Recommendations for Federal Regulation of Legal Cannabis

September 2021

Introduction

The Cannabis Freedom Alliance (CFA) appreciates the opportunity to provide feedback on the Cannabis Administration and Opportunity Act (the CAO Act or Discussion Draft). The Discussion Draft represents a meaningful engagement with achieving our shared goal of ending cannabis prohibition, removing the consequences of criminal prohibition from those adversely affected, and establishing a fair, free, and competitive American cannabis market.

In its "Recommendations for Federal Regulation of Legal Cannabis"[1] earlier this year, the Cannabis Freedom Alliance identified four primary goals for any successful legislation intended to legalize marijuana federally. Such legislation should:

1. Establish a regulatory framework that promotes public safety while allowing innovation, industry, and research to thrive;
2. Ensure individuals previously involved in the illicit market can effectively secure a second chance and contribute to the legal market;
3. Create low barriers to entry and non-restrictive occupational and business licensing so that large companies and new entrepreneurs can compete on a level playing field; and
4. Impose a total tax burden – federal, state, and local combined – that does not incentivize the continuation of gray or black markets and ensures competitive global footing for a vibrant, novel U.S. industry.

We thank the authors for their attention to these issues and have provided comments in response to the Discussion Draft.

About the Cannabis Freedom Alliance

The Cannabis Freedom Alliance (CFA) is a coalition of advocacy and business organizations seeking to end the prohibition and criminalization of cannabis in the United States in a manner consistent with helping all Americans achieve their full potential and limiting the number of barriers that inhibit innovation and entrepreneurship in a free and open market. For more information on the CFA, please contact info@cannabisfreedomalliance.org or visit our website at cannabisfreedomalliance.org.

[1] Cannabis Freedom Alliance. "Recommendations for Federal Regulation of Legal Cannabis." July 2021, https://bit.ly/2WzaMnR.

A Special Thanks to the Members of the CFA Steering Committee for Their Support on this Project!

Comments of the Cannabis Freedom Alliance on the Cannabis Administration and Opportunity Act

CONTROLLED SUBSTANCES ACT CHANGES

In Section 101(a), the CAOA directs the U.S. Attorney General to initiate a regulatory process that removes marijuana and tetrahydrocannabinols (THC) derived from marijuana from Schedule I of the federal Controlled Substances Act within 180 days of passage. This section would accomplish the overarching goal of legalizing the cultivation, manufacture, distribution and possession of marijuana products at the federal level. We applaud this goal and offer the following suggestions to further effectuate it.

1. Ensure cannabis is not later listed under a different schedule of the Controlled Substances Act by adding it to the definitional exclusions of "substances" in technical conforming amendments to the CSA. This change would simultaneously remove barriers to the legal marijuana industry for obtaining financial services, insurance, and other issues that are legally imposed on persons who traffic in Schedule I or Schedule II substances. Such changes would also fully eradicate the need for legislation such as the SAFE Banking Act.
2. Because Congress is performing the Act of descheduling and, consistent with Suggestion 1 above, aiming to ensure cannabis is not later scheduled, to avoid confusion, delay, and any inconsistency in effective dates and their application to prior offenses, we recommend that the Attorney General's role be clarified as purely ministerial—the role of conforming outdated rules to the CAOA. This process can and should be executed quickly after enactment of the CAOA. We believe 180 days is sufficient time but the application of rulemaking processes and APA processes to the Attorney General's work under this provision is legally unnecessary to accomplish its fulfillment and would likely only increase delay.

FEDERAL CANNABIS REGULATION AND COMMERCE

We thank the authors of the Discussion Draft for their unique thoughtfulness on this issue among their colleagues who have introduced similar legislation and the obvious research effort that was incorporated into the draft. We broadly agree with the desire for a safe and effectively regulated cannabis market that provides opportunities for small business and entrepreneurial success.

1. **Agricultural Production**. As written, the Discussion Draft authorizes FDA to regulate raw cannabis, cannabis that has not yet been made into a finished good or delivered at the facility of a producer, but we believe primary USDA oversight

would be more efficient and consistent with the regulatory framework for other crops. Folding raw cannabis into the existing crop management regulatory framework would be efficient and facilitate safe market maturation under an experienced regulator. Moreover, we recommend explicit statutory language designating raw cannabis as a full federal crop so that it is subject to similar rules and protections as other crops.

