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FISCAL POLICY IN THE REGULATION OF ADULT-USE CANNABIS IN COLOMBIA

EXECUTIVE SUMMARY

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Translation
Hilary Burke

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Diego Alberto Valencia

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Alejandro Ospina

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Dejusticia
Calle 35 # 24-31, Bogotá, D.C., Colombia
Telephone: (57) 601 608 3605
www.dejusticia.org

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The Authors

Alejandro Rodríguez-Llach

is an economist who holds a Master's in applied economics with a focus on public policy from the University of the Andes (*Universidad de los Andes*) in Colombia. Over his professional career, he has been a researcher for Fedesarrollo and a consultant for the UN Office of the High Commissioner for Human Rights and the Carter Center. He is currently the main researcher in the sub-area of Fiscal Justice at Dejusticia. His work is centered on analyzing the relationship between fiscal policy and human rights. Orcid: https://orcid.org/0000-0002-6633-0622

Luis Felipe Cruz-Olivera

is a lawyer and sociologist who graduated from the National University of Colombia (*Universidad Nacional de Colombia*). He has studied the quality of life in territories where coca is cultivated and the impact of drug policies on access to social rights among coca-growing populations. He contributed to the report *El daño que nos hacen*, presented to the country's Truth Commission, and to the book *Laberintos de prohibición y regulación*. He is currently a researcher in Dejusticia's Drug Policy area. Orcid: https://orcid.org/0000-0003-3670-9292

Isabel Pereira-Arana

is a political science graduate from the University of the Andes (*Universidad de los Andes*) in Colombia who holds a Master's in Development Studies (IHEID). She has explored the impact of drug policies on rural development and on the right to health. She currently coordinates the Drug Policy area of Dejusticia. Her publications include *Voices from the Coca Fields: Women Building Rural Communities* and *Laberintos de prohibición y regulación: los grises de la marihuana en Colombia*. Orcid: https://orcid.org/0000-0001-7036-8407

Fiscal Policy in the Regulation of Adult-Use Cannabis in Colombia[1]

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In Colombia today, discussing a legal framework for marijuana is not a hypothetical matter – it's a real political possibility. In fact, in the 2018-2022 legislative period, three bills were introduced that proposed regulating cannabis for adult use as well as coca-leaf derivatives. This regulatory boom is not exclusive to Colombia; to date, 19 states in the United States and two countries – Uruguay and Canada – have approved a legal framework for adult-use marijuana. This marks a significant change from the hardhanded laws that have shaped the war on drugs from the time of former U.S. President Richard Nixon to the present.

In Colombia, cannabis is the most widely used substance that has been declared illicit. According to the National Survey of Psychoactive Substance Use (*Encuesta Nacional de Consumo de Sustancias Psicoactivas*), published in 2019 by the country's Ministry of Justice and the National Administrative Department of Statistics (*Departamento Administrativo Nacional de Estadística*, DANE), more than 637,000 people used marijuana within the last year (2019, p. 66), which corresponds to 2.7% of the population between 12 and 65 years of age[2]. Seventy-two percent (72%) of these people were between 18 and 34 years of age and

1 This is an executive summary of a text by the same name published by the authors. For the bibliographic references, we recommend consulting the list of sources in that document.

2 According to the survey, nearly 800,000 people used some kind of substance that had been declared illegal in the last year, or 3.36% of the country's population (Ministerio de Justicia & DANE, 2019, p. 57).

lived in Bogotá, Cali, the coffee belt or Medellín (Ministerio de Justicia & DANE, 2019, p. 68).

According to the National Planning Department (*Departamento Nacional de Planeación*, DNP), the geographical distribution of marijuana use tends to be concentrated in urban areas that are attractive for selling the cannabis produced in the Northern Cauca subregion (DNP, 2017, p. 105). Although that is not the only region with marijuana crops, the country is currently experiencing a boom in so-called "creepy" marijuana[3] (as a result of the extent of this substance and dependence on the income from it), which is produced in the Northern Cauca municipalities of Caloto, Corinto, Miranda, Toribío and Santander de Quilichao.

In this context, two sensitive factors arise in debating cannabis regulation in Colombia. One is that the areas that supply the illegal market have significant gaps in terms of socioeconomic well-being and continue to experience conflict dynamics partly associated with the substance's prohibition. The other is that the regulation of marijuana, as the most widely consumed illicit substance in the country, must address the protection of public health and the health of those who use it.

