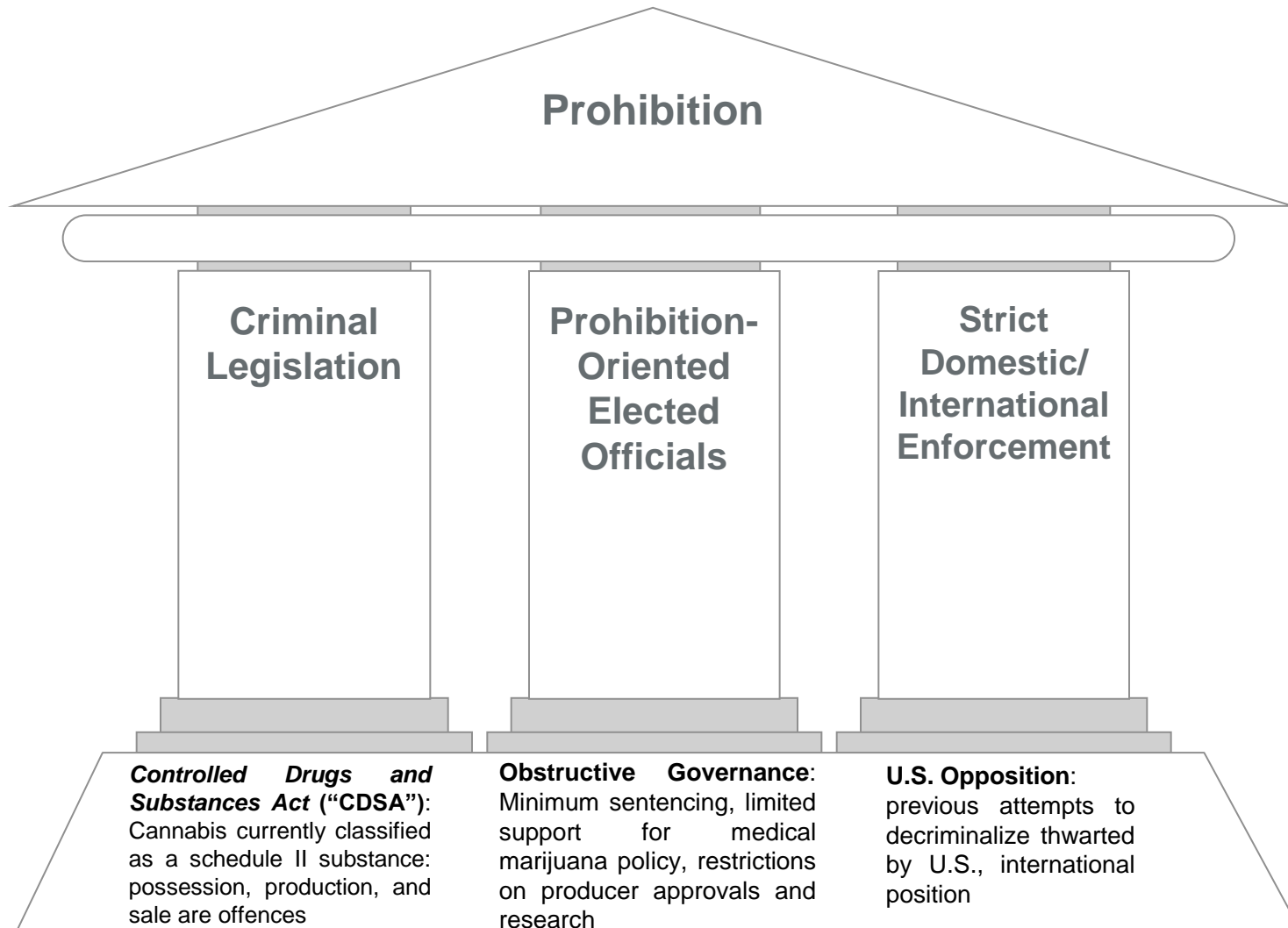


The Canadian Cannabis Market

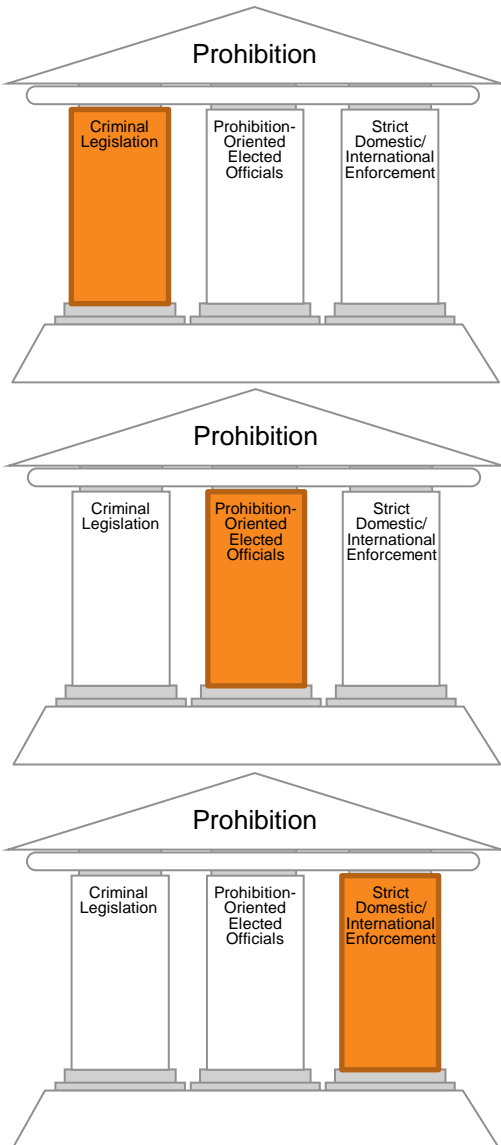
Greg Turnbull, QC



The Past: Cannabis Prohibition in Canada



The Present: Disruption of the Prohibitionist Approach



Key Disruptive Trends

- **Charter Challenges:** as early as 2000, appellate courts have consistently found medical users have a right of access to a safe supply of cannabis
- *Marihuana For Medical Purposes Regulations* (“MMPR”): Due to the unconstitutionality of previous regulations, the Federal Government introduced the MMPR regime under the CDSA; this has enabled large-scale commercial production of marijuana for medical consumption
- **Electoral Change:** On October 19, 2015, campaigning on a platform openly calling for cannabis legalization, the Liberal Party of Canada defeated the incumbent Conservative Party—under Conservative Leadership despite receiving over 1,400 applications for an MMPR production license, only 27 licensed producers had been approved
- **Rising Enforcement Costs:** Statistics from B.C. indicate 47% of all possession incidents are resolved without criminal charges and in 2013, the Canadian Association of Chiefs of Police urged the Minister of Justice to amend the CDSA to provide authority to issue tickets rather than enforce possession laws
- **U.S. “Legalization”:** Over 50% of the U.S. population now supports legalization and Colorado, California, Nevada, Massachusetts, Washington State, Alaska, Oregon, and Washington, D.C. have, or are planning to enact some form of legalization of recreational marijuana while 21 states have legalized cannabis for medical purposes.

New Market Opportunities

The Future: Shift Towards Cannabis Legalization

New Policy Objectives

- Prevent access by young persons
- Reduce burden of enforcement and prosecution for minor possession offences
- Deny a revenue stream for organized crime
- Increase tax revenue
- Align policy and associated costs with actual harms^[1]

Liberal Cannabis Policy Shift

```
graph LR; A[Liberal Cannabis Policy Shift] --> B[Legalize]; A --> C[Decriminalize]; B --> D[Outcome: Legalization refers to the abolition of laws prohibiting possession and personal use of marijuana and allows the government to regulate and tax its use and sale]; C --> E[Outcome: Decriminalization refers to the loosening of criminal penalties imposed for personal marijuana use even though the manufacturing and sale of the substance remain illegal];
```

Policy Preference

Legalize

Outcome:
Legalization refers to the abolition of laws prohibiting possession and personal use of marijuana and allows the government to regulate and tax its use and sale

Decriminalize

Outcome:
Decriminalization refers to the loosening of criminal penalties imposed for personal marijuana use even though the manufacturing and sale of the substance remain illegal

^[1] Liberal Party of Canada, "Marijuana", 2015 Electoral Platform, online: <<https://www.liberal.ca/realchange/marijuana/>>.