2. **Home Grow**. Sec. 5902(b)(2)(B) exempts individuals who grow marijuana at their homes for personal consumption from any tax liability for such plants or products. Limitations on this production of cannabis or personal use would be prescribed by rule, but Congress should explicitly clarify that it does not intend to limit such activities in the text of federal statute beyond any state limitations on home cultivation. Many states that have legalized adult-use cannabis already impose some restrictions on home grow. States are constitutionally empowered and best positioned to craft and enforce such regulations. Home cultivation, like home brewing, is a popular hobby in legal jurisdictions and can serve as an initial opportunity for research and development among cultivars (many industry growers have home plants for experimental purposes), future small and minority owned businesses, and help ensure caregiver access in states that allow for medical caregiver cultivation and production among their friends and family.[2]
3. **International imports and exports.** Section 5902 would expressly authorize international trade in marijuana products. Conceivably, this would allow for an open market between nations where marijuana is fully legal for adult use, such as between the United States and Canada. American adult-use cannabis is akin to French wine in terms of consumer understanding of premier quality and value, even on a global scale today; international commerce will benefit the U.S. and global economy. We applaud these provisions and would encourage the authors to establish as formal U.S. policy the objective to remove unreasonable foreign barriers to international cannabis commerce.
4. **Transportation.** Transportation has become a point of contention within the federally legal hemp market[3] and the CAOA wisely sidesteps these complications by making legal transport over federal and state roads explicit.
5. **Consumer Continuity on Current state-legal cannabis products**. The draft CAOA does not clearly make the commerce in existing state-licensed marijuana products legal upon passage. It remains unclear from the text whether a state-licensed marijuana businesses can operate legally under federal law prior

[2] John De Friel & Randal John Meyer, *The Illinois marijuana legalization debate: Who's afraid of a little home grow?*, CHI. TRIB., May 21, 2019, at A7, *available at* https://www.chicagotribune.com/opinion/commentary/ct-perspec-marijuana-legalization-home-grow-pritzker-20190520-story.html.

[3] Stewart, Ian. "Federal Courts Are Split on the Legality of Transporting Hemp and CBD in Interstate Commerce." *Cannabis Business Executive,* February 19, 2019, https://www.cannabisbusinessexecutive.com/2019/02/federal-courts-are-split-on-the-legality-of-transporting-hemp-and-cbd-in-interstate-commerce/.

to the adoption of implementing regulations by the respective federal agencies. This lack of clarity leaves state-licensed marijuana business, financial institutions, and related entities, as well as consumers, in a continued state of uncertainty during the short term even if CAOA were to secure passage. Thus, to minimize disruption to consumers and businesses while respecting states' rights to implement their own regulations, we recommend that the CAOA expressly authorize the interstate trade of cannabis and cannabis products that already exist in the marketplace, including products in cultivation (to the extent not already covered by the CAOA's transition provisions) and production, at the time of enactment of the CAOA, subject to existing state laws. Such pre-passage cannabis and cannabis products should be excluded from the CAOA's other regulatory provisions, with the key exception of the rules prohibiting interstate trade that violates the reasonable laws of any given state. All subsequently cultivated, produced, distributed, and sold cannabis and cannabis products should be subject to the CAOA and any implementing regulations. This recommendation would allow consumers to continue to purchase products that are lawful under state law, and only such laws; enable businesses to deplete rather than abandon their pre-CAOA inventory; give businesses time to comply with the CAOA's new rules; and respect states' authority to regulate cannabis products within their borders (provided no undue burden is imposed on interstate trade). Importantly, this recommendation does not impose an artificial time-based delay on compliance with the CAOA. The fundamental issue to be addressed is ensuring that state-lawful products that are already in the market can continue to be bought and sold, rather than deemed illegal immediately.