The majority of regulation proposals put little emphasis on the potential revenue coming from the market, or the allocation of those resources. If we agree that marijuana has played a central role in the origins of drug trafficking in Colombia, and that the regions where it is grown today lag significantly in socioeconomic terms, the transition to a legal market would be an opportunity to improve the peasant farmer and indigenous population's living conditions, while also protecting public health by controlling the quality and potency of the cannabis that is bought and sold. All of these public policy actions require resources. While those who promote business interests in

3 "Creepy" marijuana is not a strain itself; it is a generic term used for the indica strains that tend to have higher THC concentration. While the "Colombian" strains that conquered U.S. markets in the 1970s and 1980s had 7% or 8% of THC, creepy marijuana is distinguished by having between 15% and 25% of that component, which produces a much greater, but shorter, psychoactive effect (Robbins, 2019).

marijuana regulation insist on stressing the economic benefits for the overall economy, along with the amount of resources it would contribute to state coffers, they fail to mention specific measures that the State should delineate so the market can be based on rules that would finance the actions needed to address the regional problems that predate the regulations, or actually gave rise to the illegal trade.

With the goal of illuminating this discussion, based on comparative experiences and on the Principles and Guidelines for Human Rights in Fiscal Policy, this document addresses three dimensions of the problem: (i) explaining, based on available evidence and conceptual debates, why regulation is necessary and what role the fiscal framework plays in this policy; and (ii) providing, based on comparative experiences, elements for designing the regulations' fiscal frameworks. Finally, contemplating these two aspects, we present a proposal for cannabis fiscal principles.

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1. Why Regulate and Why Does the Fiscal Framework Matter?

The drug policy currently in place is a strategy designed to eliminate the use of certain substances, selected arbitrarily and with no basis in evidence, through States' use of repressive tools: criminal and/or administrative sanctions (Jelsma & Armenta, 2015). Based on the imposition of penalties as well as public stigmatization, anti-narcotics[4] strategies have sought to eradicate crops, prohibit the trafficking of illicit drugs and hinder people's access to them. All of this with the aim of safeguarding humanity's well-being and public health, especially among children and adolescents.

However, it has been demonstrated that this drug policy has not only failed on its own terms, it has also produced more

4 Within the international drug control system, the term "narcotics" is used imprecisely because it is used to refer in general to all the substances classified in the drug control treaties but, for example, cocaine is a stimulant, not a narcotic substance. In this section of the text, we use the terms as they are employed under prohibition, but we alert readers to their lack of precision.

harm than what it sought to "save" humanity from. The current model is based on the premise that the greater the use of punishment and sanctions, the faster drug markets will be fully eliminated from society. However, after 60 years of implementation, there are more people using marijuana today than at the time the drug control treaties were adopted. It is clear that prison, police sanctions, stigma and fines have not managed to dissuade the nearly one million Colombians who use marijuana (Ministerio de Justicia & DANE, 2020), or the estimated 200 million people in the world who used cannabis in 2019 (UNODC, 2021, p. 19).

It can be concluded that current drug policy is the source of the violation of multiple human rights: to personal autonomy, to life, to health, to an adequate standard of living, and the right to benefit from scientific developments, to name a few. Therefore, in the name of complying with international drug treaties, States violate their populations' human rights. The shift to a cannabis regulation scheme would eliminate the risks associated with illegality. The products would be supplied in authorized scenarios, free of violence between criminal groups; the quality and potency of the marijuana would be made known, enabling better management of the pleasure and risk involved; and police sanctions would be eliminated. As a collateral effect, the freed-up police resources could be focused on more apt and urgent tasks related to citizen security and coexistence.

Given this context, a regulation scheme must seek to: *(i) reduce marijuana's comparative impact in illegal economies and drug trafficking networks; (ii) protect public health; (iii) promote rural development in prioritized areas; and (iv) promote reparation measures funded with the scheme's resources*.

A drug policy that can be respectful of human rights and safeguard public health must position itself at an intermediate point between full liberalization and the prohibition in place today. Thus, if one of the greatest costs of prohibition has been the creation of a market outside state control, the most reasonable solution seems to be a regulation model that would incorporate harm reduction principles. We believe that this alternative is capable of progressively reducing the potential harm of drugs and of the policies implemented to date.

