



Recommendations for Federal Regulation of Legal Cannabis

July 2021

Preface

This white paper was prepared to help guide federal legislators and regulators as they consider the end of cannabis prohibition in the United States in ensuring a free, fair, open, and equitable cannabis marketplace.

About the Cannabis Freedom Alliance

The [Cannabis Freedom Alliance](https://cannabisfreedomalliance.org) (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.

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Introduction

For the first time since Congress agreed with the Nixon Administration in 1970 to outlaw the possession, sale and manufacture of marijuana and marijuana-related products, congressional leadership has recently signaled a willingness to relent on those policies. In December 2020, the House of Representatives took a historic step by passing the Marijuana Opportunity Reinvestment and Expungement (MORE) Act to remove marijuana from the limitations of the Controlled Substances Act and expunge the records of those with previous federal convictions for marijuana.¹ Although it was clear at the time of passage that the Senate would not concur before the conclusion of the session, the move signaled a changing attitude toward marijuana on Capitol Hill, securing a 228-164 bipartisan majority.

This feat came after the House of Representatives approved the Secure and Fair Enforcement (SAFE) Banking Act in early 2019 which was intended to facilitate greater access to financial services by state-licensed marijuana businesses,² although that measure also did not achieve approval by the Senate. Previous marijuana-related measures, such as the Strengthening the Tenth Amendment Through Entrusting States (STATES) Act,³ have been introduced in the House but failed to gain passage or substantial support due to questions over regulatory structure.⁴

A change in Senate leadership in early 2021, however, may inspire bicameral agreement on the federal legalization of marijuana. On February 1, Senate Majority Leader Chuck Schumer issued a joint statement with Senators Cory Booker and Ron Wyden in which they said:

¹ MORE Act of 2019, H.R. 3884, 116th Cong. (2020).

² SAFE Banking Act of 2019, H.R. 1595, 116th Cong. (2020).

³ STATES Act, H.R. 2093, 116th Cong. (2020).

⁴ *E.g.*, Full Committee Markup on H.R. 3884, the "Marijuana Opportunity Reinvestment and Expungement Act", House Judiciary Committee, Nov. 20, 2019 (statement of Chairman Jerrold Nadler (D-NY)) ("The MORE Act as is, without the [STATES Act] amendment [in the nature of a substitute], accomplishes that goal....This amendment, by maintaining all federal criminal penalties in states that have not legalized marijuana under state law would continue to limit research and commerce. It would continue to leave in place federal criminal penalties and enforcement in states that have not legalized marijuana, including draconian mandatory minimums. By not descheduling, the amendment would forego various benefits of the underlying bill, for examples: nothing in the amendment gives any clarity to the community of veterans as it fails to address the continued confusion surrounding the ability of veterans to discuss their healthcare regimens with their VA doctors and the ability of their VA doctors to comply with state legal medical cannabis programs. Nothing in the amendment provides any clarity to active or would-be service members as to their ability to serve our nation based on their past use of cannabis, medicinal use of cannabis, or consumption while off duty or on leave. By removing marijuana from schedule I, the underlying bill does both of these things. Nothing in the amendment protects from federal prosecution and scrutiny those banks which facilitate cash transfers across state lines, between states where marijuana is legal and those where it is not. Nothing in the amendment protects cannabis entrepreneurs from having to comply with § 280E of the Internal Revenue Code....").

We are committed to working together to put forward and advance comprehensive cannabis reform legislation that will not only turn the page on this sad chapter in American history, but also undo the devastating consequences of these discriminatory policies. The Senate will make consideration of these reforms a priority.⁵

Most recently, respecting the denial of *certiorari* in the Supreme Court case *Standing Akimbow, LLC v. United States*, conservative Justice Clarence Thomas criticized the federal approach as a “half-in, half-out regime that simultaneously tolerates and forbids local use of marijuana” where the “contradictory and unstable state of affairs strains basic principles of federalism and conceals traps for the unwary.”⁶

If major marijuana reform legislation is to be taken seriously in Congress this year, there are many aspects it must address. These include everything from federal regulation and tax issues to financial services, clinical research, the contours of interstate commerce and technical barriers to trade, social equity, criminal justice, and respect of states’ reserved powers. There is a danger that federal legalization, done incorrectly, could produce outcomes even more adverse than the *status quo*.

