



PRIVUS CAPITAL

Cannabis in Mexico Report

Legalization of Cannabis Use in Mexico:

Entering the Final Stretch

December 17, 2020

Context

The Mexican Congress has been engaged for two years in formulating its response to a ruling of the Mexican Supreme Court in late 2018 to allow for personal use of cannabis by individual Mexican citizens. Congress chose early on to surpass the technical requirement to amend the *General Law on Health* and some other supporting regulations and has rather pursued a more ambitious goal to put in place a comprehensive legal framework that would create a new national commercial sector, consistent with the initial intent of the Administration of President Andrés Manuel López Obrador (AMLO), and most specifically the Secretary of Government (*Secretaría de Gobernación*), former Senator and Supreme Court judge, Olga Sánchez Cordero. As was expected for such a complex objective, the legislative path has been long.

To that end, and after extensive study by several commissions jointly, the Senate finally passed its version of the new *Federal Law for the Regulation of Cannabis* accompanied by necessary amendments to other existing legislation on November 19, 2020, and referred it to the *Cámara de Diputados* (“the House”) for consideration on November 25. After three previous extensions, the Supreme Court had set December 15, 2020, as the deadline for passage of the legislation. Pleading general delays caused by the COVID-19 pandemic and the need to have the necessary time to review the Senate-approved legislation in committee, the House requested a fourth extension of this deadline on December 9, to which the Supreme Court agreed on December 10, 2020. Congress now has until April 30, 2021, the last sitting day of the next congressional session to pass legislation legalizing and regulating the adult recreational use of cannabis.

The next congressional session begins on February 1, 2021, and the members of the House will have their collective eye on the clock. We find it difficult to imagine that the Supreme Court would agree to yet another extension barring some remarkable circumstances. Such a request could appear disrespectful to the judicial branch. But the language used by the president of the *Cámara de Diputados* in seeking the latest extension left the impression that we might expect amendments to the Senate-approved draft bill. Should the House amend the cannabis legalization bill, the legislative procedure of the Mexican Congress will require that the bill be returned to the Senate for consideration and approval, or not, of the amended bill. If the latter chamber does not agree, the bill can be sent back to the House yet again, after which the House will have the last word. Since all this potential legislative work must be completed before the close of the session on April 30, the implication is that the House commissions should take on review of the cannabis legalization law as early as possible in February.

Unlikelihood of Presidential Veto

Much progress had been made on the legislation in the Senate in the past several weeks, which created a sense of congressional momentum. Regardless of this further delay, we believe that we are in the final stretch on the way to legalization of the recreational use of cannabis and its by-products. And there is no indication to date that AMLO will intervene at the end of the legislative process and wield the presidential veto power. In fact, in what were perhaps his most expansive comments to date on the legalization of cannabis for recreational use, AMLO stated on November 26 that this is:

“...part of carrying out a revolution of consciences, where each of us is responsible for his actions...The development of freedoms is very important...Things do not have to be prohibited, prohibited, prohibited. If something is authorized, if something is allowed, well, act responsibly. I believe that this will happen in this new legislation on the use of marijuana. Have confidence in people and seek to do good.”

Possibility of Further Amendments

The version of the law that the Senate sent to the House looks quite different from the original drafts proposed over a year ago, which went through various iterations and modifications along the way. Our assumption is that this Senate bill will survive largely intact despite possible amendments; such amendments could take the form of relatively minor technical tweaking related to form or the incorporation of some bigger propositions,

such as, for example, the creation of a quasi-state monopoly agency to control the buying and selling of cannabis as the middleman in the distribution chain (an idea championed earlier by Mario Delgado Carrillo, now president of the main governing party, MORENA – [Movimiento Regeneración Nacional](#)), or some flexibility in the requirements for traceability for small farmers and producers from marginalized communities.

Key Features of the Senate-Approved Version of the Law

Given that the draft law currently under consideration represents the view of the Senate, and assuming that it will remain largely intact, it provides a good head start on predicting and preparing for commercial opportunities in a future Mexican cannabis space. The provisions of the law blend a desire to create a new motor of economic development for Mexico, the need to regulate activities that were until now illegal and taboo, concerns about public health implications, economic nationalism, and political considerations in terms of being perceived to protect marginalized and vulnerable communities and promote social justice. The net result looks and feels similar in many respects to the regulatory framework regarding cannabis legalization in force in Canada with some specifically Mexican overlays.

Setting aside small edits related to clarity of language and so on, the final Senate-approved law contained at least 188 substantive changes from the previous pre-COVID version that had been published last February 2020.