Current Legal Framework









Legal Standing of Current Cannabis Suppliers

The *Access to Cannabis for Medical Purposes Regulations* came into effect and replaced the MMPR as of August 24, 2016.

Current Players		Legal Standing	Enforcement Stance
<div>Legal, Heavily Regulated</div> <div>Illegal, unregulated</div>	ACMPR Licensed Producers (Medical Marijuana)	<ul style="list-style-type: none"> Legal: permitted to cultivate, possess, and sell to customers with appropriate medical documentation 	<ul style="list-style-type: none"> Work in tandem with authorities: producers work with police, medical licensing authorities, and Health Canada
	Personal Use Growers	<ul style="list-style-type: none"> Illegal: cultivation, sale, and possession remain illegal under the <i>Controlled Drugs and Substances Act</i> ("CDSA") 	<ul style="list-style-type: none"> Low police enforcement priority: recreational users more likely to receive caution rather than to be charged by police
	Dispensaries/ Cannabis Clubs	<ul style="list-style-type: none"> Illegal: cultivation, sale, and possession remain illegal under the CDSA 	<ul style="list-style-type: none"> Low police enforcement priority: inconsistent enforcement, but raids do occur where there are sales to minors or ties to other crimes
	Organized Criminal Enterprises	<ul style="list-style-type: none"> Illegal: cultivation, sale, and possession remain illegal under the CDSA 	<ul style="list-style-type: none"> Highest police enforcement priority: police have diverted majority of enforcement efforts to criminal enterprises

Current Medical Marijuana Market

Sizing The Medical Marijuana Market

Licensed Producers		Publicly Traded		Retail Market Size	
<ul style="list-style-type: none"> There are currently 67 licensed producers of marijuana 38 of these licensed producers are based in Ontario 4 of these licensed producers are based in Alberta 		<ul style="list-style-type: none"> 23 of these licensed producers are publicly listed companies Market capitalization exceeds \$6.5 billion 		<ul style="list-style-type: none"> The value of the Canadian medical marijuana market is expected to be \$1.3 billion by 2024 (status quo)^[2] 	
 ORGANIGRAM TSXV:OGI	 mettrum TSXV:MT	 EMERALD HEALTH BOTANICALS TSXV:EMH	 CANOPY TSXV:CGC	 Aphria TXV:APH	 AURORA CSE:ACB
Private Alberta Licensed Producers or Applicants					
 SUNDIAL GROWERS	 51st				

^[2] Marijuana for Medical Purposes Regulations, SOR/2013-119 Canada, "Regulatory Impact Analysis Statement", online: <<http://gazette.gc.ca/rp-pr/p1/2012/2012-12-15/html/reg4-eng.html>>.

