Interstate Cannabis Legalization: Mind the Trap

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Abstract: *We expand the analysis related to the issues brought up in the recent paper,* Legalization Without Disruption: Why Congress Should Let States Restrict Interstate Commerce in Marijuana *by Scott Bloomberg and Robert A. Mikos. Their paper essentially argues that Congress should suspend the Dormant Commerce Clause ("DCC") and allow different states to restrict interstate commerce for marijuana (and, more broadly, cannabis) use. We believe this will create a number of disruptions and unintended consequences associated with the public choice literature. In particular, the temporary suspension of the DCC will create monopoly rents, expand rent-seeking opportunities, and lead to underground market issues similar to what currently exist in the cigarette market. In other words, the DCC, rather than an "arcane" institution, actually provides important constraints on states' abilities to regulate commerce in a manner that helps special interests at the expense of the public.*

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I. INTRODUCTION

"Too many lives have been upended because of our failed approach to marijuana. It's time that we right these wrongs."[1] These words come from a Biden Administration press release on cannabis reform issued on December 22, 2023. It echoes current sentiments about federal cannabis legalization, or at least decriminalization, a policy that seems to be imminently approaching. The full statement from President Biden is a call for clemency and reform, and it admits that the approach of the War on Drugs has been a failure that has not only been vastly unfair but also has harmed numerous lives. The U.S. Drug Enforcement Administration ("DEA") has heard the President's message and will, according to an April 2024 Associated Press article by Zeke Miller and colleagues, move to reclassify cannabis as a Schedule III drug, consistent with the 2023 recommendation by the Department of Health and Human Services ("HHS").[2]

[1] Statement from President Joe Biden on Clemency Actions, The White House (Dec. 22, 2023), https://bidenwhitehouse.archives.gov/briefing-room/statements-releases/2023/12/22/statement-from-president-joe-biden-on-clemency-actions/.

[2] Zeke Miller, Joshua Goodman, Jim Mustian & Lindsay Whitehurst, US Poised to Ease Restrictions on Marijuana in Historic Shift, but It'll Remain Controlled Substance, AP News (Apr. 30, 2024, 7:51

The political climate across U.S. states concerning legal cannabis use has changed drastically over the past decade. While still prohibited at the federal level, the prohibition is largely unenforced, and adult use is currently legal in twenty-four states plus the District of Columbia.[3] Five states (Connecticut, Missouri, Delaware, Maryland, and Ohio) joined this list in 2023.[4] Minnesota, where recreational use and possession by adults has been legal since August 2023, is finalizing licensing for legalized recreational retail and manufacturing to begin in 2025.[5] And Virginia, where small-scale possession has been legal since 2021, was on a similar trajectory as Minnesota for legal recreational sales before Governor Youngkin of Virginia vetoed bills in March 2024 and March 2025 that would have legalized recreational retail sales.[6] Further, use of cannabis for medical purposes has, at the time of this writing, been approved by thirty-nine states.[7] In Kentucky, medical marijuana is now legal as of January 1, 2025.[8] There have also been failed legalization attempts, most recently in Oklahoma in 2023, as well as in Florida, North Dakota, and South Dakota in 2024.[9]

Current Political Climate

The political debate concerning the further expansion of legalized cannabis use is a fruitful one. Arguments largely grounded in individual freedom, medical research and quality of care, and tax revenue make up one side of the debate, in contrast with arguments grounded in associations with criminal activity and morality on the other side. The former group of arguments appears to be garnering relatively more patronage, as public support for

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PM), https://apnews.com/article/marijuana-biden-dea-criminal-justice-pot-f833a8dae6ceb31a8658a5d65832a3b8.

[3] See Elliott Davis Jr., Claire Hansen & Horus Alas, Where is Marijuana Legal? A Guide to Marijuana Legalization, U.S. News & World Rep. (April 30, 2024), https://www.usnews.com/news/best-states/articles/where-is-marijuana-legal-a-guide-to-marijuana-legalization.

[4] Id.

[5] Id.

[6] Id; A.J. Herrington, Virginia Governor Vetoes Recreational Cannabis Sales Bill, Forbes (Mar. 25, 2025), https://www.forbes.com/sites/ajherrington/2025/03/25/virginia-governor-vetoes-recreational-cannabis-sales-bill/.

[7] State Medical Cannabis Laws, National Conference of State Legislatures (NCSL) (Jun. 5, 2025), https://www.ncsl.org/health/state-medical-cannabis-laws#:~:text=Thirty%2Dnine%20states%2C%20three%20territories,1%2C%202025.

[8] A.J. Herrington, Medical Cannabis Is Now Legal In Kentucky, Forbes (Jan. 6, 2025), https://www.forbes.com/sites/ajherrington/2025/01/06/medical-cannabis-is-now-legal-in-kentucky/.

[9] Davis Jr. et al., supra note 3; Associated Press, Trio of Ballot Failures Leads Marijuana Backers to Refocus Their Efforts for Recreational Weed, U.S. News & World Report (Nov. 6, 2024), https://www.usnews.com/news/us/articles/2024-11-06/trio-of-ballot-failures-leads-marijuana-backers-to-refocus-their-efforts-for-recreational-weed.

cannabis legalization is overwhelming, according to at least some polls. For instance, a 2022 Pew Research Center survey indicated that eighty-eight percent of adults—roughly nine in ten—supported legalization of at least medical cannabis.[10] Moreover, Gallup polling from October 2023 indicates that support for total cannabis legalization has never been higher, at seventy percent of U.S. adults polled.[11]

We do not aim in this Article to contribute to the debate on whether cannabis *should* be legalized by the federal government or individual states. Rather, given the realities of state legalizations and public support of legalized cannabis including by President Biden, the DEA, and HHS, we suggest that federal legalization of cannabis will occur, likely sooner than later. The issue we wish to address, then, is *how* the federal government should legalize cannabis. More specifically, we seek in this Article to help answer the following questions: what is the political economy of cannabis policy reform, and if the federal government is to legalize cannabis, what provisions, particularly regarding issues related to interstate commerce, should and should not be included in such a law?

The existing combination of federal illegality and state legality has created an environment that has insulated many cannabis firms from competitive pressures, particularly competition from outside of the firms' home states. Changes to federal law threaten these firms' protected profits, creating a strong incentive for these firms to support political opposition to such changes. One possible way to placate political opposition to federal cannabis legalization is to exempt cannabis from the Dormant Commerce Clause ("DCC"). Article I, Section 8, Clause 3 of the U.S. Constitution, known as the Commerce Clause, states that "Congress shall have Power . . . To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes."[12] In contrast to the doctrine of preemption, which applies when Congress has actively enacted relevant legislation, the DCC has been interpreted by the Supreme Court as a prohibition on state laws that unduly restrict interstate commerce even in the absence of congressional legislation—that is, even when Congress has been dormant. Such an interpretation ensures an environment that is conducive to a national market for goods and services by prohibiting protectionist policies by states. Relevant to the

[10] Ted Van Green, Americans Overwhelmingly Say Marijuana Should be Legal for Medical or Recreational Use, Pew Rsch. Ctr. (Nov. 22, 2022), https://www.pewresearch.org/short-reads/2022/11/22/americans-overwhelmingly-say-marijuana-should-be-legal-for-medical-or-recreational-use/.

[11] Lydia Saad, Grassroots Support for Legalizing Marijuana Hits Record 70%, Gallup (Nov. 8, 2023), https://news.gallup.com/poll/514007/grassroots-support-legalizing-marijuana-hits-record.aspx.

[12] U.S. Const. art. I, § 8, cl. 3.

federal legalization of cannabis is that states which have already legalized it, whether just for medical use or also for recreational use, are generally calling for the exemption of cannabis from the DCC. Such an exemption would effectively create an environment in which we would observe fifty independent markets, and in which the limited number of firms in each market would be insulated, as would their profits, from competition from those firms operating in the other state markets.

In the debates over federal legalization, the currently protected firms in legalized states serve as the primary sources of political support behind the call for cannabis's exemption from the DCC. As such, elected officials from legalized states generally support the exemption of cannabis from the DCC. Exemption would permanently insulate licensed cannabis firms from competition, benefiting the pocketbooks of select constituents. However, exemption would also lead to less entrepreneurship, less innovation, increased prices, and an overall less efficient market. Furthermore, with higher prices, a substantial segment of the market will remain in the underground economy with all the related dangers that come with such economies.

We argue that not only will these negative features exist if the DCC is suspended, but the suspension will also be exceedingly difficult to get rid of because it will create what Gordon Tullock refers to as a "transitional gains trap,"[13] which we will delve deeper into in Part II.I.

The remainder of this Article is laid out as follows: Part II explains what a transitional gains trap is and provides context for the current state of cannabis policy among the states as well as the current proposals for federal legalization. Part III explains why the current cannabis policy environment is a transitional gains trap. Part IV lays out the dangers of suspending the DCC, even with a sunset provision. Part V provides parallels to cannabis that highlight the dangers a sunset provision would create. Part VI provides concluding remarks on how special interests groups will capture the federal cannabis industry if constitutional constraints, such as the DCC, are weakened.

II. THE CANNABIS STATUS QUO AND OUR CURRENT TRANSITIONAL GAINS TRAP

In this Part, we will argue that the state-by-state legalization paradigm is creating incentives for current residual claimants to craft and fight for legislation that protects the rents created through the current regulatory regime

[13] Gordon Tullock, The Transitional Gains Trap, 6 Bell J. Econ. 671, 671-72 (1975).

with the coming federal legalization. This creates an issue in which varying and complex state laws and provisions exist. As will be detailed, state laws, to not run amiss of federal law and to achieve other social goals, have been constructed in ways to create insulated, state-specific markets, such that those firms granted permission to operate in the state enjoy exclusive privileges and monopoly rents. These privileges create obstacles to changing public policy as those enjoying them will expend resources to prevent changes that remove or reduce the monopoly rents. As such, we are stuck in a transitional gains trap in many of these states.

A. What is a Transitional Gains Trap?

Economist and Nobel laureate James M. Buchanan famously pointed out that it is one thing to want the government to do something, but it is a different matter to have the government do what you want.[14] And to effectively get the government to do what you want requires removing our rose-tinted glasses in how we view the government's abilities. We must treat the study of government without romance. We need a positive framework. This means that in the context of cannabis legalization, it is necessary to look at the institutions of the government itself and see what incentives the current environment creates for its actors.[15] Although there are normative implications worth considering, the positive analysis that Tullock's transitional gains trap framework enables is a critical step in the process and represents one particularly dangerous outcome we may face in our current environment. [16] But such a value-free analysis has been largely absent in the previous literature on the federal cannabis debate.