The law, of course, contains many technical details, but its key features can be summarized as follows:

- **Jurisdiction:** The law is now a Federal Law, which has constitutional implications for its applicability in the 32 Mexican entities; for the first time, the law includes specific reference to the mayoralties (*Alcaldías*) of Mexico City as well as municipalities.
- **Recreational vs. Medical:** The law now governs **only** recreational use of cannabis and its derivative products; the law explicitly exempts medical use and refers it to the jurisdiction of the General Law on Health (*Ley General de Salud*), including the deletion of an entire former chapter on medical, therapeutic, and palliative use of cannabis.
- **THC vs. CBD:** The law is principally focused on the activities associated with so-called psychoactive cannabis (i.e., with THC content) and as a smokable product,

but also treats generally non-psychoactive cannabis, or hemp, and describes that area as effectively “industrial use;” matters related specifically to the production of “cosmetics” (including presumably skin creams, ointments, etc.) containing CBD are referred to the General Law on Health.

- **Personal Use:** Subject to a series of restrictions largely related to protecting minors and others from exposure to second-hand smoke, the law legalizes the personal use of cannabis by individuals, including possession of up to 28 grams of cannabis and the right to maintain up to six plants in the home for personal supply (eight for households with more than one adult).
- **Edibles:** There is no longer an explicit ban on edibles, including beverages, as had existed in previous versions of the law, with the exception of a prohibition on mixing cannabis with alcohol, nicotine, caffeine, energy drinks, etc., much like similar prohibitions in legal markets like Canada.
- **Commercial Activity Permitted:** The law also establishes a wide range of commercial activities related to cannabis that will now be legal, subject to the issuance of the appropriate operating licenses, and which include cultivation and growing (agriculture), processing (manufacture and value-added processes), and commercialization (point of sale), including the sales from one part of the value chain to the next.
- **Regulator for Recreational Use:** The federal agency that will supervise the new cannabis regime for the recreational use of cannabis is the renamed *Mexican Institute for the Regulation and Control of Cannabis*; the new name implies a more “managerial” role focused on the implementation and execution of the law and regulations, and much of the body’s previously autonomous policy-making or executive character has been removed; the Institute now reports as a subsidiary agency to the Secretary of Health, and its governance has been simplified, including the removal of members of Congress from its board, placing it squarely under the jurisdiction of the Ministry of Health and therefore more administrative in character than envisaged originally; it will continue to be responsible for issuing licenses, setting regulatory guidelines and standards of various kinds, coordinating programs such as those aimed at addiction and problem use, making recommendations to the government, and so on.

- **Vertical Integration:** Importantly, the law has abandoned earlier prohibitions on vertical integration and a single entity or individual can apply to obtain more than one type of license and, therefore, participate in all segments of the value chain; in addition, it affords the new regulatory institute the flexibility to award more than one license of each type to a single licensee; in view of this evolution of thinking, the law now provides the power to review the issuance of licenses to ensure that there is not unwanted concentration of ownership that might create monopolies or harm competition in the market.
- **Cultivation Licenses:** Regarding the issuance of cultivation licenses, 40% of licenses for the first five years of the law being in force will be awarded on a preferential basis to applicants from marginalized communities, and 20% thereafter on the assumption that their state of economic vulnerability will have been lessened; such marginalized communities are defined throughout the text as “Indigenous villages and communities, peasants or members of *ejidos*, *ejidos* and agrarian communities, marginalized communities or those that, because of their conditions, characteristics or having been affected by the system of prohibition, must receive priority attention;” normally the holder of a cultivation license will still be limited to one hectare for open field and 1000 sq. meters for greenhouse growing, although there is provision for an exercise of “affirmative action” that could include the award of licenses for up to eight hectares of open field growing and two 1,000 sq. meter greenhouses to a single holder who is a member of such a marginalized community or micro and small farmers, as well as expedited pre-registration of seeds.
- **Retail Sales:** Regarding the commercialization (sales) licenses, one licensee can operate up to three separate points of sale under that license.
- **Foreign Investment:** The law does not cover foreign investment in the cannabis sector and refers the matter to the existing Foreign Investment Law, and, in so doing, removes some confusing language that had appeared in earlier drafts; in other words, foreign investment in this new space is to be treated in the same way as for any other sector of the Mexican economy, implying the opportunity generally for foreign investors to participate robustly throughout the cannabis value chain, subject to the definitions in the Foreign Investment Law and on a case-by-case basis.

