



CANNABIS INSURANCE: THE BLOSSOMING WEED

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Marijuana v. Hemp



CANNABIS v. HEMP v. MARIJUANA

Cannabis

is a plant family that includes many species, including both hemp and marijuana.



Hemp

is a variety of cannabis grown for its tall, sturdy stalks and **low levels of THC**.

Marijuana

is a variety of cannabis grown for its **high levels of THC**.

Polling Question No. 1

As an actuary have you analyzed any cannabis risk?

- A. Yes
- B. No
- C. Not sure
- D. Pass me the Funyuns please

Cannabis Regulations



1970

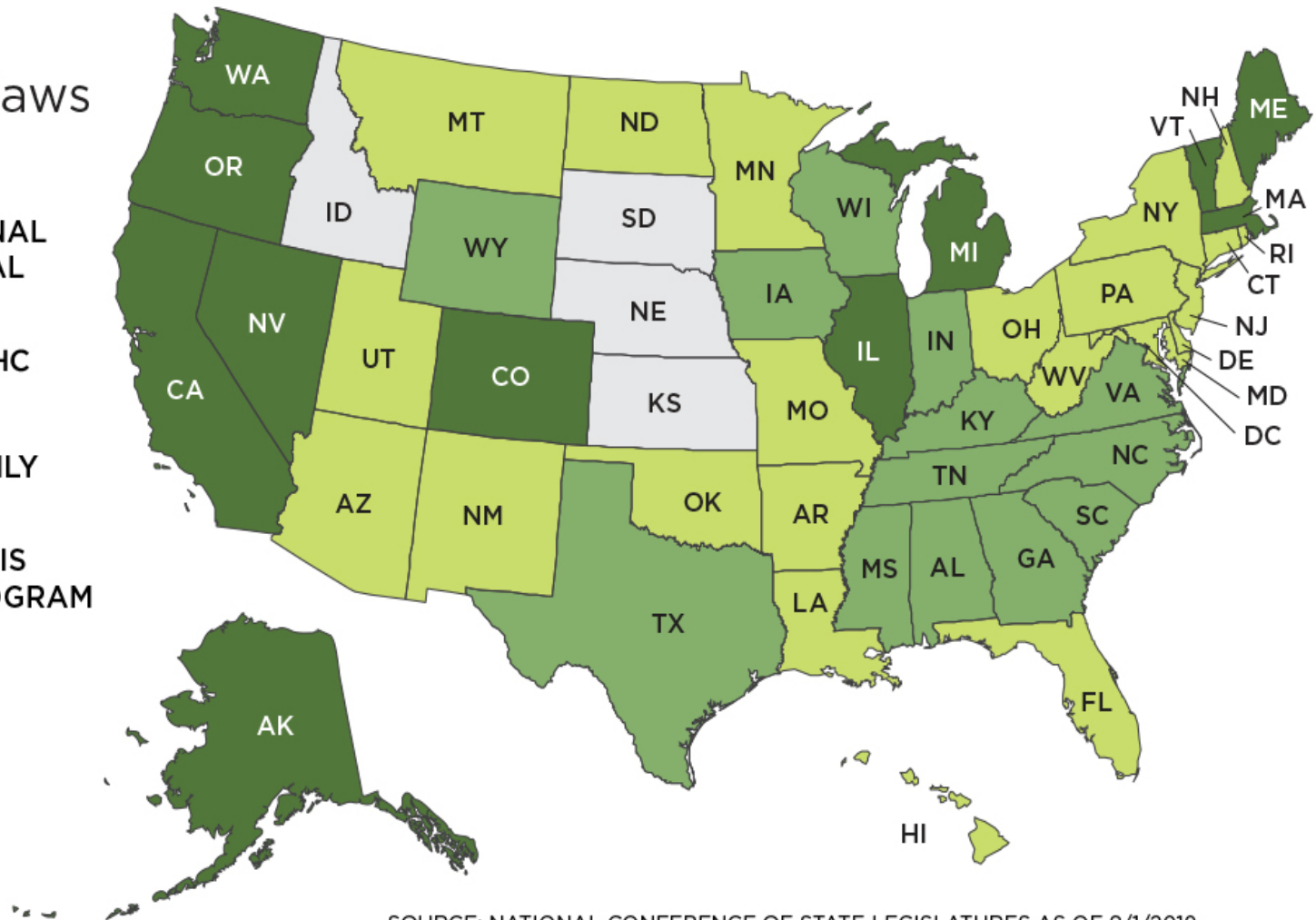
- ▶ **Federal Controlled Substances Act passed.**
 - ▶ Establishes five schedules of “Controlled” substances
- ▶ **Declares marijuana a “Schedule 1” drug:**
 - ▶ Along with heroin, LSD, Ecstasy and Peyote