A transitional gains trap occurs when the government enacts an inefficient policy that benefits a particular group. Over time, political competition erodes the benefits received by that group (or whichever group gains those benefits), yet that group still has an incentive to fight to prevent the policy

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[14] See James M. Buchanan, Politics Without Romance: A Sketch of Positive Public Choice Theory and Its Normative Implications (1979), *reprinted in* 1 The Collected Works of James M. Buchanan 45, 45, 57 (Liberty Fund 1999).

[15] See Geoffrey Brennan & James M. Buchanan, The Reason of Rules: Constitutional Political Economy (1985), *reprinted in* 10 The Collected Works of James M. Buchanan 1, 14 (Liberty Fund 2000). Our call to apply public choice theory to the analysis of the Dormant Commerce Clause is not new to the study of law generally. Paul Mahoney explains how Adam Smith's ideas on jurisprudence "anticipated by 2 centuries a surprising number of important law and economics insights," many of which relate closely to or are the foundational basis for the ideas of James Buchanan and Gordon Tullock, two of the most prominent public choice scholars. Paul Mahoney, Adam Smith, Prophet of Law and Economics, 46 J. of Legal Stud. 207, 208 (2017).

[16] Tullock, supra note 13.

from being eliminated through a further use of resources that do not produce wealth, thus increasing the inefficiencies created by the policy. Current cannabis policy is already creating a transitional gains trap. Federal legalization could be a ticket to eliminate the trap, but we argue that suspending the DCC will result in creating a new transitional gains trap rather than simply eliminating the old one.

The very existence of government regulation will result in a competitive process to shape and capture that regulation for different special interests.[17] If the DCC is suspended, this will create opportunities for various special interests to utilize different regulations to their own ends. For example, small- and medium-sized firms may lobby the government to implement regulations that erect barriers (or at least make it more costly) for big firms to enter or compete in the market. But big businesses will also face similar incentives. The result is a shift of competition from the marketplace to the political arena. If small- and medium-sized firms are successful, they could obtain market power and thus be able to capture monopoly rents. What Gordon Tullock argues in his seminal work, however, is that these windfall gains (i.e., the monopoly rents) will be short-lived.[18] This is because the existence of the rents creates and invites political competition to capture them. So, just as with market competition, where competitive forces push economic profits to zero, firms will be willing to spend (in this case, in the political arena) to capture the rents, up to the point that the monopoly profits fall to zero (what economists call "normal profits" in a perfectly competitive market).

Figure 1 shows a standard monopoly graph (with constant marginal costs as a simplifying assumption).[19] The typical inefficiencies resulting from a monopoly that economists have tended to focus on are the allocative inefficiencies resulting from the restriction of output that results in deadweight loss (Triangle H; often referred to as the Harberger triangle). But what Tullock argued is that this is often far from the end of the story. Monopolies generate monopoly rents (in the size of Area T) that are extracted from other market participants, and this will move competition from the market sphere

[17] See George J. Stigler, The Theory of Economic Regulation, 2 Bell J. Econ. & Mgmt. Sci. 3, 3 (1971).

[18] See Tullock, supra note 13, at 674. Gordon Tullock was an American economist. He is famous for several important contributions to political economy including the founding of Public Choice, rent seeking, and for our purposes, the transitional gains trap. See Roger D. Congleton, The Political Economy of Gordon Tullock, 121 Pub. Choice 213, 217, 219 (2004).

[19] This graph is an amended version of the graph found in Robert D. Tollison & Richard E. Wagner, Romance, Realism, and Economic Reform, 44 Kyklos 57, 60 (1991).

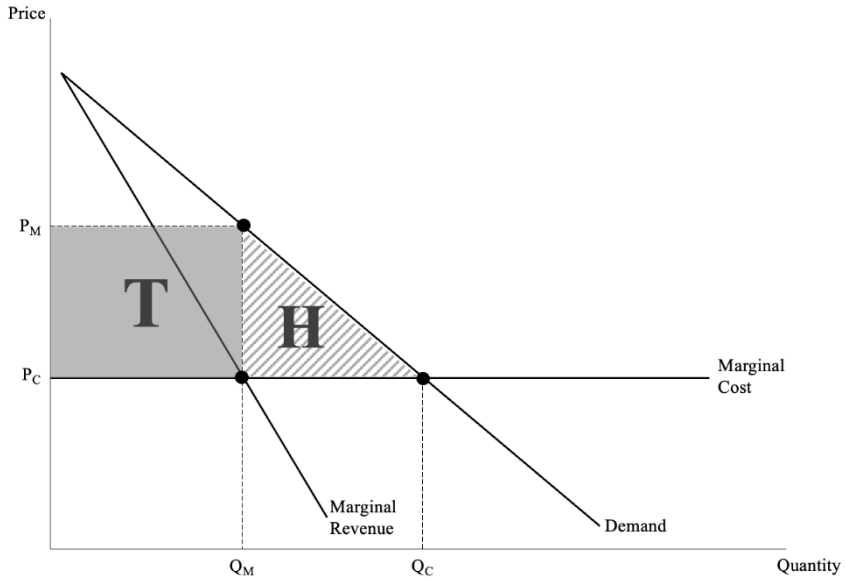

Figure 1: The Transitional Gains Trap

to the political sphere. Firms will expand resources in the political arena—crucially, without creating wealth—to attempt to capture these rents. The resulting political competition will result in further losses, as illustrated by Square T (often referred to as the Tullock Rectangle).

This competitive process is also inefficient because the resources being used (unlike in a competitive market economy) are not contributing to productive ends but are instead seeking a transfer. This concept has come to be known as rent-seeking.[20] By moving the competitive process from a market setting to a political process, resources are used in unproductive ways.[21] This same competitive process—of using resources in an unproductive way—eventually erodes away the abnormal profits from firms who hold the privilege. This results in an inefficient market with no excess gains as a result. And there is no guarantee that the small- and medium-sized firms will hold

[20] See Gordon Tullock, The Welfare Costs of Tariffs, Monopolies, and Theft, 5 W. Econ. J. 224, 226 (1967); Anne O. Kruger, The Political Economy of the Rent-Seeking Society, 64 Am. Econ. Rev. 291, 295 (1974); Jagdish N. Bhagwati, Directly Unproductive, Profit-Seeking (DUP) Activities, 90 J. Pol. Econ. 988, 989–90 (1982).

[21] See William J. Baumol, Entrepreneurship: Productive, Unproductive, and Destructive, 98 J. Pol. Econ. 893, 894 (1990).

onto control of the regulation in the end.[22] Larger firms, by controlling more capital which can be used politically, are also more likely to capture the regulation than the smaller firms, and with less capital. This is what happened with antitrust legislation during the early twentieth century.[23] Small- and medium-sized businesses were responsible for the enactment of the Sherman Antitrust Act of 1890, but by 1914, a group of labor unions and big businessmen captured the regulation to their ends. The result helped big businesses eliminate certain competitors, which kept potential competitors out of the market and prices high.[24]

The bad news is that the current cannabis markets are being shaped by the very things Tullock feared and worried about. In Tullock's estimation, the only way to avoid the transitional gains trap is to not allow it to take hold in the first place. For the most part, he is correct. Concentrated benefits and dispersed costs lead to dangerous incentives for all involved where those who gain have the upper hand. Luckily, Diana W. Thomas shows that escaping the trap is not necessarily as impossible as Tullock and others have argued.[25] Still, once in place it can be exceedingly difficult to remove. Thus, the existing array of state policies and regulations regarding cannabis ultimately insulates select special interests from competition, generating monopoly profit potentials in the process, and creating a transitional gains trap. This suggests that any proposal to change public policy regarding cannabis will face substantial obstacles as the existing vested interests compete politically to protect their granted privileges. Determining how best to move forward with structuring federal cannabis legalization given the difficulties of overcoming those vested special interests will be paramount in federal cannabis policy discussions. With the current climate on cannabis, policymakers need to take care in how they move forward with structuring cannabis legislation. How to move forward, however, requires an understanding of

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[22] Whether or not a transitional gains trap will continue with federal legalization will depend on the new institutional regime and whether the same barriers to competition are put in place. This is why the DCC is a danger to the status quo. If allowed to stay in effect, it would introduce competition, which would eliminate the trap.

[23] See Peter J. Boettke, Thomas K. Duncan & Nicholas A. Snow, Competition for Antitrust: The National Civic Federation and the Founding of the Federal Trade Commission, 7 J. Prices & Mkts. 1, 3–4, 6 (2019). See generally Gabriel Kolko, The Triumph of Conservatism: A Reinterpretation of American History, 1900-1916 (1st ed. 1963) (providing richer historical context and examples of how anti-trust legislation concentrated power to larger firms at the expense of their smaller competitors).

[24] Boettke et al., supra note 23, at 6.

[25] Thomas argues that technology allows entrepreneurs to innovate around legal barriers. She used Medieval German brewers as an example and showed how they used hops to innovate around a monopoly on beer. See Diana W. Thomas, Deregulation Despite Transitional Gains: The Brewers Guild of Cologne 1461, 140 Pub. Choice 329, 330 (2009).

the current federal cannabis policy landscape and how previously policy changes led to that status quo.

B. The Policy Status Quo and How We Got Here

The Marihuana Tax Act ("MTA") of 1937 is often cited as the U.S. federal government's first step toward shaping the current cultural and legal landscape regarding cannabis.[26] The MTA did not criminalize the use or possession of cannabis, though several states began adopting bans, starting with Massachusetts in 1911, and followed by California, Indiana, Maine, and Wyoming in 1913.[27] Within twenty years, thirty states had criminalized cannabis.[28] The MTA did, however, give the U.S. federal government the power to tax and regulate cannabis.[29] The taxes imposed were substantial and, in addition to the expected importers, growers, processors, and sellers, they were applied to health professionals who had up to that point been exploring the potential medical uses of cannabis. The taxes were prohibitive in nature, and the required paperwork for any transfer of the product was burdensome. The end result of the MTA was a de facto prohibition of cannabis: the MTA minimized legal transactions of cannabis, slowed the development of medical cannabis discovery, and criminalized unregistered cannabis possession, which was enforced by the Bureau of Narcotics.[30]

The MTA was overturned in 1969 in *Leary v. United States*, with the Supreme Court ruling that the Act violated the Fifth Amendment.[31] The Act was replaced in 1970 with the Controlled Substances Act ("CSA"), which established cannabis as a Schedule I substance with "no currently accepted medical use" and a "high potential for abuse."[32] This has largely remained the federal legal landscape to date.