- **Import and Export of Product:** Possibly with an eye to treaty obligations, international cooperation efforts in the field of drug interdiction, other legal obligations or the practice in other countries, the law distinguishes between psychoactive cannabis and hemp in prohibiting the importation and exportation of the former, while broadly permitting that of the latter.
- **Traceability:** The importance of testing and traceability is reinforced throughout the law more explicitly than in the past.
- **Approvals for Licenses:** The law now better reinforces the general culture of transparency and accountability by insisting, for example, that the Institute provide explicit reasons for any denial of licenses; in the most recent previous version of the text, the regulatory institute could have implied passive denial by simply not answering the application within the established time frame.
- **Timing for Licenses:** The law lays out the anticipated timelines for the roll-out of licensing that prioritizes the easier hemp-related licenses first within six months of the entry into force of the law and cultivation licenses as soon as the regulatory institute establishes the necessary guidelines for testing and traceability, followed by licenses for processing and commercialization within 18 months of the entry into force of the legislation.
- **Review of Implementation:** Recognizing that there may be growing pains in a new commercial sector like cannabis that require greater assessment than might normally be the case, the law builds in formal mechanisms for the review and evaluation of its implementation and lessons learned, including a public call within a year for input on possible necessary changes to the legal framework and the preparation of a national plan for improving the implementation of the law one year after the establishment of the regulatory institute.
- **Fines and Violations:** There has been a review of fines for licensing violations, and some have been increased while others that were thought too punitive have been reduced; for those affected by the new legalization, the law introduces the possibility of dropping charges, commuting sentences, and scrubbing criminal records for cannabis-related matters.
- **Public Complaints:** The law introduces the concept of citizen complaints (*denuncia ciudadana*) against violators of provisions of the law, including the advertisement of a “snitch line” in 100% smoke-free locations or those reserved exclusively for smokers.

Indications for a Strategic Pathway and Timeline

Separate from adoption of a new law legalizing recreational use of cannabis and its by-products, there are still regulations on the medical use of cannabis-derived products that are due to be enacted (see [Monarch-Privus Cannabis Report \(2020-10\)](#) dated October 21, 2020). Here, the Mexican government (rather than Congress) has also been ordered by a court to produce these regulations as the result of a decision in favor of the right of a citizen to receive legal access to medical cannabis, for which the court-imposed deadline has also been extended several times. There have been quite extensive public consultations on the regulations over the past several months. By the terms of the court's agreement to the last deadline extension, we should be seeing these final regulations on medical use around the middle of January 2021, barring another request for an extension.

The approach adopted in the cannabis legalization bill in Congress now removes any confusion about how the two uses would be governed – recreational use by a new law (including some modifications to existing laws) and medical use by a separate set of administrative regulations issued and published by the Government of Mexico. The Secretary of Health now has Cabinet responsibility for both uses, the administration and regulation of which will be conducted through different agencies – principally the new *Instituto Mexicano para la Regulación y Control del Cannabis* to be created for recreational use and the existing *Comisión Federal para la Protección contra Riesgos Sanitarios* (COFEPRIS) for medical use.

Business opportunities in the area of medical cannabis use could be very soon, followed by those in the area of industrial application of hemp, and finally those from the opening of the larger and wider space for recreational use. As we argued in our October newsletter: “We also see it [medical cannabis] as a valuable opportunity to test and run systems, establish supply chains, build relationships, gain access to authorizations, licenses, and permits by means of strategic alliances with Mexican partners, open sales channels and so on. In many ways, the *Reglamento* [regulations on use of medical cannabis] creates a pilot project space to prove the ability to create business opportunities, build carefully on brands that could then expand to the recreational use space when possible, and execute in the Mexican cannabis space. Strategic investment in medical cannabis now could pay significant dividends later when legalization of recreational use of cannabis comes into effect in Mexico.” ***We believe that this perspective and advice is even more valid now.***

/-----/

Monarch Global Strategies and Privus Capital

The steadily increasing commercial interest in cannabis, its derivatives, and ancillary products and services (for recreational and medicinal use) across North America creates business opportunities. Yet rapidly evolving legal and regulatory frameworks, which differ among jurisdictions, together with the associated complex domestic and cross-border politics, warrant careful analysis and well-planned strategies for entry into any aspect of the sector, especially for firms seeking cross-border partnerships, distribution channels, or investment opportunities.

Monarch Global Strategies LLC and Privus Capital, Inc. work together to help clients navigate this complex environment, offering unique skills, experience, and relationships to successfully expand into the legalized cannabis sector across North America.

Services include:

- Market entry support
- Risk analysis and strategic planning
- Match making for strategic partnerships, distribution agreements, start-ups, and M&A
- Private equity and corporate strategic investment
- Regulatory filings and trademark registrations
- Government relations, advocacy, and stakeholder engagement

To discuss business matters related to the emergent cannabis space in Mexico, contact us at:

Monarch Global Strategies

Gabriel Cavazos Villanueva

Senior Advisor

gcavazos@monarch-global.com

Privus Capital

Francisco Padilla

Managing Director

fpadilla@privuscapital.com

/-----/

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.