

Implementing Regulation in an Emerging Industry: A Multi-Province Perspective

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Abstract: The decriminalization of cannabis in Canada has required a host of regulatory changes at the federal, provincial, and municipal levels. Provinces have operationalized the development of legal markets in very different ways, offering an opportunity to perform comparative analysis of business responses. This article outlines and delineates the various regulatory frameworks that have been employed at the provincial level, discusses how they have impacted the development of the legal cannabis market, and considers how they have resulted in some further regulatory changes. After reviewing coevolution as a conceptual framework, the implementation of legalization of recreational cannabis is discussed, followed by an exploration of different provincial approaches at a general level. The effects of that framework on the first phase of legal market operations are explored, with a focus on issues emanating from regulatory choices through discussions of five regions: British Columbia, the Prairies, Ontario, Quebec, and New Brunswick; each section exemplifying different priorities in the regulatory choices. Several themes emerge in the discussion. First, provincial approaches to retail licence approval have created severe bottlenecks, affecting consumer access to legal recreational cannabis. Additionally, the regulatory framework for those licences has resulted in a chilling effect on many potential entrepreneurs. Second, a reduction in black market sales has not yet occurred, largely due to the failure of some provinces to adequately provide retail licences and support legal distribution channels, or to operationalize the retail sales network. Third, many provinces struggled with operationalizing wholesale distribution to the retail stores, initially leading to administrative restrictions on store licences. Finally, issues of fairness and equity, effective displacement of the illegal market, government's role as a market regulator and participant, and other issues that emerge from the critical comparison of the provincial markets are addressed.

Keywords: regulation, cannabis, entrepreneurship, socio-legal, business, provincial government, coevolution, strategy

Résumé : La décriminalisation du cannabis au Canada a nécessité une multitude de changements aux réglementations fédérales, provinciales et municipales. Les provinces ont procédé de manière très différente à la mise en place de marchés légaux, ce qui permet d'effectuer une analyse comparative des réactions des entreprises. L'article décrit les divers cadres de réglementation utilisés à l'échelon provincial, examine leurs incidences sur le développement du marché légal du cannabis et étudie le fait qu'ils ont entraîné d'autres modifications à la réglementation. Après avoir présenté la coévolution comme cadre conceptuel, l'article traite de la mise en œuvre de la légalisation du cannabis récréatif, puis analyse les différentes politiques provinciales de manière générale. Il étudie les effets de ce cadre sur la première phase d'opération du marché légal et, à cette fin, se concentre sur cinq régions : la Colombie-Britannique, les Prairies, l'Ontario, le Québec et le Nouveau-Brunswick. Chaque section illustre des priorités différentes dans les choix en matière de réglementation. Plusieurs thèmes ressortent de cette analyse. Premièrement, les politiques provinciales en matière d'approbation des licences de vente au détail ont créé d'énormes engorgements, ce qui a retardé l'accès des consommateurs au

cannabis récréatif légal. De plus, le cadre de réglementation applicable à ces licences a refroidi de nombreux entrepreneurs potentiels. Deuxièmement, les ventes sur le marché noir n'ont pas encore diminué, en grande partie à cause de l'incapacité de certaines provinces à délivrer des licences de vente au détail de manière adéquate, à soutenir les canaux de distribution légaux ou à organiser le réseau de vente au détail. Troisièmement, bien des provinces ont eu du mal à organiser la distribution en gros aux magasins de détail, ce qui a entraîné des restrictions administratives sur les licences des magasins. Enfin, l'article aborde les questions de justice et d'équité, le déplacement du marché illégal, le rôle de l'État en tant que régulateur du marché et participant à celui-ci, et d'autres questions qui se dégagent de la comparaison critique entre les marchés provinciaux.

Mots clés : réglementation, cannabis, entrepreneuriat, sociojuridique, entreprise, gouvernement provincial, coévolution, stratégie

Introduction

On 17 October 2018, the purchase and sale of recreational cannabis products became legal across Canada with the enactment of the Canadian *Cannabis Act*. The development of new regulatory frameworks and a new legal market for a previously illegal product within a mature economic system is a unique constellation of factors that might inform an understanding of the interplay between regulation and business strategy. In the Canadian context, some parallels exist between the development of regulations for the recreational cannabis market and the easing of prohibition-era restrictions on alcohol sales across the country. Indeed, both markets involve regulating formerly illegal products, which invoke important questions about public health and safety. However, the experience with recreational cannabis is different.

Canada was the second nation, and first G7 member, to legalize recreational cannabis. Canada is also the only nation with a federalist structure of government to create a legal market for the sale and use of cannabis products; Canada remains the only nation to have opened their market in this manner. In order to do so, federal and provincial governments had to establish concurrent regulatory frameworks governing the legal sale of products within the adult-use recreational cannabis market. These frameworks were created simultaneously among Canada's 13 provinces and territories, and were done so without the benefit of examples or market data from other jurisdictions to inform their development. The mandate to launch a market to be "open for business" in October 2018 is a compelling study because both federal and provincial governments simultaneously developed regulations; while at the same time and prior to understanding the scope and content of the regulatory landscape, early-stage entrepreneurs committed resources and developed the value chain to serve that market on opening day. For the entrepreneur, this is like developing a strategy for a football game before understanding the rules.

The Canadian story of cannabis regulation spans the twentieth century, and began with an extension of the social and moral reform movement which swept across Canada

in the early 1900s, into the regulation of drug and narcotic products. This history is tainted by racism, classism, and discrimination. The origins of cannabis prohibition can be traced to the aftermath of the 1907 Asiatic Exclusion League riots in Vancouver, and the publication of essays and screeds warning white Anglo-Canadians of the dangers of immoral liaisons with people of different races and ethnicities, as well as reflecting a young country's desire to participate in a series of international treaties and to harmonize its laws with those of other nations.

The production, sale, possession, and use of cannabis was illegal across Canada for 95 years. Canadian drug policy was dominated by a prohibitionist outlook for most of that time, and a gradual shift in tone from a prohibitionist mindset—having its origins in the temperance movement—to a regulatory mindset, which attempts to balance competing concerns of public health and individual rights. While there were several attempts to loosen prohibitions and restrictions over that time period, it has only been since the beginning of the twenty-first century that Canada has forged a regulatory framework to allow for the legal sale and consumption of cannabis products.

The Canadian experience of transitioning from a prohibition to a regulation mindset is an important one. Canada remains the world's first advanced economy to legalize cannabis. Canadian companies engaged in the legal production of cannabis have developed strong innovations in the cultivation and refinement of their products. That intellectual property has far reaching implications beyond this industry. Canadian policymakers, licensed producers, and researchers have advised other governments on developing approaches toward regulatory reform. The lessons of quickly framing and operationalizing a legal market within a federalist system of government have far-reaching implications. Effectively, Canada simultaneously created 13 distinct emerging economies within a mature economic framework. Each of those 13 distinct economic models approached opening their markets somewhat differently, but all of them did so at the same time. As a result, firms seeking to participate in the market had to develop entrepreneurial strategies which evolved in concert with that process, and those with national ambitions needed to develop multiple, parallel strategies.

For entrepreneurs seeking to participate in the Canadian cannabis market, this process has been a confusing one, which has impacted the lifecycle and viability of their businesses. Entrepreneurs have faced significant ambiguity around licensing and regulation processes for retail operations, supply chain constraints and production delays that have impacted their business models, local zoning controls that have made it difficult to establish traction in local markets, as well as inconsistent regulatory frameworks across provinces which have impacted their ability to scale operations.

For policymakers seeking to regulate the Canadian cannabis market, the lessons have been profound as well. Provincial governments have adapted systems and processes for participating in the supply chain and subsequently determined that some of those systems

and processes do not translate well from one regulated industry (such as alcohol) to another learning that they need to iterate and adapt regulations and procedures to manage their markets. Each of those markets has a distinctive local flavour that is informed by the unique cultural and geographic context of the provinces and territories. In many ways, the story of opening the legal recreational cannabis market across Canada is a case study on simultaneously developing public policy and entrepreneurial strategy in a coevolutionary manner.

To make sense of the story, this article briefly traces the historical background of cannabis regulation and delineates the contour of the current regulatory framework across Canada, discusses the effects of that framework on the first phase of legal market operations, offers five vignettes of early-stage development in different provincial markets, and finally, offers some thoughts about what is to come.