This analysis provides an overview of each of these subtopics and provides general recommendations to help guide the effort toward federal legalization of marijuana that will achieve the following goals:

- Establishing a regulatory framework that promotes public safety while allowing innovation, industry, and research to thrive.
- Ensuring individuals previously involved in the illicit market can effectively secure a second chance and contribute to the legal market.
- Creating 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.
- Imposing 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.

Mechanics of Legalization

Although “legalization” is a catch-all term proponents use to discuss a federal change in marijuana policy, there are many forms that legalization can take and pathways toward achieving it. After the U.S. Supreme Court struck down the Marihuana Tax Act of 1937 as an unconstitutional violation of citizens’ Fifth Amendment protections,⁷ Congress agreed with the

⁵ Booker, Wyden, Schumer Joint Statement on Cannabis Reform Legislation, (Feb. 1, 2021), available at <https://www.booker.senate.gov/news/press/booker-wyden-schumer-joint-statement-on-cannabis-reform-legislation>.

⁶ No. 20–645 (June 28, 2021) (statement of Thomas, J.) (cert. denied), slip op. at 1–2.

⁷ See generally *Leary v. United States*. 396 U.S. 6. (1969).

Nixon Administration to pass the Controlled Substances Act in 1970. The Controlled Substances Act allowed federal policymakers to replace a prohibitive tax on cannabis with an outright prohibition, by classifying the plant and its derivatives as a Schedule I substance. Schedule I substances are those the federal Drug Enforcement Agency (DEA) believes have “no currently accepted medical use and a high potential for abuse”⁸ and their manufacture, sale, or distribution carry criminal penalties. It is now generally accepted within the medical community that marijuana has at least some credible medical uses⁹ and a substantial majority of Americans now agree marijuana use should no longer be criminalized.¹⁰

Congress should pass legislation amending the Controlled Substances Act directly and clarifying that marijuana should not be included within its statutory ambit, but rather be treated like “distilled spirits, wine, malt beverages, or tobacco” under the Act.¹¹ Various recent proposals from Congress such as the MORE Act¹² proposed to do this while the STATES Act¹³ would have partially exempted marijuana from the federal Controlled Substances Act while leaving no guiding principles as to interstate trade or possession or the ability to sell the same products across state lines.¹⁴

A less ambitious approach by Congress could remove federal criminal penalties for the manufacture, sale, and distribution of marijuana without removing marijuana from the auspices of the Controlled Substances Act. Mere decriminalization is inadvisable public policy. Maintaining marijuana within the federal control schedules leaves state, local, and federal agencies constantly in limbo over various regulatory issues that will contribute to heightened consumer costs and uncertainty for small businesses. It also provides substantial opportunity for bad actors to undermine the patchwork of existing state regulatory structures that are not equipped to handle questions of fraud, product liability, and intellectual property protections. Finally, it is entirely possible that the existing medical products in the marketplace could be

⁸ U.S. Drug Enforcement Administration, “Drug Scheduling,” (last visited June 2, 2010), *available at* <https://www.dea.gov/drug-scheduling>.

⁹ NATIONAL ACADEMIES OF SCIENCES, ENGINEERING, AND MEDICINE, THE HEALTH EFFECTS OF CANNABIS AND CANNABINOIDS: THE CURRENT STATE OF EVIDENCE AND RECOMMENDATIONS FOR RESEARCH (2017), *available at* <https://www.nap.edu/catalog/24625/the-health-effects-of-cannabis-and-cannabinoids-the-current-state>.

¹⁰ Megan Brenan, *Support for Legal Marijuana Inches Up to New High of 68%*, GALLUP (Nov. 9, 2020), <https://news.gallup.com/poll/323582/support-legal-marijuana-inches-new-high.aspx>.

¹¹ *E.g.*, 21 U.S.C. § 802(6) (“The term does not include distilled spirits, wine, malt beverages, or tobacco, as those terms are defined or used in subtitle E of the Internal Revenue Code of 1986.”).

¹² MORE Act of 2021, H.R. 3617, 117th Cong. (2021).

¹³ Strengthening the Tenth Amendment Through Entrusting States Act of 2019, H.R. 2093, 116th Cong. (2019).

¹⁴ 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-regulation-fight/>.

hampered from distribution if steps are not taken to ensure pathways for FDA approval or deemed approval of existing products.

