

Insurance Risks Surrounding Legal Cannabis

Law360, New York (May 26, 2015, 12:19 PM ET) --

As of today, approximately 23 states and the District of Columbia have legalized cannabis for medical use, and four of these states — Alaska, Oregon, Colorado and Washington — and Washington, D.C., have legalized cannabis for recreational use as well.[1] Further efforts to decriminalize cannabis use and deprioritize enforcement are in progress in many cities and states.

This evolving legal framework applicable to cannabis use presents both opportunities and challenges for business owners and their employees, as well as risk managers and the insurance industry. Business owners must take into account the risks inherent in the industry (and in increased use in the wider society) and consider the insurance implications. These implications include what types of insurance may respond to cannabis-related risks, how to address potential gaps in available coverage stemming from the nascent nature of the industry, conflicting state laws and open questions about legalization on a federal level.



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Cannabis Risks for Ordinary Businesses

All sorts of companies are potentially liable for losses and damages stemming from cannabis use, given that their employees could be using marijuana for medical or recreational purposes. Businesses should therefore clearly define their policies in writing with respect to cannabis use in the workplace and potentially after hours, if such use may impact an employee's ability to function. Such workplace policies must be documented and effectively communicated to employees to minimize and avoid potential lawsuits and other liabilities.

These issues will necessarily have to be worked out on a business-by-business and state-by-state policy and regulatory basis. At present, the issues are complicated, not only by the emerging nature of this business, but also by the lack of solid regulation. According to the Insurance Information Institute, no federal revisions to workers' compensation legislation are anticipated. On a state level, however, Michigan has modified workers' compensation regulations to make clear that employers are not required to reimburse for injuries associated directly with medical marijuana treatment.

Companies that rely on federal contracts just to do business face particular uncertainty, given the

conflict between state and federal law. Nonetheless, in the end, cannabis-related risk management is not too dissimilar from business risk management generally. Given the revenue opportunities for businesses and hence, via tax receipts, for state governments, legal cannabis appears here to stay and likely will continue spreading across the nation.

Identifying Potential Business Risks

Any business could face liability associated with the use of cannabis by employees. For those engaged directly in cannabis-related businesses, the starting point in any new industry is identifying the risks and rewards the industry potentially presents. Identifying these risks, particularly in a new and largely uncharted industry, can be difficult, particularly where the laws dramatically vary state-by-state.

Your Employees, Their Use of Cannabis and Your Employee Manual

As mentioned, employee use is one obvious general-business risk associated with cannabis. As a practical matter, cannabis users should not drive, operate heavy equipment or undertake other tasks where safety and sound judgment are paramount. Moreover, it would be prudent for companies doing business in a state in which cannabis use is legal to review employee manuals and determine how (or if) they addresses cannabis use and the workplace. Consider whether and how your business may want expressly to prohibit workplace use of legal cannabis.

Growers, Dispensaries and Doctors

In addition to workplace safety issues, an array of other potential risks may arise from the growth, dispensation and prescription of cannabis. For example, doctors who prescribe or recommend the product, and those dispensaries that provide it, may be exposed to liability for property damage and/or physical injury that result from patients' use of the product. Growers as well should be mindful of the risks associated with crop management. Of course, there also are property risks involving landlords and tenants as well as broader business risks which should be considered.

Employee Theft

The cannabis industry presently is a cash business. There are several reasons for this. First, the black-market nature of cannabis distribution to date has been based on cash. Second, given the existing federal prohibitions, banks with interstate business activities tend to shy away from financing, or accepting deposits from, cannabis operations. Accordingly, the risk of theft by employees and third-party criminals is particularly acute for this emerging industry. This alone renders effective insurance absolutely essential.

Whether, how and to what extent banks and other financial institutions will embrace this emerging business remains to be seen — and the same principles apply when it comes to insurance companies. However, given the scope of the potential funds involved, it is likely only a matter of time before these issues are ironed out effectively.

Is Insurance the Solution?

While insurance may offer protection against the risks identified above, close attention to policy terms and state law is essential.

Employers aiming to implement employee guidelines to restrict cannabis use would be wise to review their employment practices liability insurance policy and work with experienced insurance professionals to understand any limitations that an insurance policy may impose on an employer's ability to restrict the use of a legal substance, as well as on drug-testing protocols and other measures that may be considered to curb the use of cannabis in your business.

An insurance program for a cannabis-related business cannot be designed without close attention to state insurance law. Some states, such as Massachusetts, mandate that companies seeking to conduct cannabis-related business within the state carry insurance. Others may expressly prohibit insurance for cannabis-related risks.

Given the nascent nature of the industry and potentially conflicting federal law and state insurance laws, it is imperative to consult with trusted counsel that can guide your business through the maze of laws and regulations that may impact how (and whether) insurance responds to a loss. Insurance professionals can help you pay close attention to the choice-of-law provision in your insurance policies as well as particular exclusions or endorsements that may relate to the cannabis industry and/or state law. Further, those insurance professionals can guide your business on using custom or manuscript insurance policies, self-insured retentions, captive insurance programs or specialty insurance policies that may address specifically the risks associated with businesses operating in this new industry.

Irrespective of whether your business opts for a conventional insurance policy, manuscript, captive or something different, understanding your insurance program is also critical. For example, employers in cannabis-related businesses concerned with employee theft may assume that their fidelity insurance policies will insure losses associated with employee theft of product or money. However, unless you review that policy language with your insurance broker or trusted insurance professional, you may be surprised to receive a claim denial because of exclusionary language applying to regulated products or that is interpreted in a novel way to bar claims. Even detailed review, however, may not be sufficient as the continuing federal prohibition and other uncertainties could lead to unexpected claim denials, especially where the loss is significant.

Conclusion

As with any business venture, companies should consult with knowledgeable and experienced insurance professionals. Make sure to ask probing questions to understand the scope of insurance coverage that may be available to insure the risks your business faces. Additionally, take care to document and explain fully the nature of your business and the risks that you have already identified to your insurance broker or other insurance professional. In this way, you may be able to avoid a situation in which you inadvertently purchase an insurance policy that does not adequately address or insure the risks to which your business is exposed.

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[1] On Nov. 4, 2015, Initiative 71, was approved by District of Columbia voters. The initiative legalized the limited possession and cultivation of cannabis by adults. Following a 30-day congressional review period, the initiative became law on Feb. 26, 2015. However, the law does not allow the sale of cannabis or include steps toward actually creating a legal, regulated market. Draft legislation — The Marijuana Legalization and Regulation Act of 2015 — was recently introduced. This legislation would allow the city to register and regulate marijuana cultivators, product manufacturers, retail stores and testing labs as well as tax sales. Nonetheless, federal law has not changed and a significant portion of Washington, D.C., is federal land.

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