Recreational (11+DC) Medical (33) CBD States (all but 4 states)

Current
marijuana laws
by state

- RECREATIONAL AND MEDICAL
- CBD/LOW THC
- MEDICAL ONLY
- NO CANNABIS ACCESS PROGRAM



SOURCE: NATIONAL CONFERENCE OF STATE LEGISLATURES AS OF 8/1/2019

Federal Climate

- ▶ *Attorney General William Barr's Position*
 - ▶ Barr stated he did not intend to use federal resources to enforce federal marijuana laws in states that had legalized cannabis products.
- ▶ *President Donald Trump's Position v. Joe Biden*

Polling Question No. 2:

Do you think marijuana will be made legal at the federal level, and if so, when?

- A. Yes, in one year or less
- B. Yes, in two to five years
- C. Yes, in five to ten years
- D. I don't know, pass me the chips please.

Please vote after the producer has launched the polling question.



The Cannabis Insurance Climate

Internal Revenue Code 280E

- ▶ Section 280E of the Internal Revenue Code forbids businesses from deducting otherwise ordinary business expenses from gross income associated with the “trafficking” of Schedule I or II substances, as defined by the Controlled Substances Act.

Banking Regulations

- ▶ Banks are required to file “suspicious activity reports” (SARS) whenever they receive large sums of possibly illegal cash.
- ▶ Banks are federally regulated, and, cannabis is still illegal at the federal level.
 - ▶ Money laundering?
 - ▶ Thus, most banks (especially those federally chartered) will not touch a cannabis business.
- ▶ A significant percentage of the cannabis trade is conducted in cash, making it a target for crime.

Problems for P&C Insurers

- ▶ We know how many people smoke cigarettes and drink alcohol...but....
 - ▶ No way to accurately underwrite marijuana exposure
- ▶ **Property Risks:**
 - ▶ Fire
 - ▶ Theft
 - ▶ Pollution
 - ▶ Potentially high concentrations of value in any one structure.
- ▶ **Potential liability exposure for an insured who makes marijuana available to a third party**
- ▶ **Fear of money laundering allegations**

Polling Question No. 3

Based on current policy wording, do you believe P&C insurers are contractually required to cover cannabis-related claims?

- A. Yes
- B. No
- C. Depends on the situation
- D. Pass me the Fritos please.

Please vote after the producer has launched the polling question.