The Dynamics of Coevolution as a Conceptual Framework

The path toward developing regulations to create a legal market for the sale of adult-use recreational cannabis has spurred great interest in the academic community. There have been a series of research symposia, conference panels, articles, and courses dedicated to examining that process. A special issue of *Canadian Public Administration* in 2019 contained articles exploring the issues around indulgence-based excise taxes (Bird, et al. 2019), applying social learning theory to understand provincial variations in policy development (Train and Snow, 2019), examining the shift in approaches between policy development and evaluation among the provinces (Wesley and Salomons, 2019), describing the policy shift from prohibition to regulation (Wesley, 2019), and determining the socially optimal price for cannabis products (Childs and Stevens, 2019).

This emerging literature has been echoed in public health discourse (Haines-Saah, et al. 2019; Watson, et al. 2019), in law (Habibi and Hoffman, 2017; Koutouki and Lofts, 2018), and in interdisciplinary studies, including a volume edited by Potter and Weinstock (2019) *High Time: The Legalization and Regulation of Cannabis in Canada*, that contains chapters written by both practitioners and scholars from an interdisciplinary perspective. Yet, while there has been robust development of a scholarly literature in these disciplines, the same cannot be said for entrepreneurship and management sciences. Despite the excitement among researchers outlined above, we found surprisingly little research from the perspective of business, in striking contrast to the extensive and insightful publications of public health, political science, and legal researchers. We conducted a systematic search of the top two research databases of peer-reviewed journals in business, using a series of search terms to find peer-reviewed articles. A search of ABI Business Premier Collection resulted in higher numbers of results: using only “cannabis AND Canada AND business” resulted in 338 peer-reviewed articles, which reduced to 137 articles since 2017 (covering

the period of legalization) but reduced to 30 articles if we removed health related articles. A search of EBSCO Business Source Premier resulted in 9 peer-reviewed articles, all of which were published since 2017, reduced to 7 articles when we removed health related topics. A close scan of the articles in either dataset showed these articles are solely concerned with legal, taxation, and accounting concerns, and not related to strategy, business model development, or entrepreneurship and new business start-ups. Some promising work is emerging at recent conferences, most notably a panel discussion at the 2019 Administrative Sciences Association of Canada annual meeting, yet the published literature about cannabis related business is very scant.

Thus, to understand the interaction between emerging policy and emerging markets from a business perspective, we focused on content analysis of public discourse, integrating grey literature and personal communications with industry stakeholders to understand the first year of legalization. The breadth of sources included conversations with knowledgeable stakeholders, grey literature sourced from conference presentations, StatsCan data, and media coverage in the national business and local press. In this article, we integrate the perspectives of these sources to create portraits ([Lawrence-Lightfoot, 2005](#)) that illuminate the broader dynamics of the recreational cannabis market and provincial regulation, and posit that the portraits are examples of the coevolutionary processes of market development.

Coevolution refers to the simultaneous evolution of an entity and its environment, whether those entities are organisms or organizations ([Baum and Singh, 1994](#); [Porter, 2006](#)). The theory of coevolution was introduced in the natural sciences as a framework for understanding the dynamic and simultaneous genetic evolution of butterflies and plant species within their contextual habitat ([Ehrlich and Raven, 1964](#)). As one species adapts, the other species also adjusts and adapts, creating a symbiotic and interrelated dyad with complex interdependencies. This mutual evolution demonstrates how changes in one entity produce responsive changes in another, and vice versa. In a coevolutionary process, distinct actors (e.g., individual entities, species, stakeholders) mutually influence each other's evolutionary paths ([McKelvey, 2002](#); [Pacheco, et al. 2014](#)). The theory has been extended across the management sciences ([Haverman and Rao, 1997](#); [Lampel and Shamsie, 2003](#); [Volberda and Lewin, 2003](#)) to explain the bi-modal and evolutionary patterns between companies and their environments that shape their context ([Dieleman and Sachs, 2008](#)).

While coevolution theory has been applied to understand firm and market behaviour in a variety of industries and contexts, it has not yet been extended to examine the development of the legalized cannabis industry. In large part, this is due to the fact that legalization of cannabis is a relatively new phenomenon and both firms and markets are still in the formation to early-growth stage. One of the interesting effects that is discoverable through a coevolution lens is that some early market regulatory barriers become the basis

for opportunity identification, as entrepreneurs develop business models and strategies to find ways around regulatory boundaries. There are early examples of this activity: in Alberta, existing licensed producers who are permitted to sell to the provincial cannabis wholesaler Alberta Gaming, Liquor and Cannabis (AGLC) are now building a new source of revenue by leveraging their licence to provide an access point for newer craft producers to sell into the supply chain; in Saskatchewan, unique regulations on the transportation of cannabis products led to an Ontario firm to develop a third-party compliant delivery service for retail stores, with the potential to expand operations to other provinces as regulations evolve. These business opportunities emerged because barriers in the regulatory framework prevented 'normal' business practices and entrepreneurs within the industry responded with work-around strategies. As those strategies mature, regulations across the country are likely to evolve as one component of the system (i.e., another province) observes and adopts successful practices from another. In turn, these changes will lead entrepreneurs to adapt and extend their strategies across the country.

The Regulatory Framework: Provincial Differences

In Canada, the regulation of cannabis follows a familiar pattern. Like alcohol, cannabis was legal and largely unrestricted when the Dominion of Canada was formed by confederation in 1867. For the next 56 years, cannabis remained legal at the federal level. Cannabis was first prohibited by the Canadian government in 1923, when it was added to the schedule of narcotic drugs prohibited under the *Opium and Narcotic Drug Act* of 1920 (Hewitt, 2004). Several iterations of regulation occurred between 1923 and 2000 until, in 2000, the production, possession, and use of cannabis for medical purposes was deemed a constitutionally protected right. From 2000 until 2018, the legal status of cannabis shifted as regulations were modified to reflect greater recognition of individual rights and liberties, and a legal market of licensed producers became established. In 2018, recreational use of cannabis became legal across Canada. Cannabis was a fully prohibited substance for 77 years in Canada, and, subsequently, a restricted and regulated substance for 18 more years. Over that period of time, the context for the regulatory framework changed dramatically.

Canada has developed a two-tier regulatory framework for the production, sale, possession, and use of cannabis products. Permitted use can either be medical (legalized in 2001, and regulated solely by the federal government) or recreational (legalized in 2018, with regulatory jurisdiction shared between federal and provincial governments, and with many provincial powers delegated to municipal governments). Regulation of cannabis used for medical purposes is exclusively the jurisdiction of the federal government, and medical use of cannabis is governed by regulations issued by Health Canada. Those regulations, which originally only allowed individuals to grow their own cannabis, were expanded in 2013 to allow for the development of a legal production industry.

In contrast to the federally controlled and regulated medical cannabis market, regulation of the recreational cannabis market is operationalized at three levels—federal, provincial, and municipal. This is reflective of Canada’s approach to allocating government powers within the structure of confederation. Section 91 of the *Constitution Act* 1867 provides that the federal government has jurisdiction over the regulation of trade and commerce. Section 92, known colloquially as the “property and civil rights clause,” provides that provincial legislatures have jurisdiction over property and civil rights in the province. The provincial authority outlined in Section 92 has been construed to extend over the regulation of matters of contract and provides a warrant for the exercise of provincial authority in regulating markets. Municipal powers are delegated from provincial governments, and generally include jurisdiction over local land use, zoning, and licensing issues. The *Cannabis Act* enacted in 2018 established the legal framework for the sale of adult-use recreational cannabis products throughout Canada, consistent with these constitutional principles.

Much of the regulation of the adult-use recreational cannabis market builds on the foundation established in the context of medical cannabis, as the regulatory infrastructure already existed. Those areas include the regulation of production, product tracking, and controls on advertising and marketing. In accordance with provincial authority under Section 92 of the *Constitution Act*, the *Cannabis Act* provides that each provincial or territorial government has the authority to determine how retail sales of cannabis products are regulated within their jurisdiction. Municipal governments exercise control over retail location, hours of operation, licensing, and other operational aspects of business activity through their power to regulate land use, zoning, and business licensing requirements via local ordinances. [Table 1](#) details the nature and scope of regulatory control exercised at each level of government.

Each province has operationalized the regulation of their local markets somewhat differently, and provincial regulations were developed concurrently in 2017 and 2018. Because existing examples for legal recreational cannabis markets are limited, the provinces had to determine a number of regulatory factors without the benefit of examples from outside Canada. In the United States, cannabis is still illegal at the Federal level and only two states (Washington and Colorado) allowed legal, recreational sales at that time. The only other nation that had legalized cannabis in 2018 was Uruguay, which does not have a federal structure, and with a population of just over 3 million people, is a much smaller market.