Policymakers should note that most state legislatures have engrossed their own versions of the Controlled Substances Act, so even in the event marijuana is removed from the federal law, marijuana would remain an illicit substance in a majority of states.¹⁵ In other words, even after marijuana is fully descheduled from the federal Controlled Substances Act, states will retain the right to decide whether, and under what circumstances, marijuana would become legal within their own borders.

Federal Regulatory Apparatus, Interstate Commerce, and Functions

The mechanics of interstate commerce in marijuana products should be fully anticipated by Congress. Interstate commerce should be limited to only states that have legalized and implemented a commercial regulatory framework for cannabis, as states without such regulatory frameworks in place generally maintain marijuana as a prohibited controlled substance in state law. However, Congress should clearly delineate whether wholesale transactions are allowed in interstate commerce or whether retail sales can be made to customers through the mail or internet across state lines. Congress ought to facilitate free and open interstate commerce as there is with most other commercial products in the U.S.

Further, state regulators will need to work to ensure any products imported from another state's regulatory regime meet their own regulatory requirements for product parameters, labeling, testing, and packaging. It's likely states will work to homogenize these standards once Congress has facilitated interstate commerce in cannabis, but federal regulators can also play an active role in facilitating these discussions to reduce or eliminate technical barriers to trade.

If marijuana is removed from Schedule I under the Controlled Substances Act, state-licensed marijuana businesses would not immediately become free to engage in interstate commerce due to preemptive and existing effects within the Food, Drug and Cosmetics Act (FDCA) for all medical products, food additives, and dietary supplements labeled or intended for use as such in the U.S., and a total lack of direction of regulatory authority for adult-use marketplaces. Under Article I, Section 8 the Commerce Clause gives Congress the power to regulate interstate transactions. Congress will need to endow a federal agency with the authority to do so for adult-use products and provide a pathway within the FDCA for existing products to be sold to existing patients and consumers under the FDA's blessing. Those are the twin pillars of needed regulatory reform in any bill that removes marijuana from the Controlled Substances Act.

This means Congress will need to select one or more agencies to carry out these duties and provide guidance for how it expects this interstate commerce to be regulated. Cannabis falls into existing regulatory competencies for various agencies at the federal level—thus, Congress

¹⁵ See, e.g., NEB. REV. STAT. § 28-401 et seq. (2021); N.C. GEN. STAT. § 90-86 et seq. (2021); W.VA. CODE §60A-1-101 et seq. (2021).

must ensure the best-equipped agencies are empowered to properly regulate the production chain with clear guidance from Congress. Cannabis should be regulated in three ways:

- As a raw agricultural crop;
- As an adult-use product similar to alcohol; and
- As a “food, drug, *and* cosmetic” item.

Congress should elect to regulate unfinished marijuana produce as an agricultural crop and commodity and delegate regulatory authority to the U.S. Department of Agriculture (USDA) to regulate that production. The USDA is the institutional regulator of agricultural crops and commodities in the US at the stage of farm production. As to dealing with the cannabis plant directly, USDA already regulates industrial hemp following passage of the 2018 Agricultural Improvement Act and hemp is a different strain of the same plant species as that from which marijuana is derived. USDA has promulgated rules governing the registration of land on which hemp is grown and coordinates its activities with state agriculture departments to track interstate transfers of hemp. As with barley, hops, and tobacco, the USDA treats these crops, which can be turned into adult-use substances, as full agricultural crops (tradable as commodities under CFTC regulation). USDA regulation of cannabis as a crop similar to those listed will also open the way to substantial state right-to-farm benefits to which federal agricultural crops are entitled, as well as the participation in state agricultural plans and regulation.

Once raw agricultural produce has been transported to a producer for finishing, however, the USDA no longer is the optimal regulator for finished products. Indeed, the lack of authority and clarity in the 2014 and 2018 Hemp bills¹⁶ has led to a limbo situation for farmers and businesses where hemp derived cannabinoid products are still subject to patchwork regulation, and an ongoing, multi-year long rulemaking process to regulate a single cannabinoid, CBD, with no end in sight.

The clearest parallel to adult-use marijuana products is alcohol, which was similarly prohibited by the federal government in the early twentieth century.¹⁷ Alcohol is now regulated primarily at the state level with an overlapping federal scheme to facilitate interstate and international commerce. As with alcohol, each state with a legal framework for marijuana has crafted its own parameters for allowable products, such as testing and labeling requirements and concentration of THC. Many state laws for marijuana, like alcohol, also allow localities to ban its sale. There is one agency that has decades of institutional competency and experience at working in such a regulatory environment with adult-use products: the Alcohol and Tobacco Tax and Trade Bureau (TTB).