6. **Federal Regulation.** Section 102 directs the ATCTTB to enter into a Memorandum of Understanding with the Food and Drug Administration (FDA) to jointly regulate the industry using standards developed by the FDA. One overriding area of concern is the barrier to entry created by the application of FDA GMP facilities requirements to all cannabis producers. These requirements impose substantial costs that many small and medium businesses as well as socially and economically disadvantaged businesses will be unable to afford. Section 1105 clarifies that these regulations would include Good Manufacturing Practices—a standard of cultivation and manufacturing defined by the FDA which vary by industry. Generally, these standards specify certain equipment or practices that are allowable within a farm or manufacturing facility, batch tracking, testing, and other requirements that sometimes can limit the scope of possible innovation because of the approvals necessary. Further, GMP facilities tend to require a level of capital investment that most existing legal marijuana businesses are not prepared to meet. GMP and other requirements the FDA is likely to insist upon would constitute significant barriers to entry for small entrepreneurs – especially current gray- or black-market participants – who may hope to gain a share of the legal cannabis market. Despite some claims by

cannabis businesses, there are currently no GMP-compliant cannabis businesses in the United States because GMP standards have not yet been defined by the FDA for the cannabis industry. Only those firms heavily endowed with capital would be able to transition an existing facility or construct a new facility to meet GMP standards. This distinction is not merely an issue of consumer safety. State regulatory frameworks for adult-use cannabis markets all include extensive provisions to protect consumer safety already, including restrictions on which pesticides and nutrients can be used, detailed logging of this information, batching of products, laboratory testing, and tracking on state-monitored systems such that recalls can be easily facilitated if ever required. FDA regulation of the industry would simply impose additional layers of cost and bureaucracy on existing marijuana businesses that many may not have the financial wherewithal to support. For these reasons, Cannabis Freedom Alliance has recommended that any marijuana product cultivated or manufactured in strict compliance with state regulatory frameworks be deemed acceptable by the FDA and other federal regulators to enter into interstate commerce.

7. **Interstate Commerce v. State Powers**. We support the Discussion Draft's inclusion of the Webb-Kenyon and Wilson Acts, fully in line with recent Supreme Court precedent in *Tennessee Wine and Spirits*, and the requirement that rules governing the promotion, sale, and distribution of cannabis products through e-commerce (and similar, non-in-person channels) be implemented by a specified time.[4] To build upon this excellent framework, we suggest ensuring robust judicial remedies are available under both the Administrative Procedure Act and the Mandamus Act to require the agencies to issue their rules quickly if they miss their deadlines. If rulemaking takes longer than the anticipated timelines, small businesses will suffer the most, as evidenced by the lack of FDA rulemaking in the hemp/CBD space. The Discussion Draft already includes partial remedies but we urge the more comprehensive and efficient remedies that apply to FDA and TTB. APA litigation for undue delay can take years, so the most cost-effective and time-efficient remedy is authorizing relief under the Mandamus Act with a "shall issue" directive to the judicial official upon demonstration of delay past deadlines. This tool will give small businesses access to an efficient judicial remedy in addition to ensuring the agencies create a marketplace consistent with congressional intent in a timely manner. Moreover, the Discussion Draft should expressly provide payment of legal fees to any party that prevails in a mandamus suit, since small businesses are most likely to need this relief.
8. **Business Continuity**. One way to help existing cannabis businesses transition successfully into the federal marketplace is ensuring comity of state licenses and

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[4] Ilya Shapiro & Randal John Meyer, "Congress Needs to Settle the Looming Cannabis-Regulation Fight", NATIONAL REVIEW ONLINE (July 10, 2019, 1:00pm), https://www.nationalreview.com/2019/07/congress-must-settle-the-looming-cannabis-regulationfight/.

grandfathering existing state licenses. A state-licensed cannabis company that engages in the activities for which a permit from the TTB would be required should be entitled to such a permit as a matter of law and be issued upon proof of a valid state-issued license. Such comity will help ensure that such entities (especially wholesalers) are incentivized to compete in interstate commerce, thereby facilitating interstate trade and preventing the continued existence or future creation of oligopolistic markets; minimizing disruption to existing markets; and lowering costs for existing businesses, especially small businesses. Doing so would also respect states' rights to regulate cannabis as they see fit (for instance, a licensee could not distribute cannabis in a state where doing so is illegal). It also would vastly speed up the federal permitting process.