While the provinces developed their regulatory frameworks at the same time, they did so informed by the direction their counterparts were taking. Each provincial market has developed a regulatory structure around four distinct pieces of the cannabis industry supply chain: Licensed Producers, who are approved, licensed, and regulated by the federal government; Wholesale Distributors, who are regulated by each provincial government; Retail Sales Outlets, which are the mechanism through which direct to consumer sales are made; and, Ancillary or Related Businesses, which do not directly sell cannabis products,

Table 1. Division of Regulatory Roles and Responsibilities

Activity	Federal	Provincial	Municipal
Possession Limits	X		
Trafficking	X		
Advertising & Packaging	X		
Medical Cannabis	X		
Seed-to-sale tracking system	X		
Production (cultivation and processing)	X		
Distribution and Wholesale		X	
Retail Sales Model		X	
Retail Locations and Rules		X	X
Regulatory Compliance	X	X	
Land Use/Zoning		X	X
Taxation	X	X	X

but participate in and support the market. In each case, provincial legislatures also had to determine: (1) whether to play an active role in the market beyond serving as a regulator; (2) whether to allow brick-and-mortar retail sales; (3) what the minimum age to purchase or consume cannabis products should be; and (4) whether to allow in-home cultivation of cannabis plants.

There are three regulatory models for the recreational cannabis market in Canada: a government-operated model (Quebec, Nova Scotia, New Brunswick, Prince Edward Island (PEI), Northwest Territories (NWT)), where the government is the sole supplier of recreational cannabis products; a private market model (Saskatchewan), where the government has taken the role of a regulator, but not as a market participant; and a hybrid model (British Columbia (BC), Alberta, Manitoba, Ontario, Newfoundland, Yukon, Nunavut), where the government takes control of—and participates in—some aspect of the market supply chain. [Table 2](#) details the regulatory models by province.

As [Table 2](#) demonstrates, initial provincial approaches to regulation were somewhat regional in nature. The system in BC and the Prairies largely mirrors the regulatory system for alcohol sales, and provinces have approved relatively large numbers of retail licences. Ontario has a model similar to Alberta, but has strictly regulated the number of licences issued, as has Newfoundland and Labrador. Quebec and the Maritimes largely employ tight government market control, where the government has been the sole supplier of recreational cannabis products to consumers. The territories have a mixed approach to regulatory frameworks, with the NWT resembling the approach favoured in the Maritimes; while Nunavut and Yukon mirror the regulatory framework adopted by BC.

Table 2. Initial Regulatory Framework by Province

	Wholesale	Brick & Mortar Retail	Online Retail	Minimum Age	Grow Your Own
BC	Government	Hybrid (Government and Private)	Government	19	4 plants
Alberta	Government	Private	Government	18	4 plants
Saskatchewan	Private	Private	Private	19	4 plants
Manitoba	Government	Private	Private	19	Not Permitted
Ontario	Government	Private	Government	19	4 Plants
Quebec	Government	Government	Government	18	Not permitted
New Brunswick	Government	Government	Government	19	4 plants
Nova Scotia	Government	Government	Government	19	4 plants
PEI	Government	Government	Government	19	4 plants
Newfoundland & Labrador	Government	Private	Government	19	4 plants
Yukon	Government	Hybrid (Government and Private)	Government	19	4 plants
NWT	Government	Government	Government	19	4 plants
Nunavut	Government	Hybrid (Government and Private)	Hybrid (Government and Private)	19	No restriction

Source: Provincial Legislation

Notably, and unlike the development of state-level markets in the US, the development of private firms engaged in Canadian markets was not hindered by considerations about how to operationalize banking or payment systems, or whether capital could be raised via equity markets or through traditional bank loans. Despite that fact, significant barriers existed for early-stage entrepreneurs seeking to participate in the emerging legal marketplace. Many entrepreneurs with substantial experience in the cannabis industry developed that experience in the illegal market; others did not have ready access to sufficient capital during what was often a lengthy and uncertain regulatory approval and licensing process. Those individuals seeking to transition from the illegal to the legal market, a stated goal of policy and regulatory reform, faced difficulty in doing so, as a conviction for a drug-related offence would bar them from eligibility for a licence. Federal restrictions around supply, advertising, storage, and seed tracking also impacted the ability of early-stage entrepreneurs to participate in the market.

The Market Framework: The Supply Chain

The development of entrepreneurial strategy is influenced by a combination of factors, including both regulatory frameworks and the structure and dynamics of an industry supply

chain. The regulatory frameworks describe the contours and boundaries within which firms are able to operate, and the supply chain provides a structure for those interactions. The manner in which these regulations shape that structure creates both opportunities and barriers for a firm seeking to engage in business activity. In order to understand the impact of regulation on an industry, it is necessary to understand the supply chain.

The cannabis supply chain has four major components: Licensed Producers, Wholesale Distributors, Retail Sales Outlets, and Related Businesses. Regardless of the regulatory framework established in each province, the components of the industry supply chain do not change, only the manner in which that supply chain develops and operationalizes within a regulatory framework. Entrepreneurs seeking to participate in the market will make strategic decisions based on the regulatory framework that is established within each province, differences between provinces will impact a firm's strategic decisions related to pursuing or scaling operations beyond that province. This section outlines the supply chain taxonomy that describes the market and discusses some global perspectives on issues within that framework. Note that while the supply chain also includes end-user consumers, they are excluded from this analysis.

Licensed Producers

A licensed producer is an individual or firm that possesses a government licence to grow, harvest, dry, trim, cure, and package cannabis. Given that a robust regulatory framework for production of cannabis products was developed for the medical-use market, licensed producers continue to be primarily regulated by the federal government, and the market that they can sell to is highly regulated and controlled. The *Cannabis Regulations* specify that a federal licence is required to cultivate, process, and sell cannabis for medical or non-medical purposes. Firms seeking to become a licensed producer of cannabis products can apply for a variety of different licence types based on the type of business opportunities they wish to pursue. For example, they can apply for a standard cultivation licence (intended for large scale bulk sales of cannabis products), a micro-cultivation licence (intended for artisanal or craft production), or a nursery licence (intended for starting material, such as seed or seedling sales). Licensed Producer designation types are also available for processing, testing, and research operations. Applicants may apply for and receive more than one type of licence.

Wholesale distribution is both a government monopsony (where the government is the only buyer of goods or services) and a government monopoly (where the government is the only seller of goods or services) in every province but Saskatchewan. As a result, licensed producers bulk-sell their products to an extremely small customer base of wholesale distributors in the adult-use recreational market, who then have the power to sell products to whichever retail entities they regulate and approve. Licensed producers also have the ability to sell small quantities of products directly to medical-use customers

for personal use. In addition, they have the ability to sell to the medical use and research export market, but not the recreational export market.

The relatively small size of both the production market and the consumer market has a significant impact on supply and pricing within the industry. As government-organized wholesale distributors typically enter into approved purchasing contracts with only a few licensed producers, the wholesale supply is dependent on a given producer's ability to meet demand, and price elasticity is somewhat inflexible given constraints on the number of alternative outlets for either producers or suppliers. Additionally, further sales restrictions exist under the federal government's *Cannabis Regulations*, as licensed producers may only export cannabis for medical or research purposes. Export limitations place significant restrictions on the ability of firms to capitalize on research and development innovation and export domestically produced products in order to satisfy potential external market demand. In order to export product for recreational use, the *Cannabis Act's* limitations on export authorization would have to be modified, as would several treaty regimes Canada is a signatory to. As a result, larger licensed producers are beginning to invest in offshore production capacity and domestically service consumer demand in jurisdictions where the legal status of cannabis is changing; several have developed foreign branch and subsidiary operations. Doing so allows them to operationalize the knowledge and intellectual property they have developed within Canada while avoiding Canada's export restrictions. However, their primary market is a domestic one, and they are therefore induced to set entrepreneurial strategy and scale operations based on their forecast for market potential in a largely closed economic system.

Within the domestic adult-use recreational cannabis market, licensed producers faced significant issues during the first year of legal sales as provincial wholesale distributors became established and the regulatory framework operationalized. Those challenges looked different at various points as the early-stage market developed. In the initial phase of the market, as licensed producers built capacity for bulk sales, production delays and supply shortages impacted the ability of licensed producers to bring product from seed to market. Additional delays, result from not having access to government mandated excise stamps, and further delays as the sole authorized government supplier of excise stamps manufactured the stamps without glue to adhere to saleable products, further delayed supply at this stage.