¹⁶ See *generally* Agricultural Act of 2014, Pub. L. 113–79, tit. VII, § 7606, 128 Stat. 912 (Feb. 7, 2014) (“Legitimacy of Industrial Hemp Research”) (codified at 7 U.S.C § 5940); Agricultural Improvement Act of 2018, Pub. L. 115–334, tit. VII, §7605(a), 132 Stat. 4828 (Dec. 20, 2018) (“Legitimacy of Industrial Hemp Research”) (codified at 7 U.S.C § 5940).

¹⁷ U.S. Const. amend. XVIII.

TTB requires producers of spirits and wine to acquire a permit from the agency to engage in interstate commerce for these products so federal regulators can track interstate shipments and coordinate those transfers with respective state regulators. Given the seed-to-sale inventory tracking systems used by state marijuana regulators, such coordination for the cannabis industry would be necessary for state regulators to ensure inventory imported from another state is tracked appropriately. This makes TTB the preferred federal regulator of state-licensed marijuana businesses for adult-use products and adult-use interstate commerce. Furthermore, TTB has an institutional history of working with the FDA on consumable adult-use products where the FDA's traditional food additive and ingredient authority comes into play. Accordingly, the agency is in the best position to ensure not only that adult-use flower and concentrate products are facilitated in commerce, but also edible products.

The most difficult regulatory issue facing marijuana descheduling is the FDA and FDCA. The scope of the problem is huge. Currently, thousands of doctors recommend millions of patients routinely use a vast array of state-licensed medical marijuana products—none of which are approved under the FDCA and are technically considered illegal, “adulterated” versions of currently-approved THC and CBD drugs Marinol and Epidiolex. Additionally, because these are FDA-approved CBD and THC drugs, there are issues of preclusion from use in foods, dietary supplements, or cosmetics/topicals. The FDA has further demonstrated a serious dragging of the feet on these issues, undertaking a multi-year rulemaking for a single cannabinoid to be regulated as a dietary supplement, let alone the more than 100 other cannabinoids that exist.

If any jurisdiction is granted to the FDA for the regulation of all marijuana products, Congress should make clear that it deems state regulatory frameworks effective for ensuring the safety of marijuana products created within their borders and that the FDA will not be responsible for licensing facilities producing adult-use products. The FDA's role should at most extend to the certification of products for sale to the public in interstate commerce. There must be a grandfathering within the FDCA of broad product classes currently available for sale on state-regulated markets. When the FDCA was passed in 1938, it grandfathered products produced under the 1906 Food and Drugs Act. Grandfathering was also employed in the 1914 Harrison Narcotics Act, the 1962 FDCA amendments, and the 2010 Medical Gas Safety Act. Congress should use grandfathering here as well. The FDCA's preclusive effect must be clearly removed for cannabis products so that adult-use edibles and non-intoxicating topicals can contain THC and CBD. The FDA should be working to set standard serving sizes and interstate medical labeling requirements and should be required to honor state-medical program products and parameters with respect to them. The cost and timeline for seeking FDA approval on marijuana products would also be prohibitive for most marijuana companies, especially those that are not greatly capitalized. This is not to say new cannabis drugs should not be developed or sold, but existing products and prevailing medical practice should not be disrupted.

Financial Services

Even fully compliant, state-licensed marijuana businesses are largely precluded from access to financial services in the United States. This means they are forced to conduct a majority of financial transactions in cash and often must store large amounts of cash on site. They are further unable to secure most forms of debt financing and insurance, creating significant barriers to entry within state-legal marijuana markets because entrepreneurs must have access to equity capital. The cash-intensive nature of the industry has become a well-known public safety issue because wrongdoers are aware marijuana businesses often have large amounts of physical cash on hand. In 2019 representatives from the Credit Union National Association testified to the Senate Committee on Banking, Housing and Urban Affairs that half of marijuana dispensaries had been robbed or burglarized.¹⁸ Even state and federal tax authorities have complained about the safety hazard stemming from tax payments made in cash by marijuana companies.¹⁹