9. **Track and trace.** All state-regulated adult-use marijuana markets require licensees to participate in a state-administered track-and-trace system. These programs typically require a cultivator to attach a unique radio-frequency identification (RFID) tag to every marijuana plant so its whereabouts are monitored and to replace this tag with a new RFID tag every time the harvest is transformed into a new product or package, such as an edible. This information is recorded in a central, state-monitored database that facilitates full tracking of every gram of legal marijuana inventory from the time of planting to the time of ultimate sale to a retail consumer. These platforms simultaneously allow state regulators to run forensic software on the database to search for anomalies that may require investigation. Section 112(b) of the CAOA would create a parallel track-and-trace system at the federal level. While it's conceivable that this system would eventually subsume state track-and-trace efforts, the initial draft of CAOA appears to make these requirements duplicative, at least initially. Cannabis Freedom Alliance has recommended that federal regulators concern themselves primarily with tracking inventory as it moves through interstate commerce and then allow state track-and-trace systems to monitor inventory within a state once the interstate transfer has been completed.
10. **Safe driving.** Section 203 directs the federal Department of Transportation to conduct research into the effect of marijuana consumption on highway driving and to establish impairment standards. Although research has shown per se standards for the presence of THC concentration in a person's bodily fluids are unreliable determinants of intoxication, the CAOA recognizes this limitation in Section 204. In that section, it would allocate federal grants to states for training of law enforcement to become drug recognition experts. This approach is supported by research and has been recommended by Reason Foundation.[5]

[5] Moore, Teri. "Addressing the Problem of Marijuana-Impaired Driving." Reason Foundation policy brief, May 2018, https://reason.org/wp-content/uploads/2018/05/marijuana-impaired-driving.pdf.

TAXES

Section 5901(a) would impose a federal excise tax on any marijuana products produced within or imported into the United States. This rate of this tax would increase rapidly over the first five years of the bill's enactment, rising from 10 percent during the first two years, to 15 percent in year three, 20 percent in year four and 25 percent in year five. Tax authorities would need to determine a "fair market price" of marijuana in instances when those authorities believe a transfer did not occur at the fair market price, according to Section 5902(e). These determinations invite arbitrary and capricious enforcement policy that will likely result in disparities across groups.

Following the fifth year after enactment, the *ad valorem* excise tax would transition to a 25 percent excise tax based on a standardized THC "equivalent amount" within each product, effectively taxing more potent marijuana products at higher rates. This approach is intended to parallel alcohol excise taxes, although THC is not necessarily the only organic molecule of interest in the cannabis plant. Calculating a THC equivalent amount will also insert complexity into the administration and compliance with these excise taxes relative to a simple *ad valorem* calculation. We would urge the sponsors of this bill to continue the *ad valorem* excise tax after the fifth year.

Policymakers should note that numerous excise taxes are already assessed on legal marijuana products by state and local governments. State-level taxes alone range from $340 per pound in Oregon to as much as $2,299 per pound in Illinois. Local governments frequently levy distribution fees, canopy taxes and additional retail excise taxes in addition to these amounts. Any federal excise tax would be in addition to these already substantial levies as the imposition of a federal tax will not automatically reduce or eliminate any of these state or local taxes. The cumulative total could be an effective tax rate higher than the cost of producing and selling marijuana in some locations. This result would make the legal marijuana market uncompetitive with the black-market since they would provide otherwise substantially similar products. Policymakers should expect this cumulative tax burden to make the black market attractive to both consumers and producers in order to avoid high tax rates. Early empirical studies show that marijuana consumers exhibit a propensity to substitute illicit marijuana for legal marijuana as the relative cost of legal marijuana rises.[6]

For these reasons, Cannabis Freedom Alliance has recommended a federal excise tax sufficient to reimburse federal regulators for the cost of monitoring and facilitating interstate transfers only. This rate should be less than one percent of the retail transaction price.

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[6] Lawrence, Geoffrey and Purnell, Spence. "Marijuana Taxation and Black Market Crowd-Out." Reason Foundation policy brief, January 2020, https://reason.org/wp-content/uploads/marijuana-taxation-black-market-crowd-out.pdf.

HEMP

Since passage of the 2018 Agricultural Act, hemp-derived THC has remained in a state of legal uncertainty since the plant can be grown legally and at large scale under a plan approved by the U.S. Department of Agriculture. Regulations promulgated by the USDA subsequently made clear that extracts and preparations of hemp had to be remediated for THC content, although it has been unclear what persons involved in the hemp trade must do with this THC and whether it can be legally transferred from one party to another. A comprehensive cannabis legalization statute would be an opportune time to remove this ambiguity, although the CAOA includes express language to leave it in place.