As supply production delays were resolved at licensed producer facilities and they began to scale operations to meet anticipated market demand estimates, a second phase of market bottleneck emerged as provincial wholesalers were not adequately prepared to accept and distribute high volumes of bulk cannabis products. This was due to several factors. First, provincial wholesalers needed time to develop internal processes and procedures, hire and train staff, establish relationships and negotiate contracts with both producers and retail operators, and integrate systems for receiving, shelving, inventory

control and management, and shipping products. In addition, wholesalers faced significant pressures in determining consumer demand for products in the retail market, as no reliable market data existed. Further, the wide disparity among provincial market models in terms of operating and/or regulating both wholesale suppliers and retail stores also impacted the market.

Wholesale Suppliers and Distributors

In 2018, each of Canada's thirteen provinces and territories had to determine how cannabis products would be distributed at the wholesale and retail level within their respective jurisdictions. The provincial frameworks for wholesale distribution took one of four forms: in the first (Quebec, New Brunswick, Nova Scotia, PEI, and NWT) the government ran the entire recreational cannabis market and managed both wholesale and brick and mortar (storefront) retail distribution. In the second (Alberta, Manitoba, Ontario, and Newfoundland) the government managed wholesale distribution, but licensed private sector companies to establish and operate retail stores. In the third (BC, Yukon, and Nunavut) the government managed wholesale operations, and applied a hybrid model to the operation of retail stores, allowing for both the government and private sector firms to establish and operate retail stores. In the fourth, (Saskatchewan), the government simply regulated a private market at both the wholesale and retail level. Online retail sales were managed by the government in every jurisdiction other than Saskatchewan, Manitoba, and Nunavut, who allowed private firms to provide and fulfill online sales.

With the exception of Saskatchewan, each province or territory has retained control over wholesale distribution and determines which, and how many, licensed producers the wholesale entity will contract with in order to supply cannabis products. As such, the provinces have control of the market through crown corporations they established and are free to both dictate regulatory frameworks and supplier contracts, as well as exert pressure over pricing. Most provinces have contracted with only a few licensed producers to meet demand for both dried cannabis and cannabis extract products. When each provincial wholesale operation commenced in October 2018, each experienced similar issues in creating both the regulatory and physical infrastructures needed to: establish an order processing, fulfillment, and distribution system; monitor supply; predict inventory needs; and determine the market cycle. As the majority of provinces are the sole source of wholesale product available to be distributed to retail outlets, they also exert control over retail market dynamics. These include determining who can be an authorized retailer, the quantity and type of product available for sale for each retailer, pricing considerations, and how retailers place and receive product orders.

Government management of the wholesale distribution network has largely been blamed for delays in the development of a stable recreational market in many provinces with private retail businesses. Government control of the wholesale market and

bottlenecks associated with that control have been roundly criticized in the media, the market, and the cannabis industry. Provincial authorities, who may not have wanted to be in the position of being a market participant to begin with, are looking to modify the regulatory model at the wholesale level.

Brick-and-Mortar Retail Operations

The third link in the supply chain is the retail operation segment, composed of both brick-and-mortar and online sales outlets. Online retail sales are managed by the government in all provinces other than Saskatchewan and Manitoba. In the first year of the market, online sales were not only a small percentage of total annual retail sales but were also a strongly declining percentage over time—as the brick-and-mortar retail store network evolved, the percentage of online sales diminished ([Statistics Canada, 2019](#)). Therefore, we focus on the brick-and-mortar retail store segment in this analysis.

As noted above, the model in some provinces is a government-operated store structured along the lines of existing government-run retail alcohol operations, monopolizing the market. Where private-sector adult-use recreational cannabis stores were allowed to operate, a mixture of retail chains and independent one-store businesses emerged to serve the market. Qualifying for a licence as a cannabis retailer was both risky and difficult; entrepreneurs seeking a licence were required to expend significant financial resources to identify locations compliant with municipal rules, pay for property leases for months while awaiting the licence, complete extensive and detailed renovations to upgrade the facilities for security concerns (including a “bank” vault for overnight storage), block the view of the store interior, create an effective customer experience on the inside, and finally await inspections and approvals before opening for business. Clearly, patient capital was needed throughout this process, regardless of whether the entrepreneurs were young entrepreneurs opening a single shop, or larger companies working on building a retail chain. In the early phase of legalization, the time required could be as much as one year from commitment of capital to acquisition of the licence, without any guarantee that a licence would be granted.

The regulations prohibit retail licensees from operating in the same manner other retail businesses might choose to organize. This can have important consequences for whether and how entrepreneurs approach engaging in the market. For example, unlike other industries, provincial cannabis regulations generally do not allow a licensed producer to create a vertically integrated company, which would afford a firm the opportunity to establish its own retail chain. This impacts the ability of firms to leverage and maximize capital in an efficient manner. Some provinces also severely limit the ways a joint merchandising and stock management strategy can be used to build brand identity or manage costs. Retail chains already face limitations based on geography, for example, the sheer distance between population centres in the Prairies is a natural barrier to efficiency. But

firms in some provinces also face regulatory limitations that impact their business models. In Alberta, provincial restrictions on transferring product between stores prevent chains from efficiently managing their stock and ensuring the right product mix for their local customer demographic.

The difficulty of firms in most provinces to become licensed retail stores is also a considerable issue. Prior to legalization, many entrepreneurs operated smoke shops that sold cannabis paraphernalia, and many were expected to become licensed retailers. In fact, very few have converted; the reasons proffered include lack of capital, location restrictions that disqualify their current shop, or risk aversion. Similarly, provincial regulations that prohibit market participation by an individual who may have had a drug-related criminal conviction prior to legalization have further raised questions regarding equity and access.

Ancillary Businesses and Services

As an industry matures, an ecosystem of supporting businesses emerges to fill in the gaps within the market. Often, these businesses help the supply chain succeed by finding ways to work within the regulations, and in some cases, around the regulations.

One of the earliest support services for the supply chain that emerged was certification for employees to work in the licenced producer (LP) facilities. The certificates were offered in community colleges (public institutions), and trained employees to understand cannabis growing and compliant handling of product and related agricultural waste. In the retail part of the supply chain, companies seem to be handling training in house. There is an appetite among consumers for more knowledge, especially among older consumers who have never consumed cannabis, or who have not done so for some time. Thus, certification for cannabis sommeliers has grown in popularity, creating legitimation for people who create education events disguised as pairing events with beverages and/or food.

Marketing cannabis products or cannabis retail stores is challenging because federal regulation disallows a wide range of options. Cannabis marketing cannot appeal to children and youth, cannot be associated with exciting activities or lifestyles, and cannot use people's images. This makes popular associations with cannabis off limits. The industry has developed some ways around this regulation. For example, a digital marketing company is working with LPs and retailers across the country to attract people by targeted messaging in online postings, which directs them to websites that are not actually the clients' company websites, and from there, enables direct marketing to people who express an interest in cannabis products. In addition, the use of social media influencers or celebrity endorsements is somewhat of a grey area.

Similarly, federal regulations of cannabis packaging specify the detail and design of cannabis products designated for consumer use. Regulations require specific information, and allow the retailer little to no flexibility around layout or design. The THC (tetrahydrocannabinol) warning symbol is by regulation larger than the LP brand image,

and is intentionally designed to be quite unappealing. This packaging regulation limits the ability to build a brand identity at the point of sale (POS), unlike most consumer products one sees in a pharmacy or supermarket. No images of people or plants are allowed; brands are not allowed to distinguish their products by using visually interesting or appealing design. Compared to the POS marketing and packaging of US products, Canadian cannabis products look boring. This has required Canadian firms to differentiate their marketing strategy from their North American neighbours. Brand image for LP product lines have to be developed differently, and generally a clear focus on the product quality itself is the best way to create a brand reputation that allows them to build a loyal following and to improve profit margins. It will be interesting to see what other strategies emerge to support LPs with workarounds, or whether product packaging restrictions ease.

Other business concepts related to the supply chain include event management firms, consulting firms that assist producers and retailers in complying with age-gated websites and avoiding illegal content, delivery services, and other creative business models entrepreneurs are using to enter the industry.

The Impact of Regulation on Market Activity

As detailed in the previous two sections, governments make choices in framing market regulations that have a significant impact on the development of that market. The particular regulatory framework used by a government provides the mechanism through which firms assess business opportunities and develop entrepreneurial strategy. In new markets, the creation of both nascent regulatory frameworks and nascent business strategies often occurs simultaneously, and those efforts typically do not have benefit of prior industry knowledge, experience, or a predictable sense of the market. That is certainly the case in the Canadian adult-use recreational cannabis market.