Multiple federal laws and regulations preclude marijuana businesses from gaining access to financial services. The Bank Secrecy Act, PATRIOT Act, and federal racketeering laws all apply to entities that manufacture, sell, or distribute Schedule 1 substances and aiding and abetting crimes can be prosecuted against financial entities that help facilitate this activity by offering bank accounts. The Justice Department articulated enforcement priorities in 2014 advising U.S. attorneys to focus those efforts on actors not in compliance with effective state regulatory frameworks for marijuana and the Financial Crimes Enforcement Network (FinCEN) promulgated accompanying guidelines nominally intended to facilitate banking for state-compliant marijuana companies by specifying the reporting requirements financial institutions would need to follow. Those priorities issued by the Justice Department, known as the “Cole Memo,” were rescinded by the U.S. Attorney General in 2018 but the FinCEN guidance remains in place. That guidance requires financial institutions to conduct significant and ongoing “Know Your Customer” background checks and to submit Suspicious Activity Reports over both individual transactions and transactions in the aggregate for account holders it believes are involved in the manufacture, sale, or distribution of any Schedule 1 substance. Despite FinCEN’s stated intention of facilitating financial services for legitimate marijuana businesses, most

¹⁸ *Hearing on Challenges for Cannabis and Banking: Outside Perspectives: Before the S. Comm. on Banking, Housing, and Urban Affairs*, 116th Cong. 2 (2019) (testimony of Rachel Pross on behalf of The Credit Union National Association) (“A 2015 analysis by the Wharton School of Business Public Policy Initiative found that, in the absence of being banked, one in every two cannabis dispensaries were robbed or burglarized—with the average thief walking away with anywhere from \$20,000 to \$50,000 in a single theft.”).

¹⁹ Geoffrey Lawrence, “Commentary: The SAFE Banking Act Fails to Ease Challenges Facing Marijuana Businesses and Banks,” REASON FOUNDATION (May 20, 2020), <https://reason.org/commentary/the-safe-banking-act-fails-to-ease-challenges-facing-marijuana-businesses-and-banks/>.

commercial banks have made a business decision not to service those accounts simply because the compliance requirements are so costly and onerous for financial institutions.²⁰

States have considered creating state-chartered financial institutions to solve the public safety issues and lack of audit records inherent to a cash-based industry but have discovered federal banking regulators have denied both deposit insurance and Federal Reserve master accounts to these new institutions.²¹

Recent proposals in Congress such as the SAFE Banking Act seek to bar federal regulators from discriminating against financial institutions that offer accounts to legitimate marijuana businesses and would provide some protection against possible aiding and abetting charges. However, the Know Your Customer and reporting requirements facing these financial institutions would still be costly and onerous, meaning most financial institutions would likely remain unwilling to offer these accounts. The SAFE Banking Act provides essentially no protection to financial institutions that offer loans or other financing to marijuana companies, meaning most businesses would still need to rely on private equity financing even though that dynamic carries significant equity considerations.

The most direct route of freeing up financial services to the marijuana industry is to de-schedule marijuana and regulate it. This ends any question of federal illegality and uncertainty for financial and securities exchange institutions. Absent this change, Congress could amend the Bank Secrecy Act, PATRIOT Act, racketeering and aiding and abetting laws, and the panoply of related statutes directly to exclude actions involving only state-licensed marijuana commercial activity. Regardless, agencies out to ensure that guidance is updated in a de-scheduling environment to ensure outdated policies do not inhibit businesses from access.

Criminal Justice

The prohibition of marijuana has criminalized many otherwise law abiding citizens and left a legacy of widespread convictions. More than 500,000 arrests are still made each year for mere possession of marijuana.²² Even an arrest record can limit an individual's ability to engage in productive behaviors such as pursuing employment or higher education or applying for a small business loan. Further, a serious equity question arises when considering marijuana legalization: Should individuals continue to carry a criminal record for actions that are no longer a crime while others are free to engage in those behaviors without legal consequence? To many, this is a clear injustice that must be remedied alongside the end of criminalizing the substance.

²⁰ GEOFFREY LAWRENCE, MARIJUANA INDUSTRY FINANCIAL SERVICES: OBSTACLES AND SOLUTIONS, REASON FOUNDATION (Sept. 2019), available at <https://reason.org/wp-content/uploads/marijuana-industry-financial-services.pdf>.