That said, there have been some noteworthy changes since 1970. In 2014, the Rohrabacher-Far Amendment passed, which prohibits the Department of Justice from interfering with state medical cannabis laws. This largely

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[26] Marihuana Tax Act of 1937, Pub. L. No. 75-238, 50 Stat. 551 (1937).

[27] George Fisher, Racial Myths of the Cannabis War, 101 B.U. L. Rev. 933, 949 (2021).

[28] Angela Dills, Sietse Goffard, Jeffrey Miron, & Erin Partin, The Effect of State Marijuana Legalizations: 2021 Update, Cato Inst. Pol'y Anal. No. 908 (February 2021).

[29] See generally David F. Musto, The 1937 Marihuana Tax Act, 26 Gen. Psychiatry 101 (1972) (explaining the causes and effects of the Marihuana Tax Act of 1937 and the authority it granted the federal government in enforcement of drug laws).

[30] See Brian Gilmore, Again and Again We Suffer: The Poor and the Endurance of the War on Drugs, 15 UDC L. Rev. 59, 64 (2011).

[31] 395 U.S. 6, 12 (1969).

[32] 21 U.S.C § 812(b).

formalized the content included in the Cole Memorandum.[33] The 2018 Farm Bill, or the Agriculture Improvement Act of 2018, legalized low-THC hemp and hemp-derived products such as cannabidiol (also known as "CBD"), fully de-scheduling low-THC cannabis products at the federal level.[34] Then, in 2022, the Medical Marijuana and Cannabidiol Research Expansion Act eased restrictions on medical cannabis research.[35]

State-specific legalizations present challenges to existing federal law and make future federal action a near certainty. As of January 2024, twenty-four states plus the District of Columbia, whether through legislative action or ballot measure, have fully legalized cannabis possession for medicinal and adult recreational use, though retail sales of cannabis are not yet permitted in all of these states as states often require an additional one to two years to establish regulatory regimes, licensing procedures, and taxes.[36] As of January 2024, an additional fourteen states have legalized medicinal cannabis with Kentucky joining the list in 2025.[37] This web of complex state legalizations in a federal environment in which cannabis is illegal creates confusion, risk, high costs and prices, and extensive lobbying. As a result, many of the legal debates have centered on cannabis's effects on individual and social behavior, including educational outcomes, alcohol and drug use, suicide, crime, and traffic fatalities.

In sum, the persistent placement of cannabis on the federal Controlled Substances Schedule I list creates a major issue in the legal status quo such that states can enact laws and regulations that privilege their own cannabis producers at the expense of others. The results of the legal status quo are protectionist state policies and a transitional gains trap.

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[33] The Cole Memorandum was a Department of Justice memo written by Deputy Attorney General James Cole in 2013. This memo essentially established the federal policy after the first states legalized. See Lisa Rough, The Cole Memo: What Is It and What Does It Mean?, Leafly (Jul. 28, 2020), https://www.leafly.com/news/politics/what-is-the-cole-memo.

[34] Agriculture Improvement Act of 2018, Pub. L. No. 115-334, § 10113, 132 Stat. 4490, 4908–14 (2018).

[35] Medical Marijuana and Cannabidiol Research Expansion Act, Pub. L. No. 117-215, 136 Stat. 2257 (2022).

[36] See Israel Sepulveda, Marijuana Laws by State for 2025. Where is Marijuana Legal?, Cover Cannabis (Jan. 14, 2025) (chronicling up-to-date state-by-state details on marijuana legalizations). DISA also provides regular updates regarding state-level marijuana policy; Marijuana Legality By State, DISA, https://disa.com/marijuana-legality-by-state (last visited Mar. 10, 2025).

[37] Id.; Marina Johnson & Olivia Evans, Medical Marijuana is Legal in Kentucky on Jan. 1. Here's the Ultimate Guide to the Program, Courier Journal (Jan. 1, 2025), https://www.courier-journal.com/story/news/local/2025/01/01/kentucky-medical-marijuana-guide-to-navigating-cannabis-program/76825881007/.

C. How the Status Quo is, itself, a Transitional Gains Trap

The best protection against the transitional gains trap is to stop its emergence in the first place. The current status quo is not something to be optimistic about in this regard. Given federal cannabis policy, states have been not only left to their own devices but have been essentially granted the ability to restrict competition. Firms operating in the states that have legalized cannabis certainly enjoy, by default, less competition thanks to federal and other state prohibitions. This is not something they will want to give up willingly. The states themselves are also interested parties, as the current legal landscape allows for high excise taxes and regulations that keep the trade within their own territory.

Thus, the current regulatory regimes set up by the states that have already legalized cannabis will face abrupt changes upon federal legalization. But these changes might be a means of escaping the current trap. To escape the current trap, we argue that a constraint like the DCC cannot be removed to privilege a few first-movers. This is because protecting the first movers is tantamount to the sunk cost fallacy, and propping up existing protectionist policies—policies that only exist at present because cannabis is illegal at the federal level—will harm potential competitors and consumers.

So, what is the evidence that the legal landscape for cannabis has led to a transitional gains trap? One just needs to look at some of the results from states that have already legalized cannabis. A running theme in many states is that the black market for cannabis is not only still around but is thriving. California, New York, and Washington offer representative stories.[38] These states have enacted laws and regulations that include high excise taxes and monopoly privileges for cannabis businesses. California, for example, legalized medical cannabis in 1996.[39] Even still, cannabis smuggling arrest rates

[38] See Thomas Fuller, 'Getting Worse, Not Better': Illegal Pot Market Booming in California Despite Legalization, N.Y. Times (Apr. 27, 2019), https://www.nytimes.com/2019/04/27/us/marijuana-california-legalization.html; Amanda Chicago Lewis, California Legalized Weed Five Years Ago. Why is the Illicit Market Still Thriving?, The Guardian (Nov. 2, 2021, 6:00 AM), https://www.theguardian.com/us-news/2021/nov/02/california-legal-weed-cannabis-industry-economy; Tiffany Devitt, Excessive Taxes, Local Control Allow California Illicit Cannabis Market to Thrive, CalMatters (Jun. 22, 2023), https://calmatters.org/commentary/2023/06/california-illicit-cannabis-market-thrive/; Tim McPhillips, Weed is Legal in New York, but the Illegal Market is Still Booming. Here's Why, PBS News (Mar. 28, 2023, 6:00 AM), https://www.pbs.org/newshour/nation/weed-is-legal-in-new-york-but-the-illegal-market-is-still-booming-heres-why; Brett Davis, 'Black Market is Thriving': WA Signs Onto Normalizing Interstate Cannabis Commerce, The Ctr. Square (Aug. 21, 2023), https://www.thecentersquare.com/washington/article_a0e9f792-406f-11ee-8d95-87175347afa3.html.

[39] Medicinal Cannabis Guidelines, State of California Dept. of Justice, https://oag.ca.gov/medicinal-cannabis (last visited Jun. 18, 2025).

have risen there by 166% since 1996.[40] And legalization for adult recreational use has not caused this number to go down. As we will discuss below, these trends are eerily similar to the effects that cigarette excise taxes have created.

Firms may not like the existing high excise taxes, but by opening the door to more competition through interstate markets, the tough realities of these cannabis markets will look even more difficult. This is why cannabis firms in these states lobby to protect their privileges. Tiffany Devitt explains that not only are excessive excise taxes problematic, but so is the licensing system in California;[41] a major problem stems from "the requirement that cannabis businesses receive permits from both the local jurisdiction and the state."[42] We agree with Devitt that this double permit structure is problematic because it will simply lead to reduced competition at the customer's expense. Essentially, California's regulatory strategy has resulted in a tragedy of the anti-commons in which overlapping jurisdictions create confusion through multiple points of authority (i.e., local, state, and federal). As competition from out of state increases, the remaining legally-operating firms become weaker, incentivizing them to maintain the status quo despite the dissipated rents created by the transitional gains trap.

To overcome a transitional gains trap, simply acknowledging that the Harberger triangle is larger than the Tullock Rectangle is insufficient. Unless the rents available on the other side of the transition are larger than the current ones (i.e., the Rectangle post-transition is larger than the Rectangle pre-transition), there is little incentive to change (even if the current inefficiencies are overwhelming), thus the trap. Entrepreneurs in cannabis markets, as well as the policymakers and regulators whom the entrepreneurs inform and lobby, will undoubtedly prefer the status quo to federal legalization that will hurt their businesses.

This is further complicated by that which is not seen, a la Frédéric Bastiat.[43] If federal legalization opens the door to more efficient interstate

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[40] Joseph Detrano, Cannabis Black Market Thrives Despite Legalization, Rutgers Ctr. Alcohol & Substance Use Stud. (CAS), https://alcoholstudies.rutgers.edu/cannabis-black-market-thrives-despite-legalization/ (last visited Jan. 17, 2025). In the case of minimum eligible cannabis offences, David Bjerk finds evidence that federal mandatory minimums lead to significant increases in expected sentencing. See David Bjerk, Mandatory Minimums and the Sentencing of Federal Drug Crimes, 46 J. Legal Stud. 93, 95 (2017).

[41] Devitt, supra note 38.

[42] Id.

[43] See generally Frédéric Bastiat, What is Seen and What is Not Seen (1850), *reprinted in* 3 The Collected Works of Frédéric Bastiat (Jacques de Guenin, ed., Liberty Fund 2017) (ebook) (illustrating Bastiat's point that a good economist not only looks at what we can plainly see but also the unseen, what was given up and what did not transpire as a result, as well as the unintended consequences of any action).

production, distribution, and sales due to the economies of scale of larger corporations, particularly those with adjacent industry experience, it is probable that these larger corporations will be able to offer products on a greater scale and at lower cost than their smaller competitors. Consequently, we would likely observe local "mom and pop" cannabis companies struggling to compete and going out of business.[44] We would then observe these "mom and pop" companies going from profitable to bankrupt as a result of the federal legalization of cannabis. Those entrepreneurs and their proponents have a significant incentive to fight considerably, and at great expense, to avoid that outcome.