The timing of regulatory development, and the creation or adaption of government infrastructure to manage the regulatory process, impacts the ability of markets to form and businesses to develop both entrepreneurial strategies and efficient operations in order to participate in that market. In the first year of legalization, there were a number of structural bottlenecks in that process. Provincial markets across Canada faced significant delays in developing and operationalizing the wholesale supply chain and in creating a system for the approval and issue of retail store licences. Delays in the creation of clear and market-oriented regulations for ancillary businesses impacted the ability of the markets to fully develop during the first year. The significant ambiguity around the timing of regulatory approvals, the availability of finished goods to be supplied to and sold through provincial wholesalers, and the fragmented development of municipal zoning regulations and business licence approvals all had negative consequences for the market.

Table 3. Population, Number of Retail Outlets, Sales Data, and Percentage of Market Share by Province

	Population (Q3 2019 est.)	Number of Brick- and-Mortar Retail Outlets (Dec 2019)	Population per Retail Outlet	Provincial Percentage of National Population	Provincial Percentage of Retail Outlets
BC	5,071,336	91	88,971	13.5%	17.0%
Alberta	4,371,316	255	24,837	11.6%	47.7%
Saskatchewan	1,174,462	37	33,556	3.1%	6.9%
Manitoba	1,369,465	27	59,542	3.6%	5.0%
Ontario	14,566,547	18	606,939	38.8%	3.4%
Quebec	8,484,965	34	471,387	22.6%	6.4%
New Brunswick	776,827	21	36,992	2.1%	3.9%
Nova Scotia	971,395	13	74,723	2.6%	2.4%
PEI	156,947	5	39,237	0.4%	0.9%
Newfoundland & Labrador	521,542	25	20,059	1.4%	4.7%
Yukon	40,854	3	10,214	0.1%	0.6%
NWT	44,826	6	7,471	0.1%	1.1%
Nunavut	38,780	--		0.1%	0.0%
Total	37,589,262	535	92,357	100%	100%

Source: Statistics Canada; Bloomberg

This section presents three tables. [Table 3](#) details the number of brick-and-mortar retail outlets on a provincial level and references the provincial population at the same time. [Table 4](#) organizes sales data from the first year of market operations by province and calculates each province's percentage of overall market share. [Table 5](#) illustrates the growth in the retail store ecosystem from December 2019 to April 2020.

As noted in [Table 3](#), there were 535 brick-and-mortar retail recreational cannabis stores across Canada in December 2019. The distribution of retail stores was widely disparate, and the variance clearly reflects the impact of provincial regulation on the market. In provinces where the government has chosen to employ a less restrictive regulatory approach to issuing retail licences (Alberta, Saskatchewan, and Manitoba) the ratio of retail outlets to population was fairly high, suggesting that by the end of the first year of legal operations, the market was relatively well-served in its initial stages. It should be noted that, in Alberta, the AGLC issued a moratorium on new licence issuance for several months given supply chain constraints, which impacted and delayed the development of the retail store network. Despite that moratorium, Alberta led the nation in the total number of retail stores established in the first year of the legal market. By comparison, Quebec and

Table 4. Number of Retail Outlets by Population, Sales Data, and Percentage of Market Share by Province

	Population (Q3 2019 est.)	Number of Brick- and- Mortar Retail Outlets (Dec 2019)	B&M Sales (\$) (Oct 2018-Sep 2019)	Sales Per Capita (\$)	Sales Per Retail Outlet (\$)	Provincial Percentage of Market Share
BC	5,071,336	91	49,659,000	10	545,703	5.5%
Alberta	4,371,316	255	195,740,000	45	767,608	21.6%
Saskatchewan	1,174,462	37	38,165,000	32	1,031,486	4.2%
Manitoba	1,369,465	27	56,103,000	41	2,077,889	6.2%
Ontario	14,566,547	18	216,807,000	15	12,044,833	23.9%
Quebec	8,484,965	34	194,865,000	23	5,731,324	21.5%
New Brunswick	776,827	21	37,905,000	49	1,805,000	4.2%
Nova Scotia	971,395	13	65,805,000	68	5,061,923	7.3%
PEI	156,947	5	15,216,000	97	3,043,200	1.7%
Newfoundland & Labrador	521,542	25	30,615,000	59	1,224,600	3.4%
Yukon	40,854	3	4,216,000	103	1,405,533	0.5%
NWT	44,826	6	2,737,000	61	456,167	0.3%
Nunavut	38,780	--	--		0	--
Total	37,589,262	535	907,833,000	24	1,696,884	100%

Source: Statistics Canada; Bloomberg

Ontario, both provinces that deliberately restricted licence issuance and/or the number of retail stores, clearly underserved potential consumer demand given the low ratio of retail stores to population. Regional geography also plays a role: the Maritimes, for example, have government-run retail stores serving smaller overall populations that are highly concentrated. By comparison, the Prairies have privately run retail stores established throughout provinces with a more diffuse population distribution.

Table 4 delineates first year market sales data at a provincial level. The data suggest that the relatively diffuse nature of Alberta's brick-and-mortar retail store network served the market fairly well, as per-capita and total sales in Alberta were quite high relative to other provinces. Similarly, per-capita data from Saskatchewan and Manitoba suggests that the market was relatively well-served. By comparison, while Ontario and Quebec both had higher overall sales numbers, their per capita sales are quite low, reflecting an undersupply of retail outlets and, perhaps, inadequate coverage based on geographical distribution. Per capita numbers were quite high in the Maritimes, Newfoundland, and the territories, reflecting the unique characteristics of these relatively small regional markets. In BC, both total sales and per capita sales numbers suggest that the legal market was

Table 5. Growth in Retail Store Ecosystem: December 2019–April 2020:

	Population (Q3 2019 est.)	Number of Brick-and- Mortar Retail (Dec 2019)	Provincial Percentage of Brick-and-Mortar Retail (Dec 2019)	Number of Brick-and- Mortar Retail (April 2020)	Provincial Percentage of Brick -and- Mortar Retail (April 2020)
B C	5,071,336	91	17%	177	20.8%
Alberta	4,371,316	255	47.7%	436	51.4%
Saskatchewan	1,174,462	37	7.0%	42	4.9%
Manitoba	1,369,465	27	5.1%	30	3.5%
Ontario	14,566,547	18	3.4%	52	6.1%
Quebec	8,484,965	34	6.4%	41	4.8%
New Brunswick	776,827	21	4.0%	20	2.4%
Nova Scotia	971,395	13	2.5%	12	1.4%
PEI	156,947	5	0.9%	4	0.5%
Newfoundland & Labrador	521,542	25	4.7%	25	2.9%
Yukon	40,854	3	0.6%	5	0.6%
NWT	44,826	6	1.2%	5	0.6%
Nunavut	38,780	--	--	0	0.0%
Total	37,589,262	535	100%	849	100%

Source: Statistics Canada; Bloomberg

both underserved by the number of retail outlets and that the conversion rate of customers purchasing from illegal black market outlets to legal outlets lagged. To some extent, those concerns are echoed across Canada.

Table 5 depicts the change in the number of retail stores within each province between December 2019 and April 2020, reflecting significant changes in policy and implementation that occurred during the first quarter of 2020. This review period was chosen to evaluate what we anticipated would be a rapid increase in the number of brick-and-mortar stores across several Canadian provinces, a prediction that has been subject to revision due to the COVID-19 pandemic. The data in table 5 suggest that the retail market has begun to scale, as bottlenecks and delays smoothed out in some provinces. This was particularly true in BC, Alberta, Ontario, and Quebec, where the ecosystem began to take greater shape.

Between December 2019 and April 2020, the number of retail stores in BC rose from 91 to 177. In Alberta, the number went from 255 to 436. In Ontario, the number of stores rose from 18 to 52. In Quebec, the change was 34 to 41. Retail store growth in Saskatchewan and Manitoba was more modest, at roughly 20% and 33%, respectively. Other provinces had negligible changes.

As regulatory processes continue to mature and the process of assessment, evaluation, and revision moves through several cycles, we anticipate that regulators and market participants will continue to coevolve their respective interactions, developing a more mature industry framework. In order to further understand the interplay between provincial regulation and entrepreneurial strategy, we developed regional portraits of early-stage markets, which are contained in the next section.