The Current Medical Marijuana Model

Regulation of the Retail Value Chain

Health Canada conditional "Ready to Build Letter" allows LP to seek financing

Inputs/Start-up Requirements	Production	Marketing/Sales	Channels/Distribution	Service
<p>Pre-License Inspection Health Canada must confirm no risks to public health, safety, and security</p> <p>Storage/Security Health Canada imposes storage/security requirements</p> <p>Sanitation LPs must maintain a sanitation program with a designated QA person</p> <p>Personnel Checks Security Clearances must be obtained for certain key employees</p> <p>Seeds and Inventory MMPR allows an LP to purchase seeds and dried marijuana from another LP by a written order</p>	<p>Sow/Harvest Record LP must record dates of propagation, seed sowing, and harvest as well as an inventory record of at the end of each quarter</p> <p>Pest Control LPs must operate an integrated pest management program</p> <p>Analytical Testing LPs must test for contaminants and percentages of <i>delta-9-tetrahydrocannabinol</i> and <i>cannabidiol</i></p> <p>Packaging/Labelling Strict lot ID, branding, child proofing, expiry, and sanitation requirements</p>	<p>Client Identification LP must only sell to persons ordinarily resident in Canada and must gather name and address information</p> <p>Client Documentation LP must obtain the original prescribing medical document as well as a client statement</p> <p>Verification Required LP must verify the medical document and the prescribing practitioner</p> <p>Registration Required Client to be registered and verification of registration by LP sent with a unique client identifier</p>	<p>Order Required LP must receive a written, or a recorded verbal order with the unique client identifier</p> <p>Payment System Online orders typically fulfilled through Credit Card, Bill e-Payment, money order, or cheque</p> <p>Shipping Physical transfer of possession can only occur by shipping</p> <p>Accompanying Documents LP must include a Health Canada document and client-specific info document with each order</p>	<p>Product Monitoring Appointed QA person responsible to receive client complaints</p> <p>Recall System Capability to recall any lot of marijuana and report all recalls and any adverse product reactions to Health Canada</p> <p>Client Validity LP must monitor validity of client registration and is required to refuse orders in certain circumstances</p> <p>Requests for Client Information Upon demand to Health Canada and Police authorities</p>

Continuous Requirements

Record Keeping / Record Retention

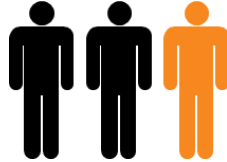
Ministry Spot Checks / Requests for Information

MMPR Good Production Practices

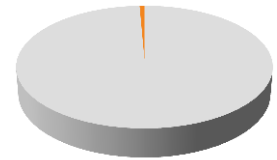
Sizing The Potential Recreational Marijuana Market in Canada

Significant Growth Potential – acknowledge pressures on Health Canada

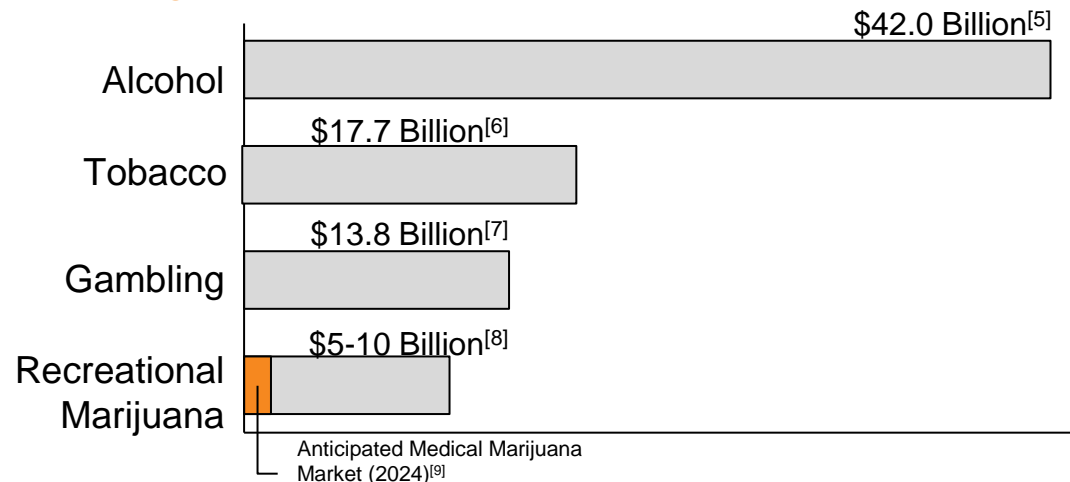
Following legalization, an estimated 1 in 3 Canadians over the age of 18 will be a consumer^[3]



Of the estimated 8 million Canadians who purchased marijuana in 2015, only 55,180 did so legally through a licensed producer^[4]



Estimating the Size of Recreational Marijuana Market



^[3] Ashley Csanady, "As many as seven million possible customers for legal weed in Canada as support hits new heights: Poll", *National Post* (9 November 2015), online: <http://news.nationalpost.com/news/canada/as-many-as-seven-million-possible-customers-for-legal-weed-in-canada-as-support-hits-new-heights-poll>.