For regulations to achieve these goals, they must make use of fiscal policy as a key instrument for guaranteeing rights by providing resources to finance them, understanding that such policy is also subject to States' human rights commitments and obligations. Meaning that in the transformation of cannabis rules, fiscal policy becomes critical, both to avoid repeating the errors of the current control system as well as to repair the harm done to communities affected by the prohibition model. In this regard, based on certain Principles and Guidelines for Human Rights in Fiscal Policy[5], we propose minimum standards for defining the regulatory structure and helping fulfill the regulations' goals.

These principles maintain that fiscal policy must be socially just[6], be designed in accordance with the principles of equality, equity, legality and non-discrimination[7], and be transparent, participatory and accountable[8]. States must use their fiscal policy to mobilize the maximum amount of resources available to progressively achieve the full realization of economic, social and cultural rights[9]. They can also encourage or discourage certain conducts and correct externalities through specific fiscal policy instruments, and adopt priority fiscal measures in order to guarantee human rights[10].

These principles serve as a road map for evaluating the fiscal policies that have been designed for regulated markets around the world, as well as for proposing a model for regulating adult-use cannabis in Colombia that would incorporate a fiscal policy with a human rights approach, suited to the country's particular context in which the war on drugs and the internal armed conflict converged.

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5 Particularly Principles 3, 5, 7, 10 and 12.

6 Principle 3.

7 Principle 5.

8 Principle 7.

9 Principle 10.

10 Principle 12.

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It is important to emphasize that given the varied objectives of adult-use cannabis regulation, tension can arise between these principles and the regulations' own goals. For example, one of the goals of regulation is to displace the illegal market and reduce its negative social and economic impacts. To achieve this goal, it is desirable for the products in the legal market to be able to compete with those in the illegal market in terms of pricing, meaning that they should have similar and competitive prices. If the price of cannabis in the regulated market is much higher, it is unlikely that demand will be reduced in the illegal marketplace. This creates a clear tension with public health and social justice goals, since the use of taxes to mobilize resources and to discourage the use of cannabis products would tend to increase the price of marijuana in the legal market.

2. Comparative Experiences and Lessons Learned: Uruguay, the United States and Canada

In this section, we present the most relevant fiscal policy aspects of the distinct regulation models for adult-use cannabis that have been implemented in Uruguay, the United States and Canada. With this analysis, we seek to learn from the positive and negative experiences of those models, to extract key aspects that can be adapted to the Colombian context and thereby propose some fiscal principles for a regulation scheme based on experiences and evidence from other countries, without losing sight of the particular facets that must be considered in a regulated market for Colombia. The variables of analysis that we used were: (i) the market models and goals of the regulations; (ii) the application, design and types of taxes in the regulated market; and (iii) the use of the tax revenue generated by the regulated market.

Although the different countries and jurisdictions in the world that have moved to regulate adult-use cannabis have relatively similar goals – to protect public health, reduce the criminality associated with the illegal market, and (in some cases) promote vulnerable communities' social inclusion and reparation – each has chosen a different design to achieve them.

Uruguay was the pioneer in this shift in the drug policy paradigm, having proposed a different approach to that of prohibition. It has carried this out through a strict regulation scheme, with a planned market that is fully intervened by the State. In this way, the country sought for its cannabis regulation to have a public health orientation (by controlling consumption) while also combating the criminality associated with the illegal market (by firmly controlling production levels and prices). These elements align its regulations with a human rights approach. However, there is nothing in publicly available information or in reports on the scheme indicating that it seeks to achieve greater social inclusion and more economic opportunities for marginalized communities (Hudak et al., 2018). We infer that this is because the scheme does not have many mechanisms for raising revenue (taxes), and what is raised is earmarked exclusively for financing the regulations' functioning.