Valuation of Cannabis: Property

▶ Variables

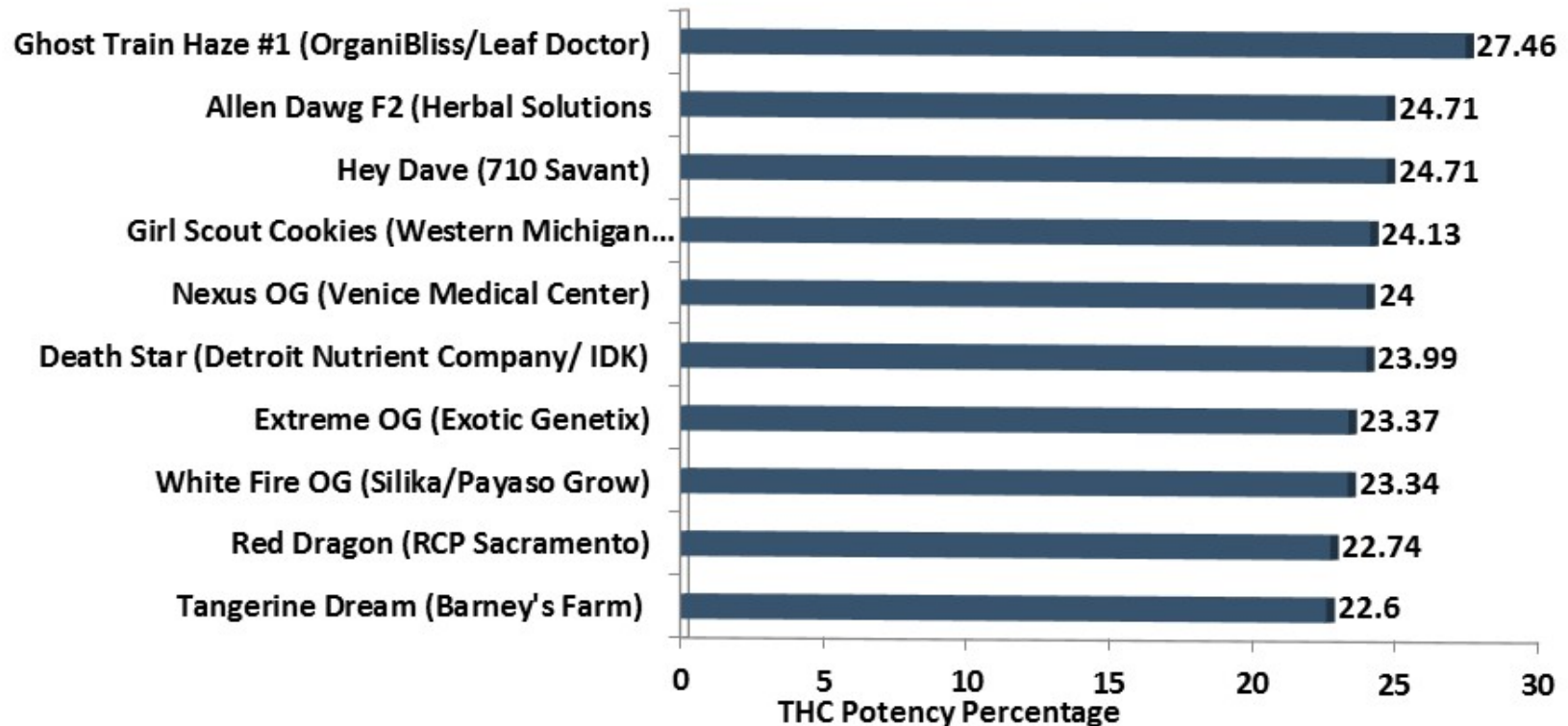
- ▶ Grade/strain of product
- ▶ Organically grown versus non-organically grown
- ▶ Indoor grown versus outdoor grown
- ▶ Point in the growing cycle when it is damaged
 - ▶ Are plants 10 days old or 100 days old?
- ▶ Climate and length of growing season

Polling Question No. 4

Which name is a real strain of marijuana?

- A. Double Dipped Oreos
- B. Boy Scout Popcorn
- C. Girl Scout Cookies
- D. Pass me the Doritos please

Most Potent Strains Submitted to 2014 High Times Cannabis Cups




Of the 10 most potent strains submitted to the five Cannabis Cups held in 2014, potencies ranged from 22%-28%. Nineteen of the 20 strains contained potencies over 20%. Marijuana potency has increased dramatically over the past 40 years. In 1975, the average THC potency was 1% and has increased to 15% by 2013.

For more insights like this and in-depth analysis of the cannabis sector, go to:

Valuation of Cannabis: Income

- ▶ Suppose you have a fire when your crop is 90 days into the grow cycle.
 - ▶ The plants are valuable for the:
 - ▶ Cost to replace the plants (seeds, growing medium)
 - ▶ Lost profit you would have made if you had sold the plants.
 - ▶ You must also continue to pay rent and utilities and salaries while you wait 90 more days to get up to speed.
- ▶ This is called a “business income” or “business interruption loss, and must be considered as part of the valuation of a cannabis crop.



Insurance
Needs:
Is Anyone
Even Buying
Insurance?

Who Needs and Buys the Insurance?