^[4] Pete Evans, "20% of Canadians smoked pot last year, but more than 30% would if legal, poll suggests", *CBC News* (10 November 2015), online: <http://www.cbc.ca/news/business/marijuana-pot-poll-survey-1.3312151>.

^[5] Agriculture and Agri-Food Canada, "Consumer Trends: Wine, Beer and Spirits in Canada", *Agriculture and Agri-Food Canada Market Indicator Report* (September 2013), online: <http://www5.agr.gc.ca/resources/prod/Internet-Internet/MISB-DGSIM/ATS-SEA/PDF/6476-eng.pdf>.

^[6] MarketLine, "Tobacco in Canada", *MarketLine Industry Profile* (September 2015).

^[7] Katherine Marshall, "Gambling 2011" *Statistics Canada* (September 23, 2011), online: <http://www.statcan.gc.ca/pub/75-001-x/2011004/article/11551-eng.pdf>.

^[8] Bruce Cheadle, "Legal pot taxes could add \$5B a year to government coffers, CIBC says", *CBC News* (28 January 2016), online: <http://www.cbc.ca/news/politics/pot-revenue-government-5-billion-1.3423705>.

^[9] *Marihuana for Medical Purposes Regulations*, SOR/2013-119 Canada, "Regulatory Impact Analysis Statement", online: <http://gazette.gc.ca/rp-pr/p1/2012/2012-12-15/html/reg4-eng.html>.

The Government of Canada is building a world class cannabis industry.

- Canada's target is to provide regulated and restricted access to cannabis no later than July 2018.
- If successful, Canada will become only the second nation in the world to legalize both medical and recreational marijuana. (Uruguay was the first)
- Forecast total demand for marijuana will be approximately 800,000 kilograms (kg) in 2018. This equates to a market value of approximately \$6.0 billion. To satisfy this requirement, a whole new industry is being built from the ground up.
- Canada is not the only country with a more liberal view toward marijuana.
- A growing number of countries – Germany, Australia, Switzerland, Netherlands, Italy, Denmark, South Africa - are not prosecuting individual cannabis users, and many jurisdictions have made publicly reported statements suggesting a move toward legalized cannabis for medical purposes or the decriminalization of marijuana in some capacity.

Supply/Demand

- Forecast total demand for medical and recreational marijuana to be approximately 800,000 kg in 2018. Despite an aggressive build-out, analysts forecast that licensed producers will exit 2017 with marijuana production capacity of just over 100,000 kg/year, which will not nearly be enough to fulfill near-term demand. No supply/demand equilibrium until late 2020.
- More than \$1 billion has been raised in the cannabis industry since January 2014, and the majority of these funds have been directed at expanding existing facilities or building new ones. The production shortfall will result in product shortages and retail price volatility. As a result, I believe the illicit market will continue to be the principal source of supply for the majority of recreational users for the foreseeable future.

Bill C-45

Proposed Cannabis Act

- The proposed *Cannabis Act* provides a strict legal framework to control the production, distribution, sale, and possession of marijuana across Canada.

The objectives of the *Cannabis Act* are to prevent young people from obtaining cannabis and to reduce criminal activity by imposing serious penalties for those operating outside the legal framework. The legislation takes into account many of the recommendations from the Task Force on Cannabis Legalization and Regulation report, “A Framework for the Legalization and Regulation of Cannabis in Canada,” which was released in December 2016.

- First Reading – April 13, 2017
 - Second Reading – June 8, 2017
 - Committee Review
 - Committee Reporting the Bill with Amendments – October 5, 2017
-
- Fundamental Change – Item 1 of Schedule II of the Controlled Drugs and Substances Act will be repealed.