However, just because that path comes at a cost, we cannot assume that an alternative federal legalization strategy that is less costly to specific cannabis entrepreneurs is less costly to society as whole. Unseen costs come from granting monopoly privileges to small-scale producers whose profitability only exists due to inefficiencies in state-level legalization. These privileges will persist in a federally legalized market because their incumbent position under state-level legalization creates a first-mover advantage upon federal legalization, including the ability to influence future regulation to protect profitability. Although these incumbent producers benefit from these profits, these profits are only the byproduct of an inefficient regulatory landscape, so they come at a cost to consumers, future competitors, and would-be competitors who can no longer viably enter the market. The costs are also incurred by the cross-state businesses that were never able to legally enter the market.

There are costs going forward, whether protectionist policies are adopted or not. But extending the existing regulatory landscape to the federal level will impose non-zero costs on competitors and consumers. Because there is no costless path forward, we must consider how costly each option is and to whom.

III. TRANSITION TO FEDERAL LEGALIZATION—MIND THE IMPENDING TRAP

With insights from Tullock and Bastiat in mind, we can regard many of the federal legislative proposals on the table as attempts to escape the transitional gains trap. For any of these bills to gain traction and to incentivize current cannabis entrepreneurs and policymakers to support them, they must

[44] Transitional gains traps pose problems for small businesses because they do not have the capital to compete politically in the lobby efforts the way larger firms would.

contain the promise of rents on the other side of the transition that exceed the rents they currently enjoy. However, these exact promises of policy to limit competition will lay the groundwork for a new transitional gains trap. Federal policymakers are stuck between a rock and a hard place. On the one hand, to escape the current trap created by exclusively intrastate cannabis commerce, they need political incentives for leverage. Yet the very leverage that will free us from the current trap will land us squarely in a new one. Therefore, if political incentives, such as licenses that limit intrastate competition, protection from competition across state borders, and tax credits, are not offered to entice incumbent firms to favor federal legalization and make the transition incentive compatible, then we are stuck in the original trap.

Let us consider some of the current federal legislative proposals through this framework. At the time of writing, it is unclear what specifically will happen regarding federal legislation, but it looks like it is a question of when, not if. The loosening of federal cannabis policy mentioned above has sparked a flood of changes at the state level. Given the changing laws and policies at the state level, and weakening public support of cannabis prohibition, it seems almost inevitable that federal changes will occur, and efforts to legalize cannabis on the federal level have already started. But details are important, so we must ensure we understand the full structure and consequences of the coming federal legalization (or at least decriminalization) of cannabis.

A. Slow Moving Federal Reforms

In the summer of 2021, Senate Democratic leaders introduced the Cannabis Administration and Opportunity Act.[45] The Act would have decriminalized marijuana at the federal level and given states autonomy to prohibit or otherwise regulate cannabis without federal interference. It did contain heavy excise taxes and faced steep difficulties in gaining the necessary political support to pass, as many federal lawmakers have been slow to update their voting positions on cannabis, despite growing public favorability for cannabis legalization, and have been resistant to change.[46]

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[45] Cannabis Administration & Opportunity Act, S. 4591, 117th Cong. (2022).

[46] See, e.g., Natalie Fertig, Schumer's Legal Weed Bill is Finally Here, Politico (Jul. 21, 2022, 2:58 PM), https://www.politico.com/news/2022/07/21/schumer-legal-weed-bill-00047058 (discussing bipartisan differences in voting for federal cannabis bills and pessimism amongst federal policymakers in acquiring sufficient votes).

A more promising bill was the Strengthening the Tenth Amendment Through Entrusting States Act ("STATES Act").[47] Originally introduced in 2018 with bipartisan support, the bill sought to exempt individuals from the federal CSA laws if they were not in violation of state laws regarding cannabis.[48] Still, some policymakers saw the original version as too limited in scope.[49]

A third major act, with an oddly similar name, the States Reform Act, was introduced in 2021.[50] This act would have implemented a process for federal regulation, like the process seen in the alcohol industry, and it attempted to address interstate transportation of cannabis. After stalling in Congress in the midst of multiple bills addressing federal cannabis reform, the States Reform Act was reintroduced in October 2023 as House Bill 6028, where it is currently under review by House subcommittees.[51]

The most recent relevant bill at the time of writing is the STATES 2.0 Act, which was introduced in December 2023.[52] Like the original STATES Act proposal, the STATES 2.0 Act would declassify cannabis under the CSA and would federally legalize state-legal cannabis so long as interstate commerce was not inhibited.[53] This bill would also allow for states to make cannabis illegal and to introduce more stringent rules and regulations regarding its consumption, production, distribution, and sale. However, under the Act, state laws and regulations may not treat in-state businesses preferentially compared with out-of-state businesses. Section Three of the Act specifically addresses the interstate transport of cannabis, stipulating that such transport would be legal, even if traveling through states in which cannabis is locally illegal, provided it is legal at the origination and destination states.[54] Furthermore, the STATES 2.0 Act, like the States Reform Act, stipulates that the Alcohol Tobacco Tax and Trade Bureau would serve as the rulemaking body for commerce in cannabis products.[55] States would still maintain

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[47] Strengthening the Tenth Amendment Through Entrusting States Act (STATES Act), H.R. 2093, 116th Cong. (2019); STATES 2.0 Act, H.R. 6673, 118th Cong. (2023).

[48] Jeffrey A. Singer, STATES Act 2.0 Would Make the Federal Government More in Sync with the States and the People on Marijuana, Cato at Liberty Blog (Dec. 8, 2023, 12:19 PM), https://www.cato.org/blog/states-act-20-would-make-federal-government-more-sync-states-people-marijuana.

[49] See Geoffrey Lawrence, Frequently Asked Questions About STATES Act 2.0, Reason.org (Dec. 14, 2023), https://reason.org/backgrounder/frequently-asked-questions-about-states-act-2-0/.

[50] States Reform Act, H.R. 5977, 117th Cong. (2021).

[51] House Members Reintroduce Legislation Repealing Federal Marijuana Prohibition, NORML (Nov. 2, 2023), https://norml.org/news/2023/11/02/house-members-reintroduce-legislation-repealing-federal-marijuana-prohibition/.

[52] STATES 2.0 Act, H.R. 6673, 118th Cong. (2023).

[53] Id.

[54] Lawrence, supra note 49.

[55] Id.

authority to establish stricter regulation for their own markets under the STATES 2.0 Act.

B. An Argument for Suspending the DCC

Despite gaining traction in federal policy and public opinion, federal cannabis legalization is not operating full steam ahead. The most significant contestation over how cannabis will be legalized federally pertains to how cannabis will be treated under the DCC. And this debate about cannabis and interstate commerce is ongoing at the policy level and in the academic discourse. To date, Scott Bloomberg and Robert A. Mikos give the most thorough and strongest argument in favor of suspending the interstate commerce clause, at least initially, in cannabis markets upon federal legalization.[56] Given the depth of Bloomberg and Mikos's analysis, as well as their deference to concerns that correspond with our own, we will leverage insights and proposals from their argument to articulate why a suspension of the interstate commerce clause in cannabis markets would precisely illustrate the aforementioned trap-to-transition-to-trap concern.

Bloomberg and Mikos describe how, when the federal government legalizes cannabis, the DCC will take effect, disrupting current cannabis markets in states where it is presently legal.[57] In response to this concern, the authors do not suggest that the federal government should refrain from legalizing cannabis but instead propose that Congress temporarily suspend the DCC so that current actors in state-level cannabis markets (including cannabis producers, cannabis sellers, and state and local policymakers) may adapt to the new landscape.

Suspending the DCC, Bloomberg and Mikos argue, would permit Congress to legalize cannabis but also give state and local policymakers time to craft regulations that address the operational realities of a legal cannabis market.[58] The regulatory framework in states where cannabis is presently legal shape and have been shaped by the intricacies and complexities of the state-specific cannabis market, Bloomberg and Mikos argue.[59] Without

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[56] See Scott Bloomberg & Robert A. Mikos, Legalization Without Disruption: Why Congress Should Let States Restrict Interstate Commerce in Marijuana, 49 Pepp. L. Rev. 839 (2022).

[57] Id.

[58] Id. at 845.

[59] Id. at 847 ("In each legalization state, a state agency—or sometimes multiple agencies—has the power to license different types of marijuana businesses and to promulgate regulations governing those businesses. The licensing and regulatory choices made by the various states have shaped the character of their respective marijuana marketplaces, from big-picture issues regarding how marijuana businesses are structured and licensed, down to the minutiae of how those businesses operate on a day-to-day basis.").

keeping the state-level regulations in place, Bloomberg and Mikos fear that federal legalization would "inadvertently creat[e] gaps in the regulation of the marijuana industry—namely, scenarios where there is effectively no state *or* federal law governing the industry."[60] They go on to suggest that suspending the DCC would empower states to maintain their "closed-loop systems" which would "provid[e] states with detailed information about regulated activities, . . . greatly enhanc[ing] the states' ability to enforce their regulations on the marijuana market."[61]

To clarify the ramifications of federal legalization they anticipate—due to the holes and bottlenecks in the disconnect between state- and federal-level regulation brought on by the DCC—Bloomberg and Mikos directly point to concerns such as product testing and labeling, tax evasion, and child labor. "It is difficult to overstate the pressure that states will face to keep or attract marijuana firms. The marijuana industry is booming."[62] As states vie for more cannabis business, Bloomberg and Mikos fear that corners may be cut, and that enforcement of regulation will be difficult while courts hash out which regulations are permissible across states. "In the wake of [state-level testing regulation being blocked by the DCC], vendors could sell untested and potentially unsafe marijuana products while lawmakers scramble[] to find a way to plug the gap created by the DCC."[63] As they state regarding child labor, "[b]ecause other states could not block the sale of marijuana produced elsewhere by, say, eighteen-year-olds, states will feel pressure to follow suit and drop their own age requirements, thereby setting in motion the proverbial race to the bottom."[64] States without preexisting regulations will also be affected by the DCC.

