



PRIVUS CAPITAL

Cannabis in Mexico Report

April 2020

CBD and Hemp Markets May Form More Rapidly

Legislative Activity

While the current COVID-19 crisis may impact deadlines and workflow, the underlying determination of the administration of President Andrés Manuel López Obrador (AMLO) to legalize the production and use of cannabis for recreational and medicinal purposes remains firm as does the emphasis on addressing the needs of communities most impacted by the illegal drug trade and on prioritizing access for medicinal, pharmaceutical, or palliative use. Since the last edition of this newsletter, the Mexican Senate released revised versions of the proposed cannabis legislation in January and [February](#) in order to comply with the Supreme Court-mandated deadline of April 30 (when the Mexican Congress is scheduled to adjourn). The February draft version (on which the following comments are based) was [approved by a joint session](#) of the Justice, Health, and Legislative commissions on March 3 with support from the Morena, Movimiento Ciudadano, and PRD delegations. The PAN delegation opposed the draft bill because of concerns about certain specific provisions while PRI senators abstained. The full Senate began its deliberations on the current working draft during the week of March 9. Additional changes to the legislation are likely given the wide range of viewpoints expressed to date by supporters and opponents of legalization.

In view of the COVID-19 situation, it is not possible at the time of this writing to predict with certainty whether the mandated deadline of April 30 can be met. We discuss this situation in greater detail below.

In order to chart the progression of thinking about legalization of cannabis in Mexico, this edition of our newsletter compares changes between the October draft legislation (addressed in our [December edition](#)) and the version that is now on the floor of the full Senate. **We encourage interested readers to [contact us](#) with specific questions about the *dictamen*.**

General Comments

In comparing the October 2019, January 2020, and February 2020 versions of the draft bill (or *anteproyecto*), one can clearly see its evolution. Some of the changes are stylistic in nature and ensure the use of preferred legal language and definitions but others are substantive and significant. These changes include welcome clarifications, business-friendly improvements, further restrictions, and changes that reflect the AMLO government's political objectives and overall themes.

The current working draft defines *cannabis psicoactivo* as the plant or any product with a THC content of *greater* than 1%. It is important to note that there are limited regulations and references to products containing *less* than 1% THC, which suggests there may be more immediate opportunities for CBD products and industrial hemp. Indeed, our sources in Mexico expect that products falling under the 1% threshold will be considered legal by default. We note that COFEPRIS, Mexico's FDA equivalent, might consider developing regulations for food and cosmetics containing CBD as is the case in the United States.

The continued prohibition on vertical integration clearly reflects concerns about the intrusion of organized crime into what is intended to be a legal, regulated market. However, the exemption to the general prohibition on holding multiple types of licenses for vulnerable communities may create an interesting space (see licensing comments below).

The proposed legislation seeks to favor or at least protect those who seek to use cannabis for medical, pharmaceutical, or palliative use. Access for such patients will be [exempt from any administrative procedure](#) that would limit their ability to exercise their rights and the government will take the necessary measures to allow for market entry of drugs or products with cannabis that satisfy the needs of people who require them. Further, the legislation directs the issuance of licenses for the processing and marketing of psychoactive cannabis for medical, pharmaceutical, or palliative uses immediately after entry into force of the legislation whereas licenses for recreational cannabis can be issued only eighteen months after entry into force.

Though the current working draft continues to call for the creation of the Mexican Cannabis Institute, a number of questions arise regarding its role, the scope of its authority, and its consistency with the government's stated objective to limit the size (and cost) of the federal bureaucracy. There are also questions surrounding the interaction between the new institute and COFEPRIS. Some of these issues may be resolved through the legislative process but others may not find their resolution until after formal creation of the institute by January 2021.

In our prior report, we addressed several specific provisions that are likely to be especially relevant to those interested in pursuing opportunities in this sector. Below we address relevant changes and highlight new provisions that may influence business and investment decisions. All references to specific articles are keyed to the February draft law.

Specific Provisions

Licensing: The current working draft legislation adds a fifth type of license for research to the previously defined types of licenses for cultivation, processing, sale, and import/export, all of which include the auxiliary activities of transport and storage but are mutually exclusive and non-transferable (Article 36). The draft also defines the maximum size of the land parcels that can be used for cultivation per license holder – one hectare per licensee for open field, 1,000 sq. meters for greenhouse growing. Reconversion of forest lands for cannabis production is prohibited (Article 35).

Consistent with the AMLO administration's focus on poor and underserved communities, and as an "affirmative action to compensate for damages," the draft legislation exempts *ejidos* and agrarian communities that have been affected by past interdiction efforts and find themselves vulnerable from the prohibition on holding more than one license in any of the four original categories (Article 36).

Only Mexican nationals can be issued licenses. Applicants must be registered in the Federal Taxpayer Registry and obtain a certificate confirming compliance with their tax obligations from Mexico's internal revenue service (*Servicio de Administración Tributaria* or SAT). Prior versions of the legislation simply required that applicants not be delinquent in their tax payments (Article 39, I).

Foreign Ownership: A material change in the current working draft takes treatment of foreign direct investment out of this law (where it had been set at 20% in the earlier version)

and defers instead to the Foreign Investment Law with specific reference to Article 7, Clause 3 of the law (Article 39). We intend to return to the critical issue of foreign investment in the Mexican cannabis sector in a future newsletter.

