From: Ian Irvine and Rosalie Wyonch

To: Canadians concerned about cannabis retailing

Date: January 31, 2019

Re: **MOVING ONTARIO'S CANNABIS RETAIL PLAN FROM GOOD TO GREAT**

The Ontario government's decision last fall to put the retailing of cannabis in the hands of the private sector was a good one. The province recently held a lottery to determine who would operate as a cannabis retailer.

The use of a lottery, as opposed to an auction or a "preferred suppliers" rule, to allocate retail outlets can be defended on two grounds. One is that the government did not wish to give excessive retail power to existing cannabis interests with deep pockets, or to other retailers such as Walmart or a pharmacy chain. An auction would likely have resulted in a concentration of retail power akin to the concentration of production power that exists at present. That concentration of production power already places the major licensed producers at a strong advantage relative to smaller competitors, given the ubiquitous presence of government monopsonies – situations where there is only one buyer – across the provinces.

The allocation of licences also was "fair", because it gave every applicant, regardless of characteristics, an equal opportunity.

But the rules defining the recent retail licence lottery have to some degree undermined its ultimate objective – the development of an orderly market that will serve the province in developing a legal market that will be competitive with, and largely supplant, an illegal market.

The largest drawback of Ontario's lottery of 25 retail authorizations is its small size relative to the ultimate need. Further, no municipality with fewer than 50,000 residents will have a retail location. This means that, in many areas of the province, the online Ontario Cannabis Store will be the only accessible legal market, which leaves room for the black market to continue operating. The province has said more licences will be forthcoming – when the supply side picks up.

The apparent reasoning behind the limit on licences was that product was, and is, in short supply. Puzzlingly, Health Canada's preliminary numbers show finished inventories at the end of December that are more than sufficient to supply current sales levels for about three months. It is unclear why this inventory isn't being released to ease shortages at the retail level. But if the production capacity announcements and the snapping up of existing greenhouse capacity means anything, more than enough product will be available by the end of 2019.

Ontario's current lottery structure applies until December 13, when cannabis retail regulations will be amended. The lottery itself may be cancelled or changed at any time without notice. This is puzzling and counterproductive because there is no clarity for current licence winners or those hoping to open a storefront about when or if there will be opportunity for additional retail authorizations. Since supply will be increasing throughout the year, presumably more authorizations will be forthcoming, but when, if and how they may be awarded is not clear.

Paradoxically, the government has decided that the 25 winners must have their outlets in full operation by April 1. Licence winners are to be fined $12,500, increasing to a total of $50,000 by the end of the month.

If, instead, the government had issued many more licences, the winners would be under no pressure to have a fully functioning retail operation in the near term, though there would be a strong market incentive for them to do so. Their planning could progress at a steady pace.

We suggest therefore that the government conduct a second-round lottery or award additional retail authorizations to those on the wait list in the near term. It should also state clearly how many retail outlets it envisages in the long term. Since Ontario has decided to use the private sector in the retailing of cannabis, then it should take off the shackles and allow the sector to operate competitively, rather than in a haze of uncertainty.

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