In addition to supplying policymakers with adequate time and tools to regulate effectively and stave off the aforementioned dilemmas, Bloomberg and Mikos are also concerned about the consequences to existing firms as they must transition from competing and complying with regulations within state-level cannabis markets to competing at the national scale. Short of at least temporarily suspending the DCC for cannabis, Bloomberg and Mikos argue that "almost overnight, the DCC would make obsolete investments that thousands of firms have made in existing state regulatory systems and insular state markets."[65] They go on to argue that "[i]t is difficult to overstate

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[60] Id. at 861.
[61] Id. at 862.
[62] Id. at 867.
[63] Id. at 862.
[64] Id. at 867.
[65] Id. at 844. We believe it is more accurate to say federal legalization could make investments obsolete. It would depend upon the structure the new regulations take.

the ramifications this development would have for state regulators and marijuana markets. Existing state regulations that insulate local firms from outside competition, including ubiquitous import-export bans and residency preferences for marijuana licenses, plainly would not survive a DCC challenge."[66]

A specific group of incumbent cannabis licensees that would be directly affected if the DCC is not suspended are beneficiaries of state-level social equity programs. In an effort to correct for past injustices of the War on Drugs,[67] "many states give preference to marijuana business license applicants who belong to groups that were disproportionately harmed by their drug policies."[68] These programs exist precisely to help firms that in an otherwise competitive market would not exist.

Why would these social equity programs not remain successful at the national level if the DCC were to remain intact upon legalization? As Bloomberg and Mikos explain, "[a]t the core of these social equity programs lies a law that facially discriminates against non-residents," and they point out that "[l]imiting . . . social equity programs to state residents almost certainly violates the DCC."[69] In the overwhelming majority of industries in which the DCC is applicable, "states ordinarily cannot restrict imports and exports of goods from other states."[70] However, since cannabis is illegal at the federal level, state regulations can treat in-state licensees, including social equity licensees, preferentially relative to out-of-state firms without violating the Commerce Clause. "In addition to states' express import-export prohibitions [on cannabis], some states restrict non-residents from owning marijuana businesses. These ownership restrictions can take the form of an absolute bar on non-resident ownership, or they can be structured as a preference

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[66] Id. at 859.

[67] See Decio Coviello & Nicola Persico, An Economic Analysis of Black-White Disparities in the New York Police Department's Stop-and-Frisk Program, 44 J. Legal Stud. 315, 315 (2015) (finding evidence that New York Police Department officers are not biased against African Americans in regards to the officers' choice to stop individuals as part of the Stop-and-Frisk Program, alongside results that do suggest there is bias in the police department's choices to frisk in general).

[68] Bloomberg & Mikos, supra note 56, at 851.

[69] Id. at 871. Bloomberg & Mikos further write:

> Pursuant to these programs, many states give social equity applicants preference in marijuana business licensing—sometimes by awarding them extra points in a competitive licensing process and sometimes by making licensing opportunities exclusive to such applicants. States give social equity applicants a range of other benefits as well, from exclusive funding programs, to fee waivers, to specialized training and educational opportunities.

Id. at 870.

[70] Id. at 850–51.

whereby residents receive extra points in a competitive licensing process."[71] The ability to discriminate against non-residents to the benefit of residents underpins the viability of state-level social equity programs, allowing small, resident firms to compete.[72]

Concerns over federalism are also a component of the argument put forward by Bloomberg and Mikos. They explain that "abruptly nationalizing the marijuana market would be inequitable both to states that have already legalized marijuana and to states that have not yet done so" and "transitioning immediately from state-based markets to a national market would prematurely terminate state experimentation with different approaches to regulating marijuana."[73] They go further to explain that upon federal legalization, cannabis production would relocate to states with regulations that are more favorable to producers, thus bringing harm to the states from where these producers depart and windfalls to the states to which they relocate.[74] The losses to many of these states, they argue, is magnified by the considerable time and resources that firms put in to comply with state-level regulation, only to have those investments and jobs destroyed by federal legalization.[75]

According to Bloomberg and Mikos, "[b]eyond repealing federal prohibition, all congressional reform proposals purport to leave the regulation of marijuana largely if not quite exclusively in the hands of the states,"[76] so moving forward, it seems that it is likely that states will be left to regulate cannabis on their own. Under federal cannabis prohibition, Bloomberg and Mikos suggest that horizontal federalism concerns create an additional reason for states to establish insular, state-level cannabis markets as "states instituted these restrictions to reduce friction with states that had stricter marijuana rules or prohibited the substance entirely."[77] How this will evolve, if the DCC is still actionable in cannabis markets, is a concern for Bloomberg and Mikos. They explain that when state-level cannabis legalization was gaining traction, "states chose to restrict interstate marijuana transactions as a means of warding off federal interference in their marketplaces."[78] By keeping the DCC at bay in cannabis markets, Bloomberg and Mikos believe

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[71] Id. at 851.

[72] Id. at 873–74 ("Extant congressional reform programs would suddenly throw businesses owned by social equity licensees into a national market populated by large, well-capitalized producers that are able to leverage economies of scale. The emergence of the national market would likely make it difficult for many smaller scale producers, including social equity applicants, to compete.").

[73] Id. at 879–80.

[74] Id. at 880.

[75] Id. at 880–81.

[76] Id. at 854.

[77] Id. at 852.

[78] Id. at 851.

"[t]he federal government could . . . benefit from seeing how states regulate their marketplaces once marijuana is federally legal," and "leave states the option to engage in interstate commerce, should they so choose."[79]

However, they are not without their concerns about the unintended long-term consequences that could arise from the suspension of the DCC. Bloomberg and Mikos acknowledge that "allowing protectionism could spark hostilities among the states" and protectionism "blocks the development of a more efficient national market."[80]

In fact, protectionism is offered by Bloomberg and Mikos as another explanation for the insular nature of state cannabis markets prior to federal legalization in the first place: "states restricted interstate commerce in marijuana to advantage their residents and to guard their fledging marijuana industries from out-of-state competition."[81] By including a sunset clause of seven years, Bloomberg and Mikos argue that their proposal strikes a balance between these competing concerns because the "sunset clause would help to limit the potential costs of suspending the DCC without necessarily sacrificing the benefits [Bloomberg and Mikos] foresee."[82]

The suggestion of suspending the DCC that Bloomberg and Mikos are putting forward can be analyzed as an attempt to overcome the present transitional gains trap outlined in Part II. By creating a set of rules that would not cause the incumbent firms established under the state-level legalization regime to entirely lose their privileged status upon federal legalization, Bloomberg and Mikos present a path forward that will not incentivize those very incumbents to expend resources to fight federal legalization. This will increase the likelihood of federal legalization being successful, particularly if incumbent cannabis firms are the most likely interest group to lobby to prevent federal legalization. However, as we explain in Parts IV and V, we are skeptical of the long-term outcomes of this proposal and any proposal that seeks to undermine constitutional constraints to favor special interest groups. Our skepticism and criticism stem not from the concerns that Bloomberg and Mikos raise, nor from their intentions, as we generally agree with most of their diagnoses and many of their concerns regarding the present status of cannabis markets leading up to federal legalization. Instead, we are concerned with the unintended consequences that public choice theory and new institutional economic theory tell us are likely.

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[79] Id. at 883.
[80] Id. at 893.
[81] Id. at 852.
[82] Id. at 891.

IV. AVOIDING THE DAWN OF A NEW TRANSITIONAL GAINS TRAP

While Bloomberg and Mikos note valid concerns related to federalism and regulatory uncertainty when recommending DCC suspensions, the consequences of their proposal outweigh the benefits. As we outlined in Part III, Bloomberg and Mikos suggest that suspending the DCC would provide the necessary latitude for states with similar regulatory requirements to cooperate with one another and establish import-export agreements. However, this same latitude has already been largely available to states. States have had ample opportunity to consider interstate agreements prior to federal legalization when the DCC was functionally inactive in cannabis markets, and yet, legal interstate commerce in cannabis is nearly non-existent. Thus, it is not clear why we should expect this to happen moving forward if the DCC remains suspended. In Part IV, we will address why we believe suspending the DCC, even with a sunset clause, is a dangerous move. In the following Part V, we will provide other examples of sunset clauses failing.

Notwithstanding our belief that suspending the DCC would be dangerous, it is true that there may also be dangers related to outright, unconstrained federalism. First, economist Bryan Caplan examines how property taxes make the supposed benefits of competition across jurisdictions, also known as the Tiebout Effect, more difficult to realize because property values are affected by state policies and are thus reflected in property prices that have lasting power in every state.[83] Property taxes make it more costly for states to move from a "bad" policy state into a "good" policy state, though states are in competition with one another. Therefore, states are unlikely to adjust their cannabis policies even to align with their constituents' wishes reflected in the competitive market.

Second, Michael S. Greve makes the case that rather than a competitive outcome, the result of federalism could very well lead to collusion instead.[84] The federal government could withhold funding on the specific budget items states need to push their desired policy outcomes. This would lead to states converging on the same policy as if federalism did not even exist, as

[83] See Bryan Caplan, Standing Tiebout on His Head: Tax Capitalization and the Monopoly Power of Local Governments, 108 Pub. Choice 101, 101 (2001).

[84] See generally Michael S. Greve, The Upside-Down Constitution (2012) (explaining how federalism can take the form of "cartel federalism" instead of "competitive federalism," and as a result, under cartel federalism, power is concentrated through the collusion of state governments, resulting in higher taxes, greater state-level regulation, etc.).

exemplified in the market for alcohol with the legal drinking age.[85] States are permitted to choose their own laws as to the age when alcoholic beverages can be sold. Today, however, all states have set the drinking age to twenty-one years.[86] Historically, Louisiana attempted to set its drinking age at eighteen, but the federal government withheld highway funding, forcing the state to fall into line similarly to South Dakota.[87]

These are serious concerns for federalism, but we believe there is an even greater concern. Unleashing federalism by suspending the DCC opens up—or more accurately, keeps open—the likelihood of protectionism within each state. The proposal to suspend the DCC, however well-meaning, would create new opportunities for special interests to use legislation to their own gain, essentially shifting market competition to political competition. The venue of political competition, as discussed in Part II.I, results in zero or negative-sum outcomes that favor more politically connected special interest groups at the expense of the public.

In contrast, market competition results in positive-sum outcomes, as consumers are made better off when producers, in the pursuit of profit, lower prices, cut costs, and improve quality. Market competition ensures producers only succeed when they provide a valuable service to consumers for which the consumers are willing to pay. In so doing, value is created for both sides of the market, and thus the outcome is positive sum. Suspending the DCC for cannabis would undermine the prevalence of positive-sum exchanges in the cannabis market.

The DCC is far from an "arcane constitutional doctrine that is ill-suited for the task," as suggested by Bloomberg and Mikos.[88] Instead, the DCC is a constitutional constraint that prevents states from enacting legislation that would benefit particular in-state firms—at the expense of consumers—by significantly limiting out-of-state competition. By acting as a constitutional constraint on the state's ability to regulate, the DCC restrains the state's ability to block competitors from other states and, in turn, protects consumers and firms from cronyism. The DCC cannot be suspended without necessarily

[85] See generally Jeffrey A. Miron & Elina Tetelbaum, Does the Minimum Legal Drinking Age Save Lives?, 47 Econ. Inquiry 317 (2009) (empirically estimating the effect of raising the legal drinking age as well as the Federal Uniform Drinking Age Act on the number of traffic fatalities of underage drivers).

