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Not all Crime is Organized – Classifying the Illicit Cannabis Market



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In North America, it is commonly reported that the illicit cannabis market represents nearly seventy percent of all cannabis transactions. Given this substantial market share, it is necessary to recognize that the illicit cannabis market is more common than the licensed cannabis market.

The illicit cannabis market is a common high-risk area affecting commercial cannabis businesses, but differentiating between the illicit market operator type and the organized crime operator type within this high-risk area is critical for commercial cannabis businesses to better manage inversion and diversion to the illicit cannabis market.

Defining the Illicit Cannabis Market

The definition of the illicit cannabis market should be as follows: cannabis cultivators, manufacturers, distributors, or sellers of any cannabis products or services that facilitate the cannabis product supply chain outside of licensed or legally sanctioned channels. The illicit cannabis market may also be self-described as the legacy, traditional, or black market.

On June 3rd, 2018, New Frontier Data reported that "the legal market equated to less than 1/3 the size of the illicit market in 2017."¹ The research firm BDS Analytics is forecasting that the illicit cannabis market will make up 53 percent of all sales in 2024.² These statistics support that the major risk area for inversion and diversion is the illicit cannabis market, but the specific operator type is not classified.

The sheer size of the illicit cannabis market from its sixty years of underground activity translates into a sizeable market today compared to the fledgling licensed cannabis market. Differentiating between organized crime and illicit operators in inversion and diversion cases is important from a reputational risk and action plan perspective. Organized crime operators have a larger, well-funded, and sophisticated process for inversion, diversion, and illicit market production of cannabis products, whereas illicit operators have a trusted network of complicit contacts with less funds and sophistication that normally relies on stronger community interactions. These differences mean that controlling inversion and diversion from both organized crime and illicit operators requires different controls.

A Brief History of the Illicit Cannabis Market

Until recently, cannabis was illegal in many jurisdictions. Nearly all U.S. states classified the growing, possession, or sale of cannabis as a felony and exacted severe penalties for this crime. Nonetheless, cannabis was being grown, possessed, and sold with regularity. Beginning in 1996, governments began allowing for the cultivation, manufacturing, and sale of cannabis, described then as marijuana. California was the first state in the United States to allow marijuana to be traded in a fashion known as collectives. The cannabis industry progressed from this point. This history is essential to understand because the California collective model is the genesis of the permitted cannabis industry, and provided a springboard that allowed the illicit cannabis market to become licensed and government sanctioned. Although cannabis was first permitted in 1996, California did not require licensing until 2018; 22 years later. Given the longstanding characteristics of the illicit cannabis market, using the illicit cannabis market as the high-risk area allows us to better understand inversion and diversion risk.

The Illicit Cannabis Market Risk Area

Using the illicit cannabis market as a high-risk area allows us to encapsulate the types of operators that cause similar risks to the commercial cannabis industry. Thus, I propose the definition of Illicit cannabis market risk area as the exposure to legal penalties, financial forfeiture, adverse actions on a cannabis business license, or other material loss an organization faces if it is determined to be negligent or in conspiracy with illicit market operators.



Supply Chain Characteristics

The illicit cannabis market operates similarly to the licensed cannabis market, where there are operators providing services to sell cannabis products to the end consumer. Although substantial similarities exist between the licensed and illicit sectors, it is worth identifying characteristics of the illicit market for familiarity as follows:

- Individuals who transport cannabis as a broker (middleman) to a buyer in bulk
- Individuals who purchase or are "fronted" cannabis to sell to individuals
- Individuals who buy cannabis from a grower in some quantity and then produce hand-rolled pre-rolls for sale
- Individuals who take cannabis and make somewhat crude edibles
- Individuals who take cannabis and use various extraction methods to produce concentrates such as shatter, budder, dab oil, and waxes
- Money launderers who facilitate the funds transfers



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The risk drivers associated with the current organized crime risk area are business processes; third parties, customers, and employees; and geographic location. These risk drivers still apply to the illicit cannabis market, but allow us to expand the red flags to identify the high-risk activity in at least the first two drivers.