Regional Portraits of Markets

We created these portraits, or mini-cases, of regional markets by conducting an extensive content analysis of published media reports about the emerging adult-use recreational cannabis market. We then participated in extensive conversations with stakeholders, many of whom were also guest presenters in a special topics course offered at a university in 2019 and 2020. Drawing on this material, we developed portraits focused on five provinces or regions, moving west to east across Canada. We were intentional in choosing to include these regions, as each offers a unique perspective. BC was selected because the recreational cannabis market before legalization was conducted openly in store fronts and farms, with minimal repercussions for the entrepreneurs. The move to legalization represented a significant increase in restrictions on a long-established and pervasive grey and black market. The Prairie provinces are grouped together as they all chose more supportive, pro-business regulations launched from the beginning within a strong regulatory framework that emphasized community safety and a commitment to displacing the illegal market. Within the Prairies, Alberta also stands out as the province with the largest number of retailers, per capita and in absolute numbers, at the end of the first year of legalization. Ontario has particular interest because of the impact of delays in licence issuance and other regulatory changes due to a change in government, and how chaotic implementation of legalization negatively impacted entrepreneurs seeking to make long-term investments. The story of Quebec, which combined a sluggish start to opening a retail market with a move toward greater restrictions on the minimum age to purchase and consume cannabis products, represents a disconnection between policy goals and outcomes, as a more restrictive framework may lead to greater participation in the illegal market. We chose New Brunswick to explore the challenges of government retail distribution, and their subsequent plan to switch to a concessionaire model that is essentially the same structure as Cannabis NB (the provincial crown corporation) but operated by a private company. Collectively, the portraits illuminate the dynamics of the first year of legalization, as the market grew and both government and business decisions coevolved. These five cases let us explore the trade-offs and tensions in legalizing, regulating, licensing, controlling, and operating the recreational market.

British Columbia and the Transition from Grey Market Cannabis Retail

In our first portrait, we highlight the challenge of creating a legal recreational cannabis market in BC, where illegal farms grew cannabis and illicit dispensaries operated openly on main streets for many years. Since the 1960s introduced draft dodgers from the US and “hippy culture” to BC, cannabis became popular and an industry was created. Growing conditions in BC are excellent, leading to extensive production of “BC Bud,” of which a significant amount was exported to the US (Hamilton, 2004). Not all product was destined for export, however; BC growers also supplied the Canadian market. By the 2010s, a well-established grey market operated in BC, selling a wide range of cannabis from store fronts in cities and towns, with inconsistent enforcement of laws. For example, Kelowna was famously a centre for cannabis growing, retail sales, and consumption, and operators were rarely challenged or put out of business by the police (personal communication, Anonymous, 2019). Not only were profits excellent, but entrepreneurs in the industry also claimed to provide a public service by helping people acquire and enjoy the benefits of cannabis (Canadian Public Health Association, 2017). For these entrepreneurs, legalization of recreational cannabis in BC did not have the character of liberalizing access; on the contrary, the new regulations resulted in much more restrictive access.

The question facing the provincial government was how to implement new regulations in the context of federal legalization, and how to convert the well-established grey market into a legal market. The risk was (and remains) that BC would be left with parallel markets competing with each other. With the transition to legalization, BC’s grey market entrepreneurs faced major changes to their business models. Wholesale distribution in the legal marketplace was handled by the government, and the variety of available products from federally licensed producers and the prices charged did not compete with the offerings of grey market suppliers. Grey market entrepreneurs needed to consider whether they should continue with current operations, quit the industry, or apply for a retail licence. From the provincial government perspective, moving to a more regulated environment was challenging as well, because of the high comfort level with the existing grey market model amongst the public, who could politically reject the excessive restrictions of the new regulatory model and the government that instituted them.

The dilemma facing grey market storefront owners is illustrated by the story of Krystian Wetulani (Subramaniam, 2019d). Once cannabis sales became legal in Vancouver, Wetulani decided to transition from his illicit storefront to a licensed retail operation. Wetulani opened his store, City Cannabis Co., where several grey market cannabis stores, with a broad product range and attractive store designs, had previously been located. From a business perspective, the legal retail store had a business model that was worse than its predecessors. In order to comply with regulations, he offered higher prices and less selection than both the grey market retailers and the online BC Cannabis Store run by the province, all competing for the same customers. The store also featured a less appealing

design aesthetic, following Health Canada's advertising regulations. The differences in prices were particularly challenging: In the early stages of legalization, price and selection issues reflected both the expenses of Health Canada's regulation of licensed producers, including stringent quality controls, and the operational hiccups of the provincial distribution operations. To make matters worse for the entrepreneurs running licensed stores, BC Cannabis Online sold directly to consumers at a price 30% lower than they could afford to match and also offered more variety than they could.

In contrast, Trees Cannabis, managed by Alex Robb, decided to continue operating without a licence (Wilson, 2019). Trees Cannabis was owned by a numbered company, BC0996078, operating stores in three BC cities and employing more than 100 people. After legalization, they continued operating; in later news reports they claimed that they had applied for a licence from the province before legalization but did not receive notification from the regulators. In May 2019, BC's Community Safety Unit visited Alex Robb, the chain's general manager, and warned him about continuing operations without a licence. Nevertheless, they continued selling, and in July CSU visited again. The stores were closed within a few days and the employees were laid off. Robb continued to hope for a retail licence. In January 2020, Robb was personally fined \$1.5 million, the maximum fine assessed at twice the amount of the three months of revenue between the two CSU visits. The process did not end there for Robb, as his case is ongoing (Mulgrew, 2020). The clampdown on illicit retail started slowly in BC, but now seems to be inexorable.

These portraits show how the province was careful not to confront public opinion, especially not in the first months of legalization. But the void created by an undersupply of legal retail establishments, coupled with the difficulty of competing with the provincial online sales and the grey market retailers, created larger issues. For the entrepreneur seeking to operate legitimately, a profitable business model was difficult to implement. For the entrepreneur comfortable with operating outside of the legal framework, the inherent risk of prosecution and punitive fines also impacted business strategy. The common theme for both types of entrepreneurs was the lack of a strong public statement by the provincial government that one system was to dominate. Interestingly, the dynamic is reflected, although slowly, in the rising number of retail stores that have been licensed. In the first year of legalization, surprisingly few stores were licenced in BC (see Table 3 above). Since then, more licensed stores have been opened across the province (see Table 5 above). It seems that the BC government is beginning to coalesce behind one strategy, intended to shift the market toward legal outlets. However, the punitive fines on individuals may backfire in the court of public opinion.

The Prairies: Business Friendly, Sort Of?

The Prairie provinces are all reflective of a pro-business approach to the recreational cannabis market. Each province does it a bit differently. Saskatchewan is the only province

in Canada that does not use government distribution to supply retailers; Alberta has the most stores per capita in Canada; and Manitoba allows consumers to use an app to buy cannabis from a local store and have their order delivered to their home within an hour or two. The general perception is that the Prairie governments have enabled entrepreneurs to establish and grow their businesses. Despite that perception, the retail businesses struggled to establish their operations because the regulations have constrained normal retail practices in different ways.

The “business friendly” approach of Saskatchewan started well before legalization, when the province set up a lottery for retail licences to launch legalized sales, pre-qualifying applicants in a formal process (Fraser, 2018). After the lottery was drawn during the summer, a further process ensured that the applicants were in compliance with regulatory standards. Unlike other provinces with operational delays in the opening of retail outlets, Saskatchewan was open for business on 17 October 2018. One of the advantages for entrepreneurs setting up a retail store or chain in Saskatchewan was that they could order directly from the licensed producers, which eliminated slow deliveries, wholesale inventory control issues, and limited product variety. Saskatchewan retailers did not have problems in accessing cannabis stock in the early phase of legalization, despite the supply chain issues that plagued the rest of the country. With the cannabis 2.0 introduction, they had edibles in their stores before Christmas, a month ahead of retailers in other provinces who had to deal with the extra step of government distribution (CBC News, 2019). Unlike every other province, they were allowed to transfer product from one store to another, allowing retail chains to manage inventory across all their stores. The government also allowed stores to deliver to their customers; delivery services were required to use employees as drivers (and not the more typical independent contractors), because of bonding and insurance requirements. One company, Pineapple Express Delivery, saw an opportunity to fill a market void by working within the unique context of Saskatchewan’s regulations (Subramaniam, 2019c). Pineapple Express provides cannabis delivery services using a model similar to restaurant services like Skip the Dishes. The retailers’ contract with Pineapple Express to send cannabis orders to their customers and to transfer products between stores. Currently, Pineapple Express has been unable to scale this successful business model to other provinces; in other provinces they provide delivery in the medical cannabis market. As different issues have arisen in Saskatchewan, government officials have been willing to listen to the businesses, and adjusted the details of the regulation to solve problems.