[86] Id.

[87] National Minimum Drinking Age Act of 1984, Pub. L. No. 98-363, § 158, 98 Stat. 435, 437 (1984); Manuel v. Louisiana, La. 692 So.2d 320, 95-2189 La. 3 (1996); South Dakota v. Dole 483 U.S. 203 (1987).

[88] Bloomberg & Mikos, supra note 56, at 845.

ceasing market competition's positive-sum game in favor of rent extraction which is, at best, a zero-sum game, or a negative-sum game in many cases.[89]

This transformation would occur because the market process by which entrepreneurs should determine how to allocate resources would no longer account for the relevant and dispersed knowledge of time and place found in the market; instead, the political process would rule.[90] The political process encourages entrepreneurs to allocate their efforts and scarce resources to other activities for which they are better suited to provide feedback, such as the processes of rent-seeking and rent-extraction. Therefore, efforts to create and extract new rents as well as to protect existing rents are rewarded via the political process rather than efforts to create the highest-valued, most productive use of a resource.[91]

Because the primary goal of every firm is to maximize their individual profits, firms will always expend resources by lobbying in the political realm if it means they can reduce or eliminate market competitors.[92] The suspension of the DCC presents this problem precisely. Ultimately, we think Bloomberg and Mikos are correct in their argument about the need to be careful with how legalization at the federal level is implemented and what role in regulation is given to the states. The problem, as we have argued, is that their proposal to temporarily suspend the DCC would fail to achieve their intended goals of market adaptation and instead open the door to special interests to compete on the political level. The "profits" sought and competed for would go from productive to unproductive.

Furthermore, the problems raised by Bloomberg and Mikos of smuggling, tax evasion, and regulatory gaps may persist or even be exacerbated by suspending the DCC. Currently, under a regulatory regime in which the DCC has no bearing on cannabis markets, cannabis companies in California are estimated to owe approximately $732 million in unpaid taxes in addition to an estimated $173 million in taxes from illegal cannabis sales.[93] "These

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[89] See Gordon Tullock, Rent Seeking as a Negative-Sum Game, *in* Toward a Theory of the Rent-seeking Society 16, 31 (James M. Buchanan, Robert D. Tollison & Gordon Tullock eds., 1980); Russell S. Sobel, Testing Baumol: Institutional Quality and the Productivity of Entrepreneurship, 23 J. Bus. Venturing 641, 642 (2008).

[90] See Israel M. Kirzner, The Perils of Regulation: A Market-Process Approach, *in* Discovery and the Capitalist Process 119, 129–33 (1985).

[91] See Raymond J. March, Adam G. Martin & Audrey Redford, The Substance of Entrepreneurship and the Entrepreneurship of Substances, 5 J. Entrepreneurship & Pub. Pol'y 201, 201 (2016).

[92] See Tullock, supra note 20, at 228; Stigler, supra note 17.

[93] Rolando Garcia, California Cannabis Industry Is Drowning in Debt: $732M Owed in Taxes, 72% By Companies Already Closed Down, Benzinga (Apr. 23, 2024, 2:43 PM), https://www.benzinga.com/markets/cannabis/24/04/38387994/california-cannabis-industry-is-drowning-in-debt-732m-owed-in-taxes-72-by-companies-already-clos.

illegal sales could represent about a quarter of the market, with an estimated total of $1.2 billion."[94] The concern regarding smuggling is hardly eliminated by the suspension of the DCC. Similar to cigarette markets, which we consider in greater detail in Part V, frictions could increase across state lines following DCC suspension, causing smuggling to become a more attractive arbitrage opportunity as taxation and regulatory policies differ.

Bloomberg and Mikos's concerns over the use of pesticides, unclear packaging, and poor product quality also persist if the DCC is suspended. Suppose a pesticide producer's competitor, say an all-natural substitute that may not even work as well, was able to effectively garner political support because it is seen as more environmentally friendly, even if less effective. The all-natural substitute could then use the political process to advance regulations that would favor an all-natural product at the expense of other market competitors. In so doing, resources are shifted away from market competition, in which consumers' willingness to pay for all-natural products versus more effective products would determine the allocation of resources, and those resources are allocated instead toward more effectively navigating the political process. The regulations resulting from the political process and DCC suspension would undermine the quality and effectiveness of the pesticides and limit competition, leading to worse outcomes and reduced efficiency.

Consider a seemingly unrelated example: various lobbying groups, including those primarily made up of tax attorneys and tax accountants, expend money and resources to fight proposals to simplify the tax code and reduce the number of loopholes. The overwhelming majority of taxpayers would benefit from a simplified process, yet the length and complexity of the federal tax code has only grown over the past half-century because tax attorneys and tax accountants have made significant investments that would be threatened by a simpler tax code. And that is to say nothing of the tax software giants, such as Intuit and H&R Block, who actively lobby against tax code simplification reforms[95] and the IRS's most recent push to offer "free electronic tax-filing" options for taxpayers.[96]

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[94] Id.

[95] See Ben Popken, TurboTax, H&R Block Spend Big Bucks Lobbying for Us to Keep Doing Our Own Taxes, NBC News (Mar. 23, 2017, 12:47 PM), https://www.nbcnews.com/business/taxes/turbotax-h-r-block-spend-millions-lobbying-us-keep-doing-n736386.

[96] See Fatima Hussein & The Associated Press, Taxpayer Advocates Want the IRS to Offer a Free Electronic Tax-filing System. Intuit and H&R Block Have Spent Millions Lobbying Against It, Fortune (Apr. 17, 2023, 6:58 AM), https://fortune.com/2023/04/17/taxpayer-advocates-irs-free-electronic-tax-filing-system-intuit-hr-block-spent-millions-lobbying-against/.

But a complex tax code should not be kept in place just because it keeps tax attorney and tax accountant salaries sufficiently high to make the investment in their respective credentialing worthwhile. This same logic, we argue, also applies to cannabis regulation.

Bloomberg and Mikos correctly cite that there is legal precedent for the suspension of the DCC, as we discuss further in Part V.[97] However, they fail to point out any of the problems in these markets that are attributable to DCC suspension. In addition to the incentive problems highlighted here, there is also a massive knowledge problem at play in ensuring that federal, state, and local policymakers get the rules of the game correct. Bloomberg and Mikos presume that Congress, in suspending the DCC, will have access to insights about the best regulatory path forward by considering how the market develops post-legalization. But how will policymakers know which rules of the game will matter without actually seeing the marijuana market in operation?[98]

Even a temporary suspension of the DCC—which is unlikely to remain temporary—will not be without problems. If the suspension of the DCC is indeed temporary as Bloomberg and Mikos prescribe, then the market process and its activity during the DCC suspension will necessarily differ from that after the suspension is lifted. This suggests, therefore, that the insights into the market activity gained by policymakers—which is what justifies Bloomberg and Mikos's suggestion—will inaccurately reflect the market realities once the suspension is lifted. Regulations designed under such circumstances will necessarily be inadequate, thus arriving at the exact outcome Bloomberg and Mikos are trying to avoid. If their argument is that, in order to create rules for scenario A, we must force scenario A to act like scenario B and use the insights from scenario B to create rules to govern scenario A, it is not at all obvious that this experiment will lead to any fruitful insights. And in the process, this experiment would waste considerable time and resources, stall innovation and potential gains from cross-state economies of scale, and throw open a large door to rent-seeking and other zero-to-negative-sum schemes.[99]

Still, our main issue with the temporary suspension of the DCC is that it is likely to be anything but temporary. Bloomberg and Mikos write,

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[97] See Bloomberg & Mikos, supra note 56, at 845.

[98] See Friedrich von Hayek, The Pretence of Knowledge, The Nobel Prize (Dec. 11, 1974), https://www.nobelprize.org/prizes/economic-sciences/1974/hayek/lecture/ (elucidating the importance of local knowledge in the market and emphasizing the challenges faced when attempting to centrally plan the economy).

[99] See Kirzner, supra note 90 (advancing a more detailed argument about how regulation alters the discovery process).

"[a]ccordingly, we include a sunset clause to ensure that a transition measure does not become entrenched—unless, of course, Congress decides that continued suspension of the DCC is in the nation's best interest."[100] But what use is a sunset provision preventing Congress from impeding upon the productive efficiency and potential innovations of the cannabis market if Congress can simply vote to extend the suspension?

Individual members of Congress will have every incentive to keep the suspension of the DCC in place as they do not bear the costs of the suspension. Not only do they not bear the costs, but members of Congress are actively incentivized to maintain the DCC suspension as they are elected to office by citizens of their home states, including owners and employees of cannabis growers and dispensaries who will have strong incentives to fight to keep that privilege, despite normal profits. And, due to concentrated benefits and dispersed costs, the rest of those affected have little incentive to organize and fight back.[101] Consequently, the temporary suspension of the DCC will not only fail to provide a detour around the complications of regulating a newly emergent cannabis market, but it will instead pave a very short road directly into yet another—and even more deeply entrenched—transitional gains trap.

These problematic, potential consequences are not far-off possibilities that could arise in the future. Instead, they are the current realities at the state level as new entrants try to navigate their way through contradictory and incongruous regulatory regimes influenced by existing incumbents. For example, Ohio proposed a legalization bill in 2015 that was quickly captured by special interests to create monopoly power for those who held a limited number of licenses.[102] Voters saw through this and voted against the legalization effort,[103] despite overwhelming support for legalization in general.[104]

In addition, many current social equity programs are at odds with the DCC because they heavily favor in-state residents. The problem with these

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[100] Bloomberg & Mikos, supra note 56, at 898–99.

[101] See generally Mancur Olson, The Logic of Collective Action: Public Goods and the Theory of Groups (rev. ed. 1971) (articulating the myriad incentives, many times complex and incompatible incentives, that face members of groups when they attempt to overcome collective action problems, which only stand to intensify as the size of the group increases).

[102] See Audrey Wagstaff & Theresa Knopf, 'Up in Smoke': Shaping Attitudes Toward Legalizing Marijuana in Ohio, 55 Ohio Commc'n J. 64, 65 (2017).