Red Flags for Business Processes

- Crudely packaged flower product with no defining origination markings or production information
- Packaging for any product category that lacks license and testing information for traceability purposes
- A facility address used for any purpose that is not indicated on legitimate licensing
- Any facility that appears to lack necessary worker safety systems
- Any facility or location that appears to have crude, makeshift, or undeveloped business processes in place
- Any amount of inventory shrinkage
- Weak supply chain management controls

- Invoices or purchase receipts from or to an unlicensed or non-existent vendor
- Any amount of inventory "excess" compared to recorded information
- Reported product destruction lacking a convincing paper trail

Red Flags Associated with Third Parties, Customers, and Employees

- Relationships with a vendor wherein the vendor business appears vague or provisional
- After-hours activity involving cannabis product inventory leaving the track and trace system
- Close relationships between employees and the unlicensed sector in a business setting
- Clandestine meetings involving supervisors or managers (those in control)
- Cannabis product introduced to a licensed facility that is not in the track and trace system

Defining the Illicit Cannabis Market Adds Value to Cannabis Risk Management

By broadening the risk area to illicit cannabis market, it allows us to bring the concept of the two main operator types in the illicit cannabis market into the risk assessment. As identified, early cannabis decriminalization brought rise to a group of illicit operators that do not reasonably fit in the definition of organized crime; however, this market is not devoid of organized crime as an operator model. Differentiating between these two operators allows us to further analyze the differences needed in controls to mitigate inversion and diversion based on illicit cannabis market operator type.

Distinct Characteristics of Illicit Cannabis Market Operators

Illicit Operators

The illicit operator is an individual or loosely associated group operating outside of the law, primarily for personal financial gain. There is a simple hierarchical structure, a near absence of force, fear, or other coercion

tactics in terms of the seller-buyer relationship, and a decentralized supply chain inconsistent with organized crime.

Characteristics of illicit operators:

- Can be a single individual or small cooperative group who produces the cannabis product outside the licensed commercial cannabis framework
- There is no hierarchical structure consistent with organized crime
- Buyers and sellers of the cannabis product are not coerced, but willing participants
- At many levels, there is a standing familiarity between parties to lessen risk and avoid detection or exposure
- Individuals reap financial benefits from their activities
- Although persons involved have a typically low profile, they are not as clandestine as organized crime, meaning the illicit cannabis market operates more in the open
- Decentralized processes where business activities are more compartmentalized
- Resources of all types are less
- Timing of payments through the supply chain are unlikely to match where the product was inverted or diverted
- Obfuscation of funds is less sophisticated
- Operations are less sophisticated
- They carry a particular social status and may be seen as a social movement
- More willing to invert and divert lower values or lower volumes of cannabis product

Organized Crime Operators

Organized crime does operate in, and cooperates with, the illicit cannabis market; however, there will be noticeable variations when you encounter the organized crime operator. As defined by organized crime expert Jay Albanese, "organized crimes are distinct from traditional crimes because they involve planning, multiple participants, and require corrupt measures such as threats to maintain and protect their ongoing criminal activities."³

Characteristics of organized crime operators:

- Well-defined hierarchical structure
- Well-financed
- Centralized management structure

- Greater operational sophistication
 - Use of money laundering
 - Complex movement of the illicit cannabis product to obfuscate the origin
 - Greater supply chain consistency and ability to move larger values and volumes of cannabis product
 - Ability to operate in multiple jurisdictions
- Use of coercive tactics in all business processes and with vendors

Conclusion

The cannabis market in totality is made up of both the illicit cannabis market and the licensed cannabis market. With statistics indicating that the illicit cannabis market is larger than the licensed cannabis market, it is essential to understand the differences as they assist you in developing a more appropriate risk assessment and lead to more tailored and appropriate controls. This process in turn leads to a lower risk profile.

The Association of Certified Commercial Cannabis Experts (ACCCE) is dedicated to advancing the professional knowledge and skills of those committed to commercial cannabis risk management.

The views and opinions expressed in this article are those of the author and do not reflect the official policy or position of the author's affiliated institutions.

¹ Song, Bertie. 2018. "U.S. Legal vs. Illicit Cannabis Market Demand." Last modified June 3, 2018. <https://newfrontierdata.com/cannabis-insights/colorado-flower-sales-exceed-1-1-million-pounds-since-markets-launch-2/>

² BDS Analytics. 2019. "New Report: California's Legal Cannabis Market on Track to Reach \$3.1 Billion in 2019 Sales, \$7.2 Billion in 2024." Last modified August 14, 2019. https://bdsa.com/press_releases/new-report-californias-legal-cannabis-market-on-track-to-reach-3-1-billion-in-2019-sales-7-2-billion-in-2024/

³ Albanese, J. 2017. Organized Crime – Criminology – Oxford Bibliographies. Accessed November 13, 2020. <https://www.oxfordbibliographies.com/view/document/obo-9780195396607/obo-9780195396607-0021.xml>