Bill C-45 – continued

Proposed Cannabis Act

- The Minister of Justice can authorize the possession, production, distribution, sale, importation, and exportation of cannabis, and can suspend, amend, or revoke those authorizations when warranted.
- Holders of existing licences relating to medical marijuana under the Access to Cannabis for Medical Purposes Regulations (ACMPR) will automatically be licensed under the Cannabis Act with respect to both medical and nonmedical activities.
- Separate access to cannabis for medical purposes is maintained, including a provision that import and export licences and permits will only be issued in respect of cannabis for medical or scientific purposes.
- Provinces and territories will be responsible for distribution and retail sales.
- In provinces that have not established a regulated retail framework, individuals will be able to purchase cannabis online from a federally licensed producer with secure home delivery through the mail or by courier.
- Legal sales of marijuana will be restricted to people 18 years of age and over; however, provincial governments have the discretion to increase the minimum legal age.

Bill C-45 – continued

Proposed Cannabis Act

- Adults will be legally able to possess up to 30 g of legal cannabis in public and will be allowed grow up to four plants per household at a maximum height of one metre from a legal seed or seedling.
- There will be restrictions on promoting, packaging, and labeling cannabis and cannabis accessories, similar to the restrictions applicable to tobacco products under the Tobacco Act.
- Until the new law comes into force, cannabis will remain illegal everywhere in Canada, except for medical purposes.
- The Act will create new cannabis-related offences targeting individuals who distribute or sell cannabis to Canadian youth. These new proposed offences carry a maximum penalty of 14 years' imprisonment.

Bill C-46

An Act to amend the Criminal Code (offences relating to conveyances) and to make consequential amendments to the other Acts – published April 13, 2017

The Criminal Code will be amended to modernize and simplify the transportation provisions, strengthen the criminal law responses to impaired driving, and facilitate the effective and efficient investigation and prosecution of drug and alcohol-impaired driving.

Taxation

- The federal government is pushing the provinces to commit to low taxes on recreational marijuana.
- One large omission from the proposed *Cannabis Act* is how the federal and provincial governments will tax recreational marijuana and how that tax revenue will be shared. In June 2017, Federal Finance Minister Bill Morneau met with his provincial counterparts.
- One of the key topics of discussion was how to tax a regulated market for cannabis. During the two-day gathering, Mr. Morneau was pushing for a low-tax commitment from his provincial counterparts, highlighting the need for a coordinated approach to marijuana taxation.
- In a statement, he said, “We need to get it right, and we need to do it together. Our twin goals are to keep cannabis out of the hands of youth and keep profits out of the hands of criminals. This will mean keeping taxes low and working together on an ongoing basis to ensure a coordinated approach.”

Retail Distribution

Though the provinces will be responsible for retail distribution of marijuana once it is legalized, it is not clear whether they will be ready to fulfill that role. All provincial governments are studying what the best retail model will be for their jurisdictions.

Ontario

Announced framework on September 8, 2017 - government will control all aspects of retail cannabis distribution, including online distribution.

Industry proponents that have been leading the fight to get recreational marijuana legalized have been totally excluded from the retail distribution channel.

Expect to have 40 stores ready for next summer.

Retail Distribution

Alberta

- Announced retail framework on October 9, 2017, new consultation until October 27, 2017
- Split: either new government stores or private retail model
- Put policies into place before July 2018
- Goals
 1. Keep cannabis out of the hands of children
 2. Protect public health
 3. Promoting safety on roads, in workplaces and in public spaces
 4. Limiting the illegal market for cannabis
- Alberta will directly manage wholesale and distribution (like alcohol)
- Cannabis standalone stores – no alcohol, tobacco or pharmaceuticals
- Over 18 years
- Possess up to 30 grams of legally produced cannabis in public
- Consume at home and in public spaces where smoking is allowed
- Grow at home indoors – 4 plants, maximum height of 100cm

Impact of Municipal Laws

- Business licenses and by-laws for locations

Licensing & Alberta's Cannabis Landscape

Jason Kujath, J.D., M.B.A.