²¹ *Id.*

²² U.S. DEPARTMENT OF JUSTICE, FEDERAL BUREAU OF INVESTIGATION, ESTIMATED NUMBER OF ARRESTS: UNITED STATES, 2019, (2020).

These recognitions have inspired most state legalization statutes to incorporate provisions that remove prior convictions for individuals in cases when their underlying actions would now be legal and ensure individuals currently serving a sentence can have it reduced by the amount imposed for any marijuana offenses. The MORE Act included similar provisions for those who carry federal convictions. Congress, however, should be mindful that a large majority of low-level marijuana-related convictions occur at the state, and not federal, level. As such, responses that solely focus on federal marijuana convictions alone will not effectively alleviate the burden placed on most individuals with such convictions. This doesn't mean that Congress is constitutionally empowered to directly impose a solution to state criminal law issues, but should also pair these efforts with additional measures that can help individuals with a state conviction.

In particular, Congress should instruct the Small Business Administration, Immigration and Naturalization Service, and the federal Department of Education not to disqualify applicants for small business loans, student loans, or entry solely on the basis that those applicants carry a past non-violent marijuana conviction. Beyond that, Congress should consider how to encourage states where marijuana is legal to adopt policies that automatically expunge prior convictions, similar to Illinois, when the underlying actions would today be legal.²³

Taxation

Marijuana businesses are already taxed extensively at the federal level, even though their operations violate federal law. This is due to Section 280E of the Internal Revenue Code,²⁴ which disallows credits or deductions for any taxpayer who traffics in a Schedule I or Schedule II substance. Section 280E precludes the usual standard of deductibility for business expenses—those that are “ordinary and necessary” for a particular industry—so they may only deduct the costs paid directly to acquire inventory. Payments for employee compensation including benefits, rent, depreciation, travel costs, licensing fees, and other expenses for an industry that supports over 300,000 employees²⁵ are not deductible on either personal or corporate federal income tax returns for entities that manufacture, sell or distribute any Schedule I or II substance. In effect, state-licensed marijuana businesses must apply income tax rates to their revenue, not their net income (profits). Unprofitable marijuana businesses face significant

²³ Raymon Troncoso, *Illinois State Police clear nearly 500,000 marijuana arrest records*, JOURNALSTAR (Jan. 4, 2021), <https://www.pjstar.com/story/news/2021/01/04/illinois-state-police-expunge-almost-500-000-marijuana-arrest-records/4135803001/>.

²⁴ 26 U.S.C. § 280E (2020). Congress passed this provision in response to a 1981 U.S. Tax Court decision found in favor of a cocaine dealer who claimed an array of deductions related to his trade on a Schedule C form for the 1974 tax year. *Jeffrey Edmondson v. Commissioner*. 42 T.C.M. 1533 (1981). Although Congress at that time sought to prevent illegal street dealers of narcotics from claiming tax deductions, the provision now has the unintended effect of penalizing state-licensed marijuana companies that aim to operate a legitimate, legal business.

²⁵ BARCOTT ET AL., JOBS REPORT 2021 (2021) (annual Leafly–Whitney Economics cannabis jobs report).

federal tax liability, and this provision is so onerous that it can push a company from profits to losses. De-scheduling cannabis entirely (or re-scheduling marijuana to a Schedule III or more permissive classification) will automatically resolve this issue for state-licensed marijuana companies.

Separate proposals have arisen for a federal excise tax on cannabis to finance the costs of federal regulation as well as to generate new revenue.²⁶ Congress should follow the approach to regulation recommended here and allow the TTB to act as lead regulator to minimize the costs of federal regulations. When combined with the tax savings that marijuana companies could realize being freed of Section 280E, a modest federal excise tax could still result in a net tax cut for these companies.

Lawmakers should bear in mind, however, that legal marijuana is a substantially similar product to illicit marijuana sold through established black-market supply channels. Consumers remain unwilling to substitute legal marijuana for illegal marijuana when government burdens impose sufficient costs on legal marijuana.²⁷ Several state and local governments already assess substantial excise taxes on recreational marijuana sales²⁸ that, when combined with a federal excise tax, could represent a significant and variable cost difference between legal and illegal markets.²⁹ Tax differentials between recreational and medical marijuana could also encourage the inappropriate pursuit of and provision of prescriptions for cannabis products.