- ▶ Growers & Manufacturers (Processors)
 - ▶ Includes edibles
- ▶ Dispensaries
 - ▶ Medical
 - ▶ Recreational
- ▶ Physicians who prescribe it
- ▶ Ancillary Providers of Services to the Trade
 - ▶ Landlords
 - ▶ Insurance companies and agencies
 - ▶ Packaging providers
 - ▶ Banks

Property Business Insurance Needs

- ▶ Property Coverage (fire, theft, water damage, etc)
 - ▶ Buildings
 - ▶ Contents, including coverage for valuable crops, harvested products, cash)
- ▶ Armored Car Coverage (for transportation of cash)
- ▶ Crop coverage (for indoor crops)
- ▶ Kidnap and Ransom (for employees and executives)
- ▶ Employee Dishonesty Coverage (for theft by employees)

Liability Business Insurance Needs

- ▶ Workers compensation coverage (for employees of the facilities)
- ▶ Auto liability (for employees who deliver marijuana to customers)
- ▶ Professional liability (for doctors that prescribe it)
- ▶ Product liability (for anyone in the chain of distribution)
- ▶ Electronic data (for dispensaries if client database is breached or stolen)

MJ Biz Barriers to Purchasing

- ▶ Belief that coverage is not available
- ▶ Believe that insurance is not worth the cost
- ▶ Fear that information provided to insurer can be accessed by the federal government or others
- ▶ Cost (marijuana businesses have much more costly policies than mainstream businesses do).

Where Do We Begin Underwriting?

- ▶ Dispensaries
 - ▶ Medical → pharmacies
 - ▶ Recreational → liquor stores/vape shops
- ▶ Processors → any other food and drug processor
- ▶ Growers → farmers of other agricultural products
- ▶ Doctors → doctors (?)

Sample Crop Underwriting Factors

- ▶ Third-party inspection results
- ▶ Security systems wired to outside monitoring station
- ▶ Adequate electrical system with proper wattage and circuits
- ▶ Fire suppression systems
- ▶ Type of safe used for storing cash/product (TL-15 or ½ ton minimum)
- ▶ Motion detectors in the room where finished product is stored
- ▶ Membership in state trade associations
- ▶ Education and training of owners/operators
 - ▶ Use of Cannaregs.com

What Do the Courts Say?





COVERAGE

Tracy v. USAA (Hawaii 2012)

Hawaii resident asked her homeowner's carrier to pay over \$45,000 for 12 marijuana plants. USAA offered & Tracy demanded more money + bad faith damages

USAA argued that because the plants were illegal under Federal law, to cover marijuana would be against public policy.

The court agreed with USAA and Tracy's claim was denied entirely.

Green Earth Wellness Center v. Atain Specialty Ins. Co. (Colo. 2016)

Losses to Green Earth in 2012/2013 (wildfire and theft). Atain denied both claims on the grounds that marijuana is illegal at the federal level

Green Earth sued for

- ▶ Breach of contract
- ▶ Bad faith
- ▶ Unreasonable delay in payment

Green Earth Court Ruled:

- ▶ Colorado STATE laws governed the contract, not federal laws
 - ▶ Court did not throw out policy due to federal illegality
- ▶ Atain, having entered into the contract knowing the business involved marijuana, could not invoke federal illegality of marijuana as a reason not to pay

K.V.G. Properties v. Westfield (6th Cir. 2018)

KVG, a commercial landlord, leased properties to tenants and authorized “general office or light industrial business” use.

- ▶ In 2015, the DEA raided the premises and found a MJ grow operation. KVG evicted the tenants and found extensive damage to the property.

KVG filed a claim with Westfield which was denied under the criminal acts exclusion.

KVG v. Westfield 6th Cir. Ruling:

Growing marijuana is protected by Michigan law; *but*, no reasonable jury could find that the tenants complied with Michigan law.

- ▶ KVG's contention that the criminal acts exclusion did not apply because the tenants had not been convicted was rejected.
- ▶ The 6th Circuit indicated that its holding might have been different had the tenants been acting in compliance with state law.

Davis v. Hartford (2020)

- ▶ A Georgia bankruptcy law firm is suing Hartford Casualty Insurance Co., alleging that it wrongfully denied coverage for business income losses resulting from state-mandated shutdowns during the COVID-19 pandemic.



State, County and City Regulations

State, County and City Regulations

- ▶ Wisconsin cannabis testing lab Accelerated Analytics has accused a CBD manufacturer of falsifying its lab reports to conceal illegal concentrations of THC in its products and overstate their cannabinoid content.
- ▶ The Arizona Attorney General's Office has sent a cease-and-desist letter to a cannabis dispensary operator selling a tincture product that claims to aid the prevention or treatment of COVID-19.