[103] Id at 73. See Table 2 that shows the statement "I was opposed to the 'monopoly' part of the issue that would allow only 10 parcels for growing marijuana for resale" had the highest mean score of the statements that respondents were asked to rank as a factor in their decision to vote against Issue 3.

[104] David A. Graham, Why Did Ohio's Marijuana-Legalization Push Fail?, The Atlantic (Nov. 3, 2015), https://www.theatlantic.com/politics/archive/2015/11/where-did-ohios-marijuana-legalizers-go-wrong/414061/.

programs is not that they are designed to give individuals adversely affected by the War on Drugs a leg up on gaining access and recognition in legal cannabis markets moving forward. Rather, the problem is that the social equity programs do not grant access to all individuals adversely affected by the War on Drugs, instead discriminating against individuals based on their state of residence.[105]

Given the Supreme Court's recent rulings on cases involving the DCC, the considerations toward how such social equity programs can create discriminatory barriers for non-residents will be crucial. In summarizing the Supreme Court's recent decision in *National Pork Producers Council v. Ross*, Brian Frazelle, of the Constitutional Accountability Center, explains:

> the majority opinion vigorously reaffirms that the "core" of the dormant Commerce Clause is its "antidiscrimination principle," which bars measures benefitting in-state economic interests by burdening out-of-state competitors. . . . The court also rejected the notion that the dormant Commerce Clause contains an "extraterritoriality" principle, invalidating state laws whenever they have the "practical effect" of influencing conduct in other states. The opinion explains that such a rule is both unsupported by precedent and untenable, given that many kinds of valid state laws have indirect ripple effects in other states.[106]

He goes on to state that:

> having rejected the idea of expanding the dormant Commerce Clause, the court put a serious damper on the most controversial aspect of its existing doctrine—the *Pike* balancing test, which instructs courts to strike down even nondiscriminatory state laws if the burdens they impose on interstate commerce are "clearly excessive in relation to the putative local benefits." The majority opinion recasts this line of cases as *also* being primarily about economic

[105] See Dario Sabaghi, How US Constitution's Dormant Commerce Clause Is Challenging Marijuana Legislations, Forbes (Dec. 23, 2022, 6:00 AM), https://www.forbes.com/sites/dariosabaghi/2022/12/23/how-us-constitutions-dormant-commerce-clause-is-challenging-marijuana-legislations/.

[106] Brian Frazelle, Big Business Loses Dormant Commerce Clause as Tool Against States, Bloomberg L. (May 19, 2023, 4:00 AM), https://news.bloomberglaw.com/us-law-week/big-business-loses-dormant-commerce-clause-as-tool-against-states.

> protectionism. The *Pike* test, it explains, helps smoke out protectionist laws that appear neutral but cannot plausibly be explained as anything other than covert discrimination against out-of-state commerce.[107]

If understood correctly, the Court's concerns echo those of our own in that the DCC plays a critical role in safeguarding against a devolution of state-level regulation and consumer protection into state-level protectionism at the expense of the consumer. To the extent that social equity programs and other state-level licensing requirements disproportionately favor state-residents and deny access to non-residents, it is plausible that courts will see these state-level policies as discriminatory and protectionist in light of this recent decision. Consequently, federal policy proposals that encourage or do not at least address these potential pitfalls could stall the legalization process considerably while the legislation and its legal interpretation are tied up in court. This, in turn, would undermine much of the intent behind passing federal legislation to make the legal cannabis landscape easier to comply with. However, the Supreme Court's interpretation of the DCC in *Ross* would not preclude state regulations that require out-of-state residents to comply with the same standards required of in-state residents in sale of products.[108]

We have offered skepticism toward the likelihood of such a sunset clause actually sunsetting, so it is worth considering whether historical accounts of sunset provisions support our skepticism. David A. Fahrenthold shows, with multiple examples, how Congress has passed sunset clauses but then repeatedly ignored them in a process he calls "democracy's snooze button."[109] Antonios Kouroutakis and Sofia Ranchordás echo that same notion in their critique of policies that undermine the effectiveness of democracy, including policies with sunset clauses.[110]

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[107] Id.

[108] See Joseph Segilia & Caroline Lambert, Interstate Cannabis Markets Can Thrive by Using Commerce Clause, Bloomberg L. (Jun. 20, 2023, 4:00 AM), https://news.bloomberglaw.com/us-law-week/interstate-cannabis-markets-can-thrive-by-using-commerce-clause.

[109] David A. Fahrenthold, In Congress, Sunset Clauses are Commonly Passed but Rarely Followed Through, Wash. Post (Dec. 15, 2012), https://www.washingtonpost.com/politics/in-congress-sunset-clauses-are-commonly-passed-but-rarely-followed-through/2012/12/15/9d8e3ee0-43b5-11e2-8e70-e1993528222d_story.html.

[110] Antonios Kouroutakis & Sofia Ranchordás, Snoozing Democracy: Sunset Clauses, De-Juridification, and Emergencies, 25 Minn. J. Int'l Law 29, 34-35 (2016) ("…since sunset clauses are often renewed without being adequately revisited, temporary de-juridification has become 'democracy's snooze button,' and instead of reacting to the obsolescence of legislation, the adoption of sunset clauses simply postpones decisions regarding extraordinary powers. Therefore, sunset clauses might not always be a shield against the normalization of extraordinary emergency provisions.").

What we argue is that, given a transitional gains trap, sunset clauses are going to be of little protection because of the incentives created by the institutional setting.

Franklin De Vrieze similarly worried about COVID-19 policies with sunset clauses:

> Notwithstanding the theoretical merits of sunset clauses, their effect in practice is often determined by the review processes. While they can reinject democratic accountability and evidence-based review, they can also serve merely to rubber stamp existing powers. They can exist on paper but have little impact in practice. They can be renewed on an ongoing basis, often with little or insufficient scrutiny. Thus, adherence to sunset clauses must itself be scrutinized and lessons must be drawn from other contexts to inform the review processes that accompany them.[111]

This is not to say that sunset clauses cannot act as an effective constraint on regulations, but this is far from a given. As Ranchcordás explains, "sunset clauses and experimental legislation are not *an sich* a curse for legal certainty, but they should not be embraced as 'blessings' either."[112] Simply enacting a sunset clause while ignoring the transitional gains trap will likely lead to a perpetuation of protectionist policies.

There is no way around the fact that much remains unclear regarding if, how, and when these unintended consequences and transitional gains trap problems will emerge in cannabis markets if the DCC is suspended. As a result, the evidence to highlight these problems specific to cannabis markets is undoubtedly limited. While Bloomberg and Mikos are right that the cannabis market is different than other markets, it is far from completely unique. Therefore, we can and should draw on historical evidence to inform cannabis policy decisions moving forward.

V. WE HAVE BEEN HERE BEFORE...

In Part V, we illustrate a few parallel markets whose "unique" regulatory treatment at the state or federal level have yielded concerns that mirror the

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[111] Franklin De Vrieze, Can Sunset Clauses Live Up to Their Promise?, Westminster Found. for Democracy (Oct. 27, 2020), https://www.wfd.org/commentary/can-sunset-clauses-live-their-promise.

[112] Sofia Ranchcordás, Sunset Clauses and Experimental Regulations: Blessing or Curse for Legal Certainty?, 36 Statute L. Rev. 28, 45 (2015).

concerns outlined in Part IV for the future of the cannabis industry. The analysis of the alcohol, cigarette, and health insurance markets in this Part is not meant to be exhaustive, and more research is, of course, welcome. In fact, a closer study comparing these markets may shed light on the important issues raised by cannabis legalization.

A. Post-Prohibition Alcohol Hangover Trap

The story of alcohol prohibition and legalization provides the closest parallel to the modern issue of federal cannabis legalization. That is because of the similarities in recreational use between the two substances and the fact that alcohol was once prohibited and became legal again under the leave-it-to-the-states approach typical of cannabis legalization proposals. In 1920, the United States ratified the 18th Amendment to the Constitution which made the transportation, manufacture, and sale of intoxicating beverages illegal.[113] Despite the use of a constitutional amendment, prohibition was over after only thirteen years. This federal legalization, through the 21st Amendment, led to similar regulatory issues in reemerging liquor markets as those that would face cannabis markets if cannabis were legalized federally. While a major difference was that federal prohibition ended before state prohibitions on alcohol, the rest seems extremely similar. Regulation of the various liquor markets was left in the hands of the states.[114] States were left, through Section 2 of the 21st Amendment, with the ability to regulate the production and distribution of alcohol, as "[t]he transportation or importation into any State . . . for delivery or use therein of intoxicating liquors, *in violation of the laws thereof*, is hereby prohibited."[115] The result is that, "[i]n the years that followed passage of the amendment' [sic] in 1934, the fifty states have implemented a menagerie of alcohol regulatory regimes."[116]

In the ninety years since the legalization of alcohol at the federal level, states have continued to regulate alcohol markets in a variety of ways despite being subject to the DCC. In fact, regulations at the state level have often gone in exceedingly protectionist and monopolist routes. This has primarily been achieved through the creation of a three-tier distribution structure.

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[113] U.S. Const. amend. XVIII.
[114] See Douglas Glen Whitman, Strange Brew: Alcohol and Government Monopoly 1 (2003).
[115] U.S. Const. amend. XXI, § 2 (emphasis added).
[116] Whitman, supra note 114.

Whitman explains that

> [f]ollowing the repeal of Prohibition, responsibility for regulating the alcoholic beverage industry fell to the states, which adopted a variety of different approaches to the issue. Whereas the eighteen "control" states chose to monopolize the distribution and (sometimes) the sale of wine and spirits in the hands of the state government, most states—known as "license" states—chose instead to regulate the behavior of private wholesalers and retailers. In all states, the sale of beer was left entirely in the regulated private sector.[117]

This focus on the regulation of wholesalers and retailers has had telling outcomes, primarily in the form of larger profits for wholesalers who are able to effectively rent seek for regulations, such as the three-tier system, that further entrench their profits.[118]

The story of alcohol is indeed troubling, as much of what we are warning could come to pass in the cannabis market has indeed come to pass in the alcohol market, and without suspending the DCC at that. Tommy Tobin and Andrew Kline, in an article on the DCC and federal cannabis legalization, also point out that in *Tennessee Wine & Spirits Retailers Association v. Thomas*, "the Court struck down a state-mandated durational residency requirement to own a retail liquor store, calling the DCC 'the primary safeguard against state protectionism.'"[119] Now, imagine what regulations would emerge if the constraints the DCC imposes on state regulators were removed. If anything, the alcohol parallel shows that more constraints on states' regulatory power should be sought, not fewer.