Much like Saskatchewan, Manitoba supports the operations of retailers. In order to reduce the black market, the government had a clearly stated objective to ensure that 90% of the population was within a 30-minute drive of a cannabis store, believing that level of access was necessary to displace the illegal market (Hayne, 2019). The government decided they could best achieve that goal by partnering with a limited number of private

businesses who would establish multiple stores, effectively creating local monopolies that included branches in underserved communities while allowing profitable operations through scaling the business operations. Manitoba initially selected four companies from a relatively small pre-qualified lottery pool, much like Saskatchewan, and later held another, similar lottery to ensure access in several more remote communities of the province (Froese, 2019). The retailer chains could send product to customers within an hour or two of ordering and were able to transfer product between stores. A subsequent decision allowed retailers to contract with third party apps to sell their products and make transactions for purchase and delivery. Like Saskatchewan, the delivery service is provided by Pineapple Express, although the business model was operationalized slightly differently to comply with provincial regulation. Unlike Saskatchewan, retailers in Manitoba do have to deal with government distribution, which may lead to increased transaction costs and further opportunities for private delivery services. The speed and flexibility with which the Manitoba government regulators evaluated the legality of third-party apps illustrate the public-private partnership that is core to Manitoba's approach.

Alberta's commitment to business is most evident in the number of stores that have received licences, consistently the highest across Canada (see Table 5). Alberta clearly does not intend to right-size the market by guessing what the right number of businesses should be, but will let market forces make that decision. In the early days of legalization, this approach was not obvious, the government distribution system was overwhelmed, and the approval process for retail licences was slow. Amid the questions about whether there was sufficient supply of cannabis available, the real problem was the challenge of setting up the inventory, ordering and fulfilment systems. Initially, blaming supply issues, a moratorium was declared on retail licences in order to protect the existing licensees from complete lack of supply. Many stores were open only a few hours a day, because they simply did not have enough product, impacting the ability to develop a loyal customer base and displace the illegal market.

Meanwhile, a number of would-be retailers were told to wait indefinitely for their licences, while they continued to pay a risk premium in the form of inflated rents to landlords for the spaces they had already leased. In addition, the licences required those spaces to be renovated to fit regulatory standards for security, community protection, and design. The financial burden was significant and not everyone could finance the delay, effectively stratifying the pool of entrepreneurs into have and have-nots. Those with access to patient capital could afford to wait, while others with less access to traditional forms of start-up finance could not. By May 2019, licences were granted again, but the problems were not over. Alberta was using an ordering system of weekly spreadsheets and emailed orders, and retailers were never confident that what they ordered would arrive in the weekly delivery. This challenge was exacerbated because retail chains were not allowed to perform inter-store transfers. In order to meet customer demand, store managers had to order an

oversupply of product, in the hope that some portion of the order would be fulfilled by the provincial wholesaler. That situation was untenable. Retailers often ended up with stock they could neither sell nor transfer and had great difficulty in forecasting supply needs and serving customers. From the AGLC perspective, the situation also affected their ability to project supply needs, and create a purchasing strategy with licensed producers, which in turn affect planning by licensed producers for planting and harvest cycles. Despite decades of experience distributing alcohol, the government had significant difficulty adapting to the cannabis market. The supply chain process issues finally resolved in winter 2020, although another constraint for businesses emerged when AGLC limited the number of licensed producers who could supply the province. As these setbacks and solutions emerged, Alberta continued to grant licences to retailers, and although the province is only the fourth largest in Canada, continues to have the most cannabis retail stores.

Retail Licence Lottery in Ontario

The story of Ontario's policy for the legalization of cannabis is complicated by politics, as a change in government ushered in a change in regulatory priorities. The dynamics of the discourse around policy objectives, political perspectives, and the role of businesses are highlighted in the regulatory changes and public debates related to a new party coming into power. Before the legalization date, Ontario's then-Liberal government planned to create a market model that employed a government retail monopoly based on the model of the Liquor Control Board of Ontario (LCBO) and the Beer Store, which continue to dominate retail alcohol sales in Ontario. With the election of the Conservative government, headed by Doug Ford, the rhetoric shifted to a focus on licensing private businesses to create a network of retail stores to serve the large Ontario market. Because of the significant shift in regulatory framework, opening day was delayed to allow the new government to develop the new regulatory approach. The stated objective was to protect communities and youth, and to combat the illegal market (Subramaniam, 2019e).

What actually happened was much less pro-business than expected. Citing supply shortages, Ontario decided to hold a lottery for only 25 retail licences; the winners, announced on 12 January, would have fewer than 3 months to undertake the licensing process and open their store by 1 April 2019. The number of proposed licences seemed absurdly low given the size of Ontario's population and the heightened interest among private businesses. Additionally, the Ontario lottery lacked pre-qualification for participants (Subramaniam, 2018a), unlike Saskatchewan and Manitoba. For \$75 anyone, without a criminal record could participate, and thousands did, most without experience in cannabis, retailing, or access to capital. One argument for this approach was to ensure access to small businesses. Many of the winners had no idea how to create a cannabis retail operation, and were hoping to sell their lottery win to the companies who had spent a year or more strategically preparing for legalization. Even this aspect of the lottery added chaos, as

the rules prevented the winning companies (mostly sole proprietors) from selling majority ownership, and required every deal be reviewed by the government.

Six months later, 24 retail stores were opened in Ontario, and a second lottery was in process for 42 additional retail licences (Subramaniam, 2019b). Once again, this lottery had the same lack of pre-qualification processes. Companies responded to the second lottery by figuring out that the lottery rules allowed multiple applicants from one address; they “bought” more tickets by having dozens of people participate for their addresses. At this point, the companies were becoming increasingly desperate to get a return on their large investments.

Despite the government’s rhetoric about working with private business to expand legal retail distribution and displace illegal distribution, the licence approval process created ambiguity, frustration, and delay. As the scenario evolved, industry insiders fumed because of the government’s disregard of both their expertise and their significant financial and time investments. One large, licensed producer’s CEO spoke publicly on the issue (Subramaniam, 2018b). Equally frustrated were small business owners who had committed to participate in the legal market, making significant financial investments and sometimes closing their illegal dispensaries a year early in order to transition into becoming law-abiding businesses. As one commentator noted, “This is fundamentally a story about a callous bureaucracy that has been totally comfortable allowing innocent small business owners like my client to dangle on a thread and spend precious business funds and then yank the rug out from under them” (Daniel Sommers of Sommers Business Law, quoted by Subramaniam 2019a).

People started to question the Ontario government’s commitment to work with private businesses and combat the illegal market. By the summer, sales per retail store in Ontario were extremely high and supply in Canada had increased significantly, which raised the question of why Ontario continued to work with a small lottery system and a small number of licences, rather than following Alberta’s model. In fact, Alberta’s approach dovetailed with the conservative Ontario government’s earliest statements in support of having no cap on the number of licences provided.

The Ontario approach continues to evolve, pitting public discourse about using restricted access to control the potential social problems of widespread cannabis use against the need for widespread access to displace the illegal market. This tension seemed to be reflected in the evolving policies of Ontario’s regulation, with doubts about cannabis businesses dominating in parts of the population. For Canada’s policy, as a whole, this delay has dampened the growth of the legal production of cannabis, as licensed producers had to limit production without access to the large Ontario market.

Quebec: Unintended Consequences

The story of developing an adult-use recreational cannabis market in Quebec, Canada’s second largest province, is one where there was no interaction between business and

government regulation. The provincial focus on the protection of public health dominated the legislative process, and led to strong restrictions on the market. These intentionally created barriers to customer access, inadvertently allowing the illegal market to continue to flourish. This is evidenced through the lack of retail establishments to service likely customer demand given population statistics, the increase in the minimum age from 18 to 21, the high degree of government control over the market, and a prohibition against home cultivation.

In Quebec, concerns about youth access to and consumption of cannabis products drove policy debates. Pre-legalization, a report by the [Institut de la statistique du Québec \(2016\)](#) noted that cannabis use among people aged 15 years or older in the province was 15.2% over the prior year, with rates highest among the 15–17 (31%) and 18–24 (41.7%) age cohorts. Post-legalization, quarterly usage data compiled by Statistics Canada reports that cannabis use in Quebec is lower than it is in all other provinces ([Statistics Canada, 2019, 2020](#)).