FIFTY FIRST **PARALLEL**

- **Applicant to become a Licensed Producer**
 - Submitted in Nov. 2016
 - Review Stage (Stage 5 of 7)
- **Phase One:** 75,000 sq. ft. facility in Lethbridge, AB
 - **Yield:** 4,000 kilograms annually
 - **Cost:** \$12 million capital project
 - **Phase One:** ~50 employees
 - **Proj. Sales Revenue:** \$33mm/23mm EBITDA
- **5 to 7 Retail Stores:** 70% of product from Lethbridge

Licensing Procedure: (18 – 24 months)

1. Business Plan
2. *ACMPR* - Due Diligence
3. Site Identification
4. Hire Quality Assurance Person (QAP)
5. Application Drafting & Submission
 - ↪ Security Clearance
 - ↪ Finance/Build
 - ↪ License to Produce
 - ↪ Inspection/Testing
 - ↪ License to Sell

Licensing Requirements (ACMPR):

1. Permission to Use Land/Site Plan/Floor Plan

2. QA Person (Consultant)

- Experience in HACCP
- 5 Years of Food Production - QA Experience

3. Detailed Record Keeping Proc.

- Div 5 of Regs.
- Enterprise Resource Planning (ERP) Software
(Ample Organics/Benchmark/Biotrack THC)

Licensing Requirements (*ACMPR*)

4. Detailed Security Plan

- Sub. C of Regs.
 - Security Master Plan: *David Hyde & Associates*
 - Directive for Physical Sec. Requirements

5. Quality Assurance Practices (*QAP*)

6. Good Production Practices

- Sub. D of Regs.

7. Packaging, Labelling & Shipping

- Sub. F of Regs.

Applying to Produce/Sell Today

Today:

- ↪ Two Types of Licenses (ACMPR):
 - ↪ (1) License to produce; and
 - ↪ (2) License to Sell

What is Coming?

- ↪ *The Cannabis Act*: Multiple Classes of Licenses
 - ↪ *Licenses set out by Regulations to the Cannabis Act*
 - ↪ To be released – Late 2017

Provincial Retail & Distribution Legislation:

- ↪ Winter 2018

The Cannabis Act: License Classes

– Federal licenses:

1. License to Produce (Medical/Recreational)

– Wholesale Production License

– Paths for sale:

1. *Recreational market; or*
2. *Medical market (Medical sale license required)*

2. License to Refine

– *Extract/Concentrate License*

3. License to Sell (Medical)

– Benefit: Direct to Consumer by Mail Order

Provincial Distribution & Retail

- **Private or public retail:** Stand-alone store fronts
 - ***Public consultation: Due by Oct 27, 2017***
- **Regulatory oversight by AGLC (Liquor)**
 - Provincial Administration
 - AGLC to Develop and Enforce Admin. Policy
- **Distribution Point:** likely *Connect Logistics*
- **Minimum Age:** 18 years old

Provincial/AGLC Requirements

1. Preliminary Assessment
 - a) Property & site layout plans
 - b) proof of ownership and/or,
 - c) an accepted offer/option to purchase/lease the premises, and
 - d) a non-refundable application fee
2. Advertising of Application (21 Days)
3. Submission of Application and Documentation
4. Final Inspection and Issue of Licence

Considerations for Municipal License

▢ **Retail Licenses Guidance:**

▢ At least 300 m from:

1. Schools*
2. Community centers*
3. Neighbourhood houses*
4. Youth facilities that serve vulnerable youth
5. Other marijuana-related businesses*

▢ Business licence

▢ Development permit

- ▢ Community notification process
- ▢ With a signed good neighbour agreement

Marijuana in the Workplace

Will Cascadden



FEDERAL GOVERNMENT TASK FORCE

“A Framework for the Legalization and Regulation of Cannabis in Canada: The Final Report of the Task Force on Cannabis Legalization and Regulation”

MARIJUANA IN THE WORKPLACE

Task force said that regulators will need to:

- Facilitate and monitor ongoing research on cannabis and impairment, considering implications for occupational health and safety policies.
- Work with existing federal, provincial and territorial bodies to better understand potential occupational health and safety issues related to cannabis impairment.
- Work with provinces, territories, employers and labour representatives to facilitate the development of workplace impairment policies.

MARIJUANA IN THE WORKPLACE

What employers should do:

- Prepare for legalization – employees will use (continue to use) marijuana.
- Modify policies to expressly deal with employee marijuana use (similar to alcohol),
 - no work while under the influence,
 - no possession or use in the workplace,
 - testing and implications of positive test.
- Ensure that all impairing drugs (legal, illegal, prescription) are addressed.
- Communicate policies and train employees and supervisors.