Perhaps the "original sin" committed in Uruguay's regulations has been the aim of safeguarding public health as much as possible and fighting against the illegal market. Its "strict and responsible" regulatory approach has meant that the model has many controls and restrictions, to the point of producing undesired effects and incentives among consumers and in the illegal market itself. Access to the legal market has been limited. Currently, 14 pharmacies engage in cannabis sales, and although their locations correspond to the country's population distribution, this tiny number means that users must travel up to 100 kilometers in some cases to reach one (Arenales, 2019). A strong indication of these access problems can be found in the data provided by the Uruguayan Drug Observatory (*Observatorio Uruguayo de Drogas*) regarding adhesion to the legal market. This shows that in practice, just 14% of cannabis users have been registered with one of the regulated market's means of access in the last 12 months (Observatorio Uruguayo de Drogas, 2019, p. 132), although official data from the Institute for the Regulation and Control of Cannabis (*Instituto de Regulación y Control* *de Cannabis*, IRCCA) indicates that 28% of users are registered (IRCCA, 2018, p. 4).

Meanwhile, in the United States, some states have opted for a rigorous regulation scheme but one that is more liberal and market oriented. Upon studying the first regulations put into place (Colorado, Washington, Oregon and Alaska), it is clear that there is a dominant public health logic underlying the regulations. These approaches embrace many of the legislative parameters used to control alcohol and tobacco in that they involve market-based licensing systems that regulate private commercial activity, establish a minimum age for legal purchases, and implement tracking systems to monitor distribution and thereby minimize the diversion of resources to illegal circles.

The predominant influence of alcohol legislation has become apparent since three of these states have regulated marijuana through state liquor control boards, with the support of interest groups, taking existing policies on alcohol as the starting point for shaping cannabis guidelines. This entails some risks to the marijuana regulations' public health focus, in part because the interests of the cannabis sector – like those of tobacco and alcohol – should be excluded from public health policy design and/or orientation. In fact, the regulations in Colorado and Oregon have replicated the codes for self-regulation on advertising and marketing that characterize the alcohol and tobacco industries, which have had a limited effect on reducing consumption (Barry & Glantz, 2018).

The social justice focus, however, is one of the most interesting elements of some regulation schemes in the United States. Whether by granting preferences in the provision of licenses, eliminating prior convictions related to cannabis offenses, or making marginalized communities the beneficiaries of the resources generated by the market, these communities are benefiting from regulation in various states (Adinoff & Reiman, 2019) – which shows how regulations can serve as an opportunity for reparation and social and productive inclusion. However, these efforts have come up against obstacles created by players with powerful interests in the market.

Canada, meanwhile, has tried to take advantage of the potential of the Uruguayan and U.S. models at the same time, adopting a regulatory framework with heavy state intervention in distribution, but leaving room for the market to take the lead on production. Although this approach is aimed at protecting public health with monitoring and control of direct sales to consumers, it has weakened the goals of displacing the illegal market and of seeking greater social inclusion for affected communities.

First, in none of Canada's provinces or territories is there a licensing system that involves social justice criteria (Slade, 2020b). In fact, the lack of a specific allocation for the tax revenue generated means that there is no real commitment to this ideal. On another point, one of the biggest challenges of Canada's regulation scheme has been displacing the illegal market. Although official statistics on access to cannabis show an increase in the use of legal sources (the percentage of consumers who said they had obtained cannabis from a legal source increased by nearly 30 percentage points after legalization), the reduction in illegal sources has not been as notable (with a reported decline of around 10 percentage points).

It has been found that this difficulty in displacing the illegal market is related mainly to the price of cannabis in the legal market (Kilmer, 2019; Slade, 2020b), which has remained much higher in comparative terms. According to official figures from the national statistical office, Statistics Canada, the price of a gram of cannabis in the illegal market in 2019 was $5.96 Canadian dollars (CAD), while in the legal, regulated market it was nearly double that at CAD $10.29 (Statistics Canada, 2020a). Moreover, upon analyzing the evolution of prices in both markets, it can be seen that while the price per gram of cannabis in the legal market has remained relatively stable, it systematically declined in the illegal market between 2018 and 2019, which were the first two years of the regulation's implementation (Brown, 2020). This has led various provinces in the country to request that the federal government reevaluate the taxes on the legal market (Lamers, 2022).