CRIMINAL JUSTICE REFORM

We applaud the authors' attention to these issues. We offer the following below suggestions and feedback to help further carry out the restorative goals of the CAOA. Additionally, we note that the Discussion Draft's retroactivity provisions do not apply to administrative enforcement, related non-violent criminal activity, or forfeiture actions. If the retroactivity provisions do not apply to these areas, there will be substantial risk of legal liability for employees, consumers, and businesses.

1. The current draft of the bill creates both necessary and unnecessary new federal criminal penalties.
    a. The prohibition and associated criminal penalty of up to one year in federal prison for the sale of more than 10 ounces of cannabis should be removed. [Section 502; proposed 21 U.S.C. 331(fff)(2)]
    b. The prohibition and any associated criminal penalty for the sale of products containing alcohol, caffeine, or nicotine and the sale of flavored cannabis products for use in vaping should be entirely removed. [Section 501-502; proposed 21 U.S.C. 331(fff)(3); §1109]
    c. The following acts currently subject to criminal penalties should be revised to carry a civil fine or maximum tax penalty:
        i. Failure to notify of knowledge that cannabis products are being used in the illicit market. [Section 502; proposed 21 U.S.C. 331(fff)(4)]
        ii. Introduction, delivery, or receipt of misbranded cannabis products. [Section 502; proposed 21 U.S.C. 331(ggg)(1),(3)]
        iii. Misbranding of a cannabis product. [Section 502; proposed 21 U.S.C. 331(ggg)(2)]
        iv. Alteration, destruction, or removal of cannabis product labeling. [Section 502; proposed 21 U.S.C. 331(ggg)(4)]
    d. While a prohibition on the sale of cannabis to those under 21 years old is a reasonable and necessary policy, a medical exception should be established

given that the associated medical benefits of using cannabis are not limited to those over a certain age. [Section 502; proposed 21 U.S.C. 331(fff)(1)]

   e. Section 112(b)(4) creates potential perverse incentives by requiring persons involved in the legal marijuana trade to inform authorities if they suspect any other person involved in the legal cannabis trade has underreported their tax liabilities. This provision effectively conscripts those involved in the industry as informants to tax authorities regarding suspected activities of their competitors, over which they may not have accurate knowledge.

2. We know from recent court cases and agency interpretations of the First Step Act that <u>Congress must be explicitly clear about any changes to federal criminal law and how those changes should be implemented</u> (especially those that alter the sentences of those previously convicted).[7]
   a. The bill should make explicitly clear how agencies and courts are to interpret the descheduling of marijuana in their application to individuals who are currently detained for cannabis charges or convicted of such charges awaiting sentencing. Forcing them to continue in the normal legal process and then later submit a motion for resentencing would be unjust. [Section 311]
   b. The bill should also clarify how courts are to interpret the expungement and resentencing provisions for the following categories of individuals whose only criminal conduct is related to cannabis:
      i. Those who were subject to a §3B1.1 enhancement under the sentencing guidelines for being the organizer, leader, manager, or supervisor of activity involving cannabis ("aggravating role").
      ii. Those who received ancillary federal charges or convictions that require an underlying cannabis offense. [e.g. using, carrying, or possessing a firearm in connection with a federal drug trafficking offense under 18 U.S.C. § 924(c) and federal money laundering under 18 U.S.C. § 1956].
   c. The bill must also clarify how federal civil and administrative actions – most notably civil seizures and forfeitures – related to cannabis should respond to cannabis descheduling and require that any seized property involved in such actions be promptly returned by federal agencies.

[7] *See Terry v. United States*, __ U.S. ___ (2021) (finding that those convicted of the lowest level crack cocaine offenses do not qualify for changes made in the First Step Act); Jeremiah Mosteller, *Federal agencies should not stand in the way of improving our justice system*, Americans for Prosperity (2021), https://americansforprosperity.org/federal-agencies-should-not-stand-in-the-way-of-improving-our-justice-system/ (discussing how the failure of Congress to define even the simple term "day" has complicated implementation of key provisions in the First Step Act).