Polling Question No. 5

Can you legally say that your CBD product:

- A. Cures Covid?
- B. Cures dementia?
- C. Cures cancer?
- D. None of the above?
- E. Pass me the pretzels please.



Class Action Lawsuits

JustCBD, HempBombs, YiLo and Strength of Hope, & Charlotte's Web (Class Action Lawsuits)

Allegedly overstated the quantity of CBD contained in its products.



What Went Wrong?

- ▶ Mislabeling (intentional or unintentional)
- ▶ Faulty lab testing
- ▶ Fraud (more CBD = higher price point)
- ▶ Batch testing not frequent enough

Pot Pavilion Colorado 2016)



Vaping



Inadequate Labeling/Warnings

- No consistency (states have individual regulations)
- Lack of Warnings: (example low birth weights, developmental delays)
- Lack of testing
- What are the long term effects?
- Pesticides/Heavy Metals

Polling Question No. 6

You get a medical marijuana card for a longstanding medical condition, is this form of treatment covered under the ADA:

- A. Yes
- B. No
- C. Depends on where you live.
- D. Pass me the M&Ms please.



Employment Dismissals & CBD

Zero Tolerance Policies

- What if your CBD product contains THC – .3 is the allowable amount (if from the marijuana plant)?
- What about zero tolerance policies?





Federal Drug Administration (FDA)

Regulates cannabis-derived products and products to which cannabis or its derivatives (e.g., dietary supplements to which cannabidiol (CBD) has been added).

FDA warns and FTC fines.



FDA

2018: Approved Epidiolex, which contains a purified drug substance cannabidiol.

“Can products that contain cannabidiol [CBD] be sold as dietary supplements?...No.”

FDA Examples

“Is it legal, in interstate commerce, to sell a food to which THC or CBD has been added?...No.”

Companies that make hemp-derived edible products are trying to dodge the agency's scrutiny by avoiding labeling their goods as CBD. Instead, they are marketing their oils and edibles as "whole hemp extract" or "full-spectrum hemp."

FDA Examples

- ▶ A former NFL player's CBD company has received a warning letter from the U.S. Food and Drug Administration and the Federal Trade Commission for allegedly claiming the company's products can treat or cure COVID-19.
- ▶ BIOTA Biosciences, a CBD injections manufacturer, issued a recall products after the FDA warned the company against touting its wares as treatments for opioid addiction.

FDA Examples

The FDA has told a U.K.-based CBD company to stop making misleading claims that its products prevent or treat COVID-19, following similar warnings the agency has issued to several other companies in the wake of the coronavirus pandemic.

Federal Trade Commission

FTC has taken enforcement action (monetary fines) against CBD firms making unsubstantiated claims.

- ▶ Cures cancer
- ▶ Cures Alzheimer's
- ▶ Cure pet depression

U.S. Environmental Protection Agency

- ▶ Recent approval (Feb 2020) of certain pesticides for the cultivation of hemp is a first for the federal government.

2018 Farm Bill

The Agriculture Improvement Act of 2018 (the 2018 Farm Bill) amended the CSA to state that the term marijuana does not include any part of the hemp plant.



Blue Sky (Idaho 2019)

- ▶ A truck load of hemp is seized for traveling from Oregon into Idaho.
- ▶ An Idaho state judge has ruled that a massive shipment of hemp seized by authorities last year was not grown in accordance with the federal farm bills that legalized the crop, and therefore will remain forfeited under the Gem State's strict anti-cannabis laws.
- ▶ CBD company must forfeit the 6,701 pounds of hemp (\$1.3M) as “possession of any plants of the genus cannabis is illegal in Idaho.”

U.S. Dept. of Agriculture (USDA)

As of Feb. 27, 2020, the USDA is delaying enforcement of its requirement that all hemp crops be tested by a DEA-registered lab, a proposed hemp regulation that drew significant criticism from the industry.

State and County Regulations

- ▶ Proposition 65, California's chemical disclosure law

Bankruptcy Protection

- ▶ Personal
- ▶ Business

Polling Question No. 7 (Bonus Round)

Who is cooler?

- A. Brenda Wells
- B. Melissa Roeder
- C. You are both equally cool.
- D. Is this over yet, I am hungry.

POTHOLES IN CANNABIS CLAIMS AND UNDERWRITING

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