Allowable Number of Plants for Personal Use: The current working draft reduces the number of plants permitted in a home with more than one consenting adult to six from the prior limit of twenty (Article 17). This change would make Mexican practice comparable to that of the United States and Canada.

Edibles, Cosmetics, and Products Combining Cannabis and Other Substances: The current working draft provides greater clarity on cosmetics (Article 66, V) and edibles (including beverages) (Article 66, VI) for which there can be no sale, import, or export of products that contain over 1% THC (with an exemption for medicinal use). However, the licensing and production of edible products and cosmetics that contain less than 1% THC will be permitted 18 months after entry into force of the law, compared to the time period for non-edible non-psychoactive products that is six months (Transitory Article 14, V). Our Mexican sources indicate that the prohibition on edibles and cosmetics that contain over 1% THC is firm, thus we should expect no relaxation of these provisions prior to passage.

Industrial Use (Hemp): The current working draft clearly separates hemp (“non-psychoactive cannabis”) from psychoactive cannabis at the cutoff point of 1% THC content; any plant or product below this 1% THC threshold is considered “hemp” and not regulated by this law. Further, while plot size for the cultivation of cannabis is clearly defined within this law, plot size for the cultivation of hemp is covered by national agrarian policy as an agricultural crop (Article 35). Use of non-psychoactive cannabis is prohibited by children and adolescents except for medical, pharmaceutical, and palliative reasons (Article 66, I).

Mexican Cannabis Institute: The January version of the draft legislation had included a substantial expansion of the Board of Directors by adding representatives of the Attorney General’s office and, more important, an array of ten (10) politicians, including the presidents of five important commissions in both the Senate and the House of Representatives, respectively. Interestingly, shortly thereafter the February version of the draft proceeded to remove the Prosecutor General and the 10 politicians from the Board (Article 52), although the politicians can be invited in the same way as outside experts to meetings of the Institute’s Board but with no voting rights.

Labeling: The January draft added a requirement (retained in the February draft) that packaging must contain a quality control stamp to certify that the contents have followed traceability rules (Article 26, XIV). The current working draft requires that the portion of the visible packaging devoted to information regarding possible effects of consumption be increased from 30% to 50% (Article 26, XII). It also requires inclusion of a warning label stating that “the consumption of this product is harmful to health; it is recommended that adults between 18 and 25 and pregnant women in the period of breastfeeding avoid consumption.” (Article 26, XV).

Social Justice Carveout: The February draft increases the share of licenses that should be granted to indigenous peoples and communities, rural agricultural workers, or *ejidatarios* to 40% in the municipalities where eradication programs were implemented during the period when cannabis was banned (Transitory Article 8).

Constitutional Concerns: In the spirit of a heads-up, some lawmakers (and perhaps governors) question Congress’ authority to legislate on cannabis without taking into account the role and authorities of the individual Mexican states. Mexico’s Constitution, similar to the U.S. Constitution, devolves power to the states for all topics not specifically apportioned to the federal government. Some lawmakers hold the opinion that the federal Congress does not have an exclusive authority to legislate in the matter of drugs (based on Article 73 of the Constitution), but others consider it an implied power (Article 73, paragraph XXXI) because this matter is included in federal legislation concerning health and criminal law. Given that the federal government lacks specific authority to regulate drugs, some states could potentially challenge the constitutionality of the law, if approved.

Next Steps

The approval of the *dictamen* by the relevant commissions does not mean that the Senate will approve the bill as currently drafted. Even if the measure passes the Senate relatively soon, it is doubtful that the lower house (*Cámara de Diputados*) would have time to approve the bill by the Supreme Court’s April 30 deadline. It is possible, even probable, that the congressional session will be extended due to the COVID-19 crisis, but this would not automatically extend the Supreme Court deadline (which was already extended from October 31, 2019). If the Congress does not pass appropriate legislation by April 30, it would be formally in a position of non-compliance with a Supreme Court ruling which

could generate a constitutional crisis.¹ We suspect that the Congress will make a formal request for an additional extension although it is not a certainty that the Court would grant it despite the seeming *force majeure*-like circumstances. In this case, one possible solution would be rapid drafting and passage of legislation that would simply remove the penalties for personal consumption while continuing to debate the current, more expansive bill when possible. We will continue to monitor carefully developments on this front.

Recommendation

Mexico's Congress was progressing steadily toward regulation of cannabis, albeit more slowly than needed to meet its April 30 deadline. The interruption caused by COVID-19 will likely further extend the timeline before there is a functioning legal cannabis market in Mexico with respect to recreational cannabis with a THC content of over 1%. Authorization for industrial hemp and for CBD products (both referred to in the legislation as *cannabis no psicoactivo*) will likely come sooner and may present a quicker immediate path to market for firms and investors interested in entering the Mexican market for domestic sales or for export. Regardless, many key decisions will be made in the coming months. **In the context of the dislocations caused by the COVID-19 pandemic, firms interested in entering this nascent market should continue to monitor closely developments and define strategic goals. These newsletters are intended to assist in this process, and we encourage readers to contact us at any time to discuss possibilities, plans, and ideas.**

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The material provided in this document is for informational purposes only and not for the purpose of providing legal advice. You should contact your attorney to obtain advice with respect to any particular legal issue or problem.

¹ Given the March 31 emergency decree which requires a 30-day suspension of non-essential work, the April 30 deadline may be extended by that number of days although no formal decision has been announced.