Reason Foundation has recommended that states implement no more than a 15 percent *ad valorem* excise tax at retail to minimize market distortions.³⁰ Any additional federal excise tax could cover the cost of regulation with a modest federal excise rate (e.g. less than one-half of one percent) on the wholesale price of cannabis products. In addition, a twenty-year moratorium on increases in the excise rate would promote competitiveness and allow states to reach tax equilibrium.

Clinical Research

In late 2020 the U.S. House of Representatives passed the Medical Marijuana Research Act,³¹ aiming to expand the availability of marijuana for clinical research purposes. For decades, the

²⁶ Geoffrey Lawrence, “Commentary: State Marijuana Regulators Send Congress Cannabis Market Recommendations.” REASON FOUNDATION (Mar, 15, 2021), <https://reason.org/commentary/state-marijuana-regulators-send-congress-cannabis-market-recommendations/>.

²⁷ GEOFFREY LAWRENCE & SPENCE PURNELL, MARIJUANA TAXATION AND BLACK MARKET CROWD-OUT, REASON FOUNDATION (Jan. 2020), available at <https://reason.org/policy-study/marijuana-taxation-and-black-market-crowd-out/>.

²⁸ Ulrik Boesen, “How High Are Taxes on Recreational Marijuana in Your State,” TAX FOUNDATION (Mar. 31, 2021), <https://taxfoundation.org/state-recreational-marijuana-taxes-2021/>.

²⁹ Ulrik Boesen, “Less Should be MORE With Federal Cannabis Taxation,” TAX FOUNDATION (May 28, 2021), <https://taxfoundation.org/state-recreational-marijuana-taxes-2021/>.

³⁰ *Ibid.*

³¹ Medical Marijuana Research Act, H.R. 3797, 116th Cong. (2020).

only institution licensed to produce marijuana for research purposes has been the University of Mississippi. Clinical researchers can request access to this research-grade marijuana through the National Institute on Drug Abuse (NIDA) Drug Supply Program.

However, recent testing of the marijuana produced by the University of Mississippi by commercial testing facilities reveals that research-grade marijuana bears little resemblance to the type of marijuana available to consumers in commercial or medical markets. Tests show research-grade marijuana is closer to industrial hemp in terms of its cannabinoid content and genetic makeup because it includes very low amounts of the psychoactive cannabinoid THC.³²

If Congress wishes to accurately inform the public about potential benefits and dangers of cannabis consumption, it's imperative that medical researchers gain access to the types of marijuana individuals actually consume. Clinical researchers could be permitted to procure cannabis through readily available commercial channels rather than applying through NIDA to receive marijuana through the federal Drug Supply Program.

Conclusion

There are many facets to consider along with prospective federal legalization of marijuana. These facets are technical in nature but should not be overlooked by Congress because failure to address them correctly could lead to devastating effects on the functioning of the new market. A majority of issues affecting public safety and compliance – from the availability of financial services to punitive treatment of marijuana companies under the federal tax code – would be solved by removing marijuana from Schedule I classification under the Controlled Substances Act. However, Congress should still anticipate the regulatory approach it will adopt with regard to commercial marijuana and which agency should take charge. This agency will need to facilitate commerce between state regulatory regimes and work with state regulators to minimize technical barriers to trade between the states. Many states will undoubtedly continue to prohibit marijuana within their boundaries and Congress should respect the right of states to make these decisions. Criminal justice reforms contemplated in conjunction with federal legalization should recognize most marijuana-related convictions are made in state courts and federal agencies should not discriminate against individuals based solely on marijuana convictions that do not violate federal law. Research into the clinical effects of marijuana should be enhanced and expanded so consumers are adequately informed of the possible risks and benefits of cannabis consumption.

Congress should especially recognize that states have labored to put in place effective regulatory structures that ensure the safety of commercially available marijuana products and control their distribution. Congress needn't usurp this authority but should defer to state regulators to govern marijuana markets within their own states as has been done with wine and spirits. The Tenth Amendment to the U.S. Constitution reserves to the states the powers

³² Schwabe, Anna et al. "Research Grade Marijuana Supplied by the National Institute on Drug Abuse Is Genetically Divergent from Commercially Available Cannabis." *Biorxiv* (Mar. 19, 2019).

not enumerated within that document and some states or localities will seek to continue to the prohibition of marijuana. Federal authorities are granted the power to regulate commerce between the states and should limit their role to facilitating these transactions only to ensure a safe, efficient, and functional market.