Quebec's development of legislation and a regulatory framework for legal cannabis sales was strongly rooted in a public health approach, with multiple stakeholders providing commentary in that process, reflecting a clear bias toward favouring public health and safety over commercial interests ([Watson, et al., 2019](#)). As [Chapados et al. \(2017\)](#) note in a report commissioned by the Quebec Minister of Health and Safety, legalization of the cannabis market should reflect policy aims that were “compatible with a public health perspective: to put an end to the illicit cannabis market, to generate public revenues, and to reduce the harmful effects associated with the use of this substance,” (p. 2) but also argued that a for-profit market model was incompatible with those policy goals. Instead, the report advocated for a “not-for-profit [government] approach that seeks to respond to demand without stimulating it” (p. 3) and “makes it possible to focus squarely on prevention, health and safety” (p. 4).

As a result, Quebec manages all aspects of the retail market through crown corporations. The Société des alcools du Québec (SAQ) is the sole provincial wholesale distributor, while the Société québécoise du Cannabis, a subsidiary of SAQ, is the only provincial retailer. As evidenced by the data in [Tables 3–5](#) above, the development of a retail store network was a slow process, with approximately one retail outlet for every 500,000 Quebec residents, perhaps driven by the mandate to “respond to demand without stimulating it.” The election of a new Coalition Avenir Québec (CAQ) government in 2018, which campaigned on its promise to raise the legal age for cannabis possession from 18 to 21, was further evidence of a provincial shift toward protectionism in the absence of prohibition. As André Picard noted in the *Globe and Mail* (2018), the CAQ would not have time to change provincial law before the date cannabis became legal, but the effect of that change would likely be to drive consumers to the black market, or across provincial boundaries.

While there is not direct interaction between business and provincial regulation, Quebec's strong governmental control of the market and move toward a more restrictive

framework does have effects on the for-profit market. For one, licensed producers, who supply the SAQ wholesaler, are private entities whose sole customer base are provincial wholesalers. The effect of deliberately reducing consumer demand by restricting supply has the consequence of affecting the strategies and operations of licensed producers. For another, restricting access to legal avenues for cannabis possession has the unintended consequence of driving consumers to the grey or black market. The entrepreneurs in other provinces may target Quebecois consumers given the ease of cross-provincial shopping; while black market dealers continue to operate within the province, using well-established illicit business models.

New Brunswick: From Government Monopoly to Concessionaire Model

Unlike the earlier examples, the New Brunswick government decided to establish government control of the wholesale and retail distribution system, only to realize that the approach did not work. The initial model was similar to other Maritime provinces and reflected the model of alcohol distribution created following the end of prohibition, which is still in effect in many provinces. That model had an appeal in the context of Canadian concerns to avoid harm and control risks of addiction and use by youth. The belief was that without a profit motive, a government agency would be able to, like Quebec, respond to demand without stimulating it. New Brunswick followed this model, but soon found that the cannabis business was more complex than anticipated. In the first six months of business, they lost \$12 million dollars (Quon, 2019). It was not until the second quarter of the second year that Cannabis NB became profitable. Rather than helping the provincial budget by sourcing additional revenues, Cannabis NB was an albatross. The minister of finance made a pointed observation: “I’m convinced Health Canada did not want it to succeed. Health Canada has come out with rules like you can’t smile in pictures on our website, because that might encourage people to take part in this activity” (Quon, 2019). Health Canada’s strict regulations were the same for private businesses, but the government had no interest in patiently waiting for profits.

The solution for New Brunswick was not a dramatic change in structure, but a shift to a private business operating the system, a concessionaire model (Jones, 2020). Cannabis distribution in New Brunswick is still a monopoly, but companies were invited to bid on running the system for 20 years under a renewable, long-term monopoly model. After an initial RFP process failed, New Brunswick was still looking for a single operator to make an attractive offer for Cannabis NB. The concessionaire model would ease the cash flow problems for the government and would mean that the government would now strictly be a regulator and not an operator. The concessionaire model relies on close monitoring by government regulators to ensure contractual commitments are met, both to ensure compliance to regulations and to standards of service. One advantage with New Brunswick’s shift is that they were able to make the transition away from a crown corporation quickly,

turning the assets and operation over to the private sector for a price, and thus end the growing deficit quickly.

The curious aspect of New Brunswick's decision was that they chose to work with a single private operator, rather than opening up the province by licensing numerous retailers to serve the market. This is likely a reflection of New Brunswick's small geographic footprint and the nature of markets in the Maritimes provinces, where a few companies occupy a large market position across multiple industries. Further, the RFP process looked for an operator who not only had experience in selling recreational cannabis, but also had a plan to combat the illegal market. At the same time of the RFP process, an estimated 50 illegal dispensaries were operating in the province (Quon, 2019). The crown corporation or concessionaire models, which the government seemed to prefer, did not provide a pathway to legal business models for the existing black or grey market businesses.

Impressions and Future Directions

The story of Canada's path toward legalization and regulation of the cannabis industry is not complete. Yet the early lessons are profound, and raise important questions about equity, access, fairness, and the role of government in the marketplace. Canada's cannabis industry is big business. Even with the licensing, supply chain, logistic, and operational issues, brick-and-mortar retail sales of recreational cannabis in the first year of operation totaled just under \$1 billion. That number is expected to grow as markets become more mature; sales data from edible products and extracts are tabulated; and as regulations, business models, and practices are refined to reflect the lessons learned from the initial phase of the market.

The implications of regulatory structure are also important matters to consider. At the federal level, significant pre-licence investment requirements can be a barrier to entrepreneurs as they must invest to acquire physical space and build the operation to comply with federal guidelines prior to knowing if their licence application has been approved. As long as there are delays in the licensure process, investment risk analysis and assessment will preclude entrepreneurs from engaging in the market and constitute a significant barrier to entry. Additionally, provincial, pre-licence investment requirements to qualify for a retail sales licence will make it difficult for underfinanced and undercapitalized entrepreneurs, many of whom may be from racial and ethnic minorities, from participation in the market.

These equity issues extend to both retail and producer businesses as the monopsony position most provinces hold have implications for newer, smaller, craft-oriented LPs. As provincial wholesalers are disinclined to work with multiple suppliers, many innovative craft producers will be unable to participate in the market. There will also be important and unknown implications in terms of the market concentration of producers once the

industry becomes more mature. Will a highly concentrated market of licensed producers emerge given the small number of supply contracts likely to be negotiated by a universe of 13 wholesale purchasing facilities, or will there be a wide variety of firms competing in the marketplace? What will producers' profit margins look like? Put another way, will the licensed producer market resemble tobacco (a small number of firms) or liquor (a greater variety of firms occupying multiple areas of positional strength within a given industry)? It is tempting to simply state that only time will tell, and that the invisible hand of the market will sort out the landscape. But that approach ignores the impact that regulatory frameworks have on market development, and the responsibility of government to be thoughtful about shaping that framework.

Along the same lines, the implications and impact of a government monopoly in the sale of cannabis products from wholesaler to retailer is not yet fully understood. If provincial governments continue to occupy a bottleneck position in the supply chain (by virtue of their monopsony position with regard to suppliers, and their monopoly position with regard to buyers) the market will potentially suffer from price controls, product shortages, and other operational constraints. This is further exacerbated if provincial governments continue to play a role in the online sales market, as their participation will potentially serve to create pricing inequities and supply shortages absent clear regulation and policy development.

The impact of policy development and market regulation on the ancillary and related business community is also unclear. Market innovation tends to take place when there are market gaps and inefficiencies that serve to provide entrepreneurial opportunity. Yet, the significant province-to-province regulatory variance and limited regulatory and policy development in this area serve to limit opportunities for entrepreneurs to appropriately scale operations.

As the market matures and develops, issues of equity, justice, and fairness will come into play. The antecedents for cannabis regulation in Canada included a commitment to improving public welfare and reducing crime by providing a path toward legitimacy for black and grey market operators; and the legal framework they rest upon acknowledges the nature of racial and ethnic discrimination that is part of the history of Canadian drug policy. Yet, the regulatory environment actively discourages participants in the black and grey market from applying to legally participate in the cannabis business. There are also questions about whether adequate access to capital, sufficient licensing opportunities, and opportunities to participate in the market are available to ethnic and racial minorities, or to Canada's Indigenous population. These questions deserve further study and reflection.

Finally, the efficacy of Canada's approach to market regulation in order to meet the widely stated policy goals of achieving safe roads and communities, combatting an illegal market, protecting the health of youth, and providing safe products to consumers remains yet undetermined. That tale has yet to be told. Nevertheless, Canada has embarked on

a grand adventure as a pioneer in regulatory development of this market. The lessons, successes, failures, and experiences of this experiment will help to shape regulatory and policy innovation across the globe.

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