MARIJUANA IN THE WORKPLACE

Issues:

- Employees working in safety-sensitive positions vs. employees not working in such positions.
- Medical prescriptions and accommodation (disclosure required?).
- Employee addiction and dependency.
- Poor performance by employees working in non-safety sensitive positions.
- Is “zero tolerance” acceptable?

GENERAL ISSUES AND PROBLEMS

- Testing.
- Measuring Current Impairment.
- Transition (from now to actual legalization).
- Do people have the “right” to use marijuana?

Questions



This program qualifies for up to 1.5 hours of eligible educational activity or CPD/MCE credit under the mandatory education regimes in British Columbia, Ontario and Québec.

Presenter Contacts

Jason Kujath

51st Parallel Life Sciences Ltd.

Jay@51st.ca | 403-351-1779

Greg Turnbull, QC

Partner, McCarthy Tétrault LLP, Calgary

gturnbull@mccarthy.ca | 403-206-5555

Will Cascadden

Partner, McCarthy Tétrault LLP, Calgary

wcascadden@mccarthy.ca | 403-260-3521

Selected Bibliography

Agriculture and Agri-Food Canada, "Consumer Trends: Wine, Beer and Spirits in Canada", *Agriculture and Agri-Food Canada Market Indicator Report* (September 2013), online: <<http://www5.agr.gc.ca/resources/prod/Internet-Internet/MISB-DGSIM/ATS-SEA/PDF/6476-eng.pdf>>.

Ashley Csanady, "As many as seven million possible customers for legal weed in Canada as support hits new heights: Poll", *National Post* (9 November 2015), online: <<http://news.nationalpost.com/news/canada/as-many-as-seven-million-possible-customers-for-legal-weed-in-canada-as-support-hits-new-heights-poll>>.

Bruce Cheadle, "Legal pot taxes could add \$5B a year to government coffers, CIBC says", *CBC News* (28 January 2016), online: <<http://www.cbc.ca/news/politics/pot-revenue-government-5-billion-1.3423705>>.

Canadian Association of Chiefs of Police, "Resolution #03 – 2013", Resolutions Adopted at the 108th Annual Conference (August 2013), online: <https://www.cacp.ca/resolution.html?asst_id=327>.

Jeffrey M. Jones, "In U.S., 58% Back Legal Marijuana Use", GALLUP (21 October 2015), online: <<http://www.gallup.com/poll/186260/back-legal-marijuana.aspx>>.

Katherine Marshall, "Gambling 2011" *Statistics Canada* (September 23, 2011), online: <<http://www.statcan.gc.ca/pub/75-001-x/2011004/article/11551-eng.pdf>>.

Marihuana for Medical Purposes Regulations, SOR/2013-119 Canada, "Regulatory Impact Analysis Statement", online: <<http://gazette.gc.ca/rp-pr/p1/2012/2012-12-15/html/reg4-eng.html>>.

Michelle Rotermann and Kellie Langlois, "Prevalence and correlates of marijuana use in Canada, 2012", *Statistics Canada* (15 April 2015), online: <<http://www.statcan.gc.ca/pub/82-003-x/2015004/article/14158-eng.pdf>>.

Pete Evans, "20% of Canadians smoked pot last year, but more than 30% would if legal, poll suggests", *CBC News* (10 November 2015), online: <<http://www.cbc.ca/news/business/marijuana-pot-poll-survey-1.3312151>>.

R. v. Parker (2000), 188 D.L.R. (4th) 385.

Statistics Canada, "Drug-related offences in Canada, 2013", *Statistics Canada* (25 June 2015), online: <<http://www.statcan.gc.ca/pub/85-002-x/2015001/article/14201-eng.htm>>.

Travis Lupick, "Corporations move in on Canada's medicinal cannabis industry", *The Georgia Straight* (18 March 2015), online: <<http://www.straight.com/news/413966/corporations-move-canadas-medicinal-cannabis-industry>>.