The use of fiscal policy in the regulated markets of the United States and Canada largely contrasts to the approach in Uruguay. While Uruguay opted for a model in which control of production and cannabis sales is the strategy for regulating consumption levels, health effects and competition with the illegal market, some states in the United States and Canada decided to use the regulatory role of taxes to (i) discourage consumption and (ii) obtain fresh resources for implementing strategies for prevention, the reduction of health risks and harm, and reparation with a social justice approach (thereby fulfilling Principles 3, 5, 10 and 12). However, while Uruguay has managed to maintain a competitive price in its regulated market, Canada and the United States have had difficulty displacing the illegal market due to the high price of their regulated products. For example, in California – the biggest adult-use cannabis market in the United States – the illegal market is still bigger than the legal one and shows no sign of having been debilitated. This has occurred, in part, due to the use of indirect taxes in that state's regulation scheme (McGreevy, 2019).

The taxation model in some jurisdictions of the United States is also the object of criticism for being focused on raising revenue without paying much attention to the aspects of tax design that can discourage consumption. That is the case because (with the exception of Alaska) the indirect taxes on cannabis products do not take THC content levels into account. The evidence on health taxes indicates that levies seeking to disincentivize the consumption of products harmful to people's health must include in their taxable base the component that negatively affects health (Sassi et al., 2013). In this case, linking the tax to THC levels would be a way for governments to induce consumers to buy less potent products, which would entail fewer health risks. In this sense, the literature has shown that the price of products, especially in relation to their potency, is the most important factor in purchasing patterns (Slade, 2020a).

Currently, the majority of states have few controls on the maximum potency of cannabis products in the market, and this has led to producers developing crops with greater potency to increase demand and their profits. For example, in the state of Washington, the proportion of strains with a THC concentration above 15% grew by 93% just a few years after regulation began (European Monitoring Centre for Drugs and Drug Addiction, 2020). Thus, a tax that incorporates THC content into its taxable base can contain the emergence of more potent products and be more effective in achieving the desired public health outcomes[11].

This would suggest, then, that Uruguay's strategy to not levy taxes is the best option. However, the decision to not apply indirect taxes to products in the cannabis market is a lost opportunity for the State to wield useful tools for contributing to rights guarantees. For example, the State is not using taxes to discourage cannabis use via prices (Principle 12). At the same time, the exemption from indirect taxes prevents the State from being able to mobilize resources and spend them to pursue the goals of guaranteeing the rights of marginalized populations and of users (Principles 3, 5 and 10). In addition, having a low price does not ensure the total or immediate displacement of the illegal market.

Finally, Uruguay differs from Canada and the United States in its application of Principle 7, which is centered on the transparency of the regulated market's fiscal information. In Canada, the Statistics Canada office has public information about the types of taxes that are applied to the regulated adult-use cannabis market, along with data on the revenue they raise.

Analyzing the good practices presented in this section is of vital importance for informing the decisions that may be made on adult-use cannabis regulation in Colombia. However, it is imperative that the particularities of the Colombian context be taken into account, so that these good practices can assimilate these characteristics of the national context and be effective for ensuring the goals of the country's regulation scheme. Thus, the next chapter offers an overview of these particularities.

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11 There is evidence regarding the tax on sugary drinks, in some jurisdictions of the United States, that indicates that designing the taxes based on the sugar content and not on the price (ad valorem) improves results by up to 30% (Grummon et al., 2019).

3. Cannabis Fiscal Principles

Based on the analysis of the context and the legislation mentioned previously, we propose elements for a fiscal policy on cannabis, envisioned both in terms of raising revenue and allocating it.

Fiscal Policy for Mobilizing Resources

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The first principle that this regulation scheme's fiscal policy must comply with is that of mobilizing resources via the various types of taxes that can be applied in this market, which corresponds directly to Principle 10. It is important that the legislation gear the use of resources toward fulfilling economic, social and cultural rights.

Thus, the taxes to be applied to a future regulated market in Colombia should be direct (corporate income tax on companies that operate in any phase of this market's value chain), or they could be indirect taxes on the sale or consumption of cannabis products. The indirect taxes contemplated in the Colombian Tax Statute that could be applied to these products are the Value-Added Tax (VAT) and the excise tax. The latter levy taxes the consumption of goods that are not considered to be part of the standard family's basket of goods, and the rate is in addition to the VAT and varies between 4%, 8% and 16% (Estatuto Tributario Nacional, n.d., sec. Art. 512-1).