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[117] Id. at 3.

[118] Id.

> In effect, the regulations passed since the end of Prohibition deliberately impede vertical integration in the alcohol industry. They simultaneously inflate the profits of the wholesaler sector, whose market position depends in large part on state protection. In this environment, the lobbying efforts of wholesalers aim to entrench the three-tier system—and to shield the wholesalers from market competition.

Id. at 4-5.

[119] Tommy Tobin & Andrew Kline, A Sleeping Giant: How the Dormant Commerce Clause Looms Over the Cannabis Marketplace, 1 Yale L. & Pol'y Rev. 1, 3 (2022).

B. Interstate Cigarette Smuggling

Federal legalization of cannabis, whether it comes via a bill resembling the STATES Act 2.0 or an alternative bill, will certainly honor states' autonomy to establish their own policies regarding cannabis. As such, at least minor differences in state taxes and regulations will be observed. Such differences in policy across state lines are likely to be larger should cannabis be exempt from the DCC, as lack of state-to-state competition will limit political pressure to create an efficient institutional environment for cannabis trade relative to neighboring states.

Viewing the cigarette industry as a case study, the state policy differences will result in potentially substantial price differences across state borders, creating an incentive for consumers to engage in avoidant and evasive behavior. The Family Smoking Prevention and Tobacco Control Act of 2009 granted the Food and Drug Administration ("FDA") federal regulatory authority over cigarettes.[120] This is similar to how the STATES Act 2.0 would grant regulatory authority over cannabis to the FDA.

Since 2009, the regulation of cigarettes, under the purview of the FDA, has been standardized across the states—it is the same basic product in Kentucky as it is in New York as it is in Oregon. But states still have the authority to regulate, for example, the legal age to purchase cigarettes, cigarette flavors, and cigarette taxes. Cigarette taxes range from a high of $5.35 in New York (plus another $1.50 in New York City) to a low of $0.17 in Missouri. Additionally, Massachusetts and California have banned menthol flavored cigarettes.[121] These tax differentials create an arbitrage opportunity (tax avoidance) for consumers, particularly those living near a state border. They also create an incentive for those skilled in the underground economy to engage in large scale diversion (tax evasion) as they legally purchase in lower-tax states, illegally transport the product across multiple state lines, and then illegally sell the product in legal outlets, profiting from the tax differentials. While state-to-state diversion and cross-border shopping make up the lion's share of avoidance and evasion, illicit cigarette activity also involves international smuggling, Native American reservations, and military bases. The state menthol flavor bans have exacerbated these incentives.

The scale of tax- and ban-induced cigarette smuggling is astounding, and many researchers have attempted to estimate its scale and responsiveness to

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[120] Family Smoking Prevention and Tobacco Control Act, Pub. L. No. 111-131, 123 Stat. 1776, 1786 (2009).

[121] See Mass. Gen. Laws ch. 133 (2019); Cal. Health & Safety Code § 104559.5 (2023).

policy changes. For instance, Rajeev K. Goel and Michael A. Nelson estimate cross-border tax avoidance. Their results indicate that a ten percent increase in the minimum border state tax roughly leads to a three percent increase in legal sales in the state.[122] Michael F. Lovenheim, using survey data, matches each respondent to the closest lower-taxing state and ultimately finds that between thirteen and twenty-five percent of all U.S. cigarette consumers engage in cross-border cigarette tax avoidance.[123] Jerry G. Thursby and Marie C. Thursby, using the average retail price in contiguous border states and the tax differential with North Carolina as a measure of large-scale diversion, find that commercial diversion accounts for roughly seven percent of total cigarette sales in the United States in 1990.[124]

Since 2008, the Tax Foundation and the Mackinac Center for Public Policy have published annually updated state-level estimates of cigarette policy avoidance and evasion, what they collectively term "smuggling."[125] Their results indicate that as of 2021, the most recent estimates available at the time of this writing, cigarette smuggling accounted for just under fifty-five percent of all consumption of cigarettes in the state of New York.[126] That is, over 250 million packs of cigarettes consumed in the Empire State originated from outside of the state. Had no smuggling taken place, state tax revenues would have been over $1.1 billion greater.[127] Massachusetts, which imposed a per-pack tax of $3.51 and banned menthol cigarettes, is estimated to have observed a smuggling rate of over thirty-seven percent of consumption.[128] The ban on menthol cigarettes accounts for roughly fourteen percentage points of Massachusetts's smuggling rate.[129] Of course some states, especially those with lower taxes neighboring particularly high-tax states, financially benefit from the state-to-state diversion. For every one hundred packs of cigarettes consumed in Virginia, for instance, around thirty-five packs are

[122] Rajeev K. Goel & Michael A. Nelson, Cigarette Demand and Effectiveness of U.S. Smoking Control Policies: State-level Evidence for More than Half a Century, 42 Empirical Econ. 1079, 1092 (2012).

[123] Michael F. Lovenheim, How Far to the Border?: The Extent and Impact of Cross-Border Casual Cigarette Smuggling, 61 Nat'l Tax J. 7, 30 (2008).

[124] Jerry G. Thursby & Marie C. Thursby, Interstate Cigarette Bootlegging: Extent, Revenue Losses, and Effects of Federal Intervention, 53 Nat'l Tax J. 59, 70 (2000).

[125] See Adam Hoffer, Cigarette Taxes & Cigarette Smuggling by State, 2021, Tax Foundation (2023), https://taxfoundation.org/data/all/state/cigarette-taxes-cigarette-smuggling-2023/ (last visited Apr. 23, 2025).

[126] Id.

[127] Id.

[128] Id.

[129] Id.

purchased from inside the state and transported for consumption in a high-tax or flavor banning state.[130]

Cannabis is of similar size and weight as tobacco, which is to say it is conducive to smuggling. As such, it is prudent for cannabis policymakers to take lessons from the experience of taxing and regulating cigarettes. Cannabis taxation, both at the federal and state levels, should be moderate so as to not further encourage the ongoing illicit market for cannabis. Furthermore, federal legalization should avoid creating an institutional environment that protects complex local regulations that lead to substantial discrepancies in the legality and availability of products across state lines. Exempting cannabis from the DCC would create such an environment, and the interstate smuggling of cannabis products only available in some states would become commonplace.

C. Health Insurance

Vice markets are not the only markets in which state-level regulation has been captured by interest groups and contributed to unintended consequences that are costly to consumers. Health insurance market restrictions at the state level provide another example.

American legal scholar Steven G. Calabresi contends that "[t]he McCarran-Ferguson Act [of 1945] is one of the villains behind America's spiraling health care costs," and that "[t]he country desperately needs interstate competition among health insurers."[131] According to Calabresi, the McCarran-Ferguson Act stipulates that "each of the fifty states has the exclusive power to license health insurance within a state's own borders even if, in doing so, a state directly burdens interstate commerce by shutting out-of-state insurers out of the market."[132] Calabresi explains that the reason the Act is not a violation of the DCC stems from the 1869 case *Paul v. Virginia*, where "the Supreme Court held that 'issuing a policy of insurance is not a transaction of commerce.'"[133]

Future Court decisions, including *Allgeyer v. Louisiana* (1897) and *United States v. South-Eastern Underwriters Association* (1944), chipped away at and subsequently reversed the decision in *Paul v. Virginia*, thus

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[130] Id.

[131] Steven G. Calabresi, The Right to Buy Health Insurance Across State Lines: Crony Capitalism and the Supreme Court, 81 U. Cin. L. Rev. 1447, 1449 (2013).

[132] Id. at 1448.

[133] Id. at 1450.

pushing Congress to ultimately pass the McCarran-Ferguson Act to preserve the states' power to license health insurers.[134] Calabresi makes clear that

> [t]he McCarran Ferguson Act did not require that the states regulate insurance, but it did insulate state regulation of insurance from the federal anti-trust laws, from federal regulation generally, and from Dormant Commerce Clause scrutiny. This, in effect, restored the . . . status quo whereby the states could regulate and license insurance companies—an outcome that insurance companies no doubt lobbied for and sought.[135]

Health insurance is a clear example of DCC suspension via congressional legislation directly leading to the concerns that suspension proponents in the national cannabis market aim to avoid. Given that the McCarran-Ferguson Act is the template for the proposal put forward by Bloomberg and Mikos, the implications of its application to the cannabis industry are important.

VI. CONCLUSION

A significant change in the federal landscape of cannabis regulation is fast-approaching. However, the specific manner by which cannabis will be federally legalized is still up in the air because of the transitional gains trap we face. Many parties, including state-legal cannabis firms, state-level regulators, federal-level drug law enforcement, and policymakers at both the state and federal levels, have a vested interest in the shape that federal legalization will take.

Therefore, the dilemma that society faces regarding federal cannabis legalization is twofold. First, we must consider that the aforementioned interest groups will only pursue federal legalization if it benefits them more than the status quo. If it requires these political actors to endure costs and expend real resources to bring about institutional change, then what is on the other side must be of higher value than the current institutional structure. However, this creates significant opportunities for special interest groups to engage in political entrepreneurship by introducing policies that will entrench their vested interests for the long-term as they work toward their new regime vision. And such a regime will prove even costlier to the rest of society.

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[134] Id. at 1450–51.
[135] Id. at 1451.

Second, the concerns we raise here about those engaging in political entrepreneurship establishing a new institutional regime that further entrenches the interests of politically privileged groups have been largely missing from the current federal cannabis legalization conversation.

Any policy proposals about federal cannabis legalization must consider the trade-offs incurred not only by the incumbent interest groups, but also by consumers, future cannabis firms, and society as a whole. Constitutional constraints, like the DCC, are one way to limit the manner by which federal policy changes can favor state governments and their preferred firms at the expense of consumers. Any proposal that seeks to undermine such constitutional constraints for the purported benefit of short-term progress is not only nearsighted, but nescient to the considerable evidence that any welfare gains will be dwarfed in size by the rent-seeking, protectionism, and secondary consequences that will inevitably ensue. We should be extraordinarily clear that our argument is not one against federal legalization of cannabis. In fact, we firmly believe that federal cannabis legalization is well past due. However, it is imperative that the federal cannabis industry not join the long list of industries doomed for even greater cronyism because the "seen" benefits of protectionist policies to incumbent interests were lauded, and the "unseen," dispersed costs to everyone else were unwittingly ignored.