In the case of the adult-use cannabis market, the products should have a specific tax or a surcharge on the excise tax that would seek to protect consumers' health – either by discouraging consumption of these products via the price, or by ensuring that the effects on third parties (negative externalities) be offset with the resources contributed by the tax. However, upon establishing this type of tax, it is necessary to keep the price from going above what the illegal market offers. To address this, we propose a regime in which the tax rate on the sale of cannabis products starts at 12% and increases each year starting in 2025 until it reaches 18%.

Fiscal Policy for Allocating Resources

The revenue generated by the regulation scheme can be allocated in multiple ways to contribute to achieving the goals of reducing the illegal market, protecting public health and providing reparation to the victims of prohibitionist drug policy. This is in line with Principles 3 and 5.

First and foremost, the revenue collected from the cannabis market must fund the operation of the national institutions involved in regulation. We propose that the spending needed to set up this institutional framework come from the resources generated by the regulation scheme in its early years, with a gradual reduction of this source of financing until the expenditure becomes an operating cost of the State.

A critical goal of the regulations must be to delay, as much as possible, the age of initiation of those who will use cannabis. In other words, the State must seek to ensure that no one under the age of 18 tries or develops a constant habit of using this substance. In addition, while adverse health events should be prevented, it is impossible to eliminate them entirely since there are adverse reactions and processes related to psychoactive substances that cannot be prevented completely (which is true of all such substances).

The health care system, in collaboration with the Drug Observatory of Colombia (*Observatorio de Drogas de Colombia*), should produce information on trends regarding use, age, sex, socioeconomic stratum, modalities, consumption patterns and adverse events. We also recommend that with regard to public expenditures, the progressivity of spending must serve as the guiding principle, with the aim of reducing socioeconomic inequalities or others that, due to intersectionality, affect marginalized or historically discriminated groups, such as the LGBTI population, ethnic communities, and women in situations of poverty and vulnerability, among others.

Third, cannabis regulation must take a reparative approach to the communities and people who have been harmed by prohibition. This is not about simply handing over the funds raised by collecting taxes in the nascent adult-use marijuana industry. On the contrary, this approach entails a paradigm shift in Colombia's relationship to cannabis and other drugs that have been declared illicit – and therefore in the relationship between the State and the regions where this plant is grown.

The regulations' focus on reparation should contemplate the difficulty of repairing damage, depending on the scope of drug policy impact – whether personal, community-wide, regional or collective. To develop this focus on reparation, we propose, based on Principle 3, financing rural development efforts in the areas that produce cannabis, and even in those where the coca economy is present, to deepen territorial transformation and support the regulations' advancement along the path forged in implementing Chapters 1 and 4 of the Final Peace Agreement. We also recommend that the resources obtained from the regulations be used to finance technical assistance for cannabis production in rural areas, through support for associative schemes and investment subsidies for small-scale producers.

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The elements proposed here are subject to a continual process of construction and revision. Just as prohibition took years to be consolidated as a model to follow, the same will occur with these regulations. There will be years of testing, of trial and error, of observing and understanding what happens when a substance is moved into the legal realm, and how this interacts with particular contexts of the war that we are trying to leave behind. But even amid this laboratory of regulation that we will experience in real time, people's health and their dignity constitute the critical minimum elements for orienting a fiscal framework for regulated marijuana markets. We believe that these cannabis principles – sustained by a regulatory vision framed within human rights and fiscal justice, with multiple goals and lessons gleaned from successful international experiences – are a useful and powerful tool for the debates taking place, now and in the future, around the regulation of this plant for adult consumption.

The debate about regulating cannabis for adult use is on the public agenda. In our view, the best policy on marijuana that a State can develop is the regulation of its cultivation, manufacture and use, focused on reducing marijuana's comparative impact in illegal economies and drug trafficking networks; protecting public health; promoting rural development in prioritized areas; and promoting reparation measures financed with the resources arising from regulation. Drugs are not the devil, but nor are they child's play. A drug policy that would be respectful of human rights and safeguard public health must lie at an intermediate point between full liberalization and the prohibition currently in place.

In this document, based on a comparative analysis of the regulations issued in Uruguay, Canada and the United States and by applying the Principles and Guidelines for Human Rights in Fiscal Policy, we argue for the importance of a fiscal framework based on collecting taxes in the cannabis market and focused on mobilizing the maximum amount of available resources to finance the goals of reducing the illegal market, preserving public health and assisting the populations affected by drug policy, as set forth in the cannabis regulations.