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High Time to Open a Cannabis Business Legally in New Jersey—and You Can Obtain Insurance

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You don't want to be the people in Los Angeles area who were busted in July 2021 in connection with an illegal marijuana business. According to authorities, officials seized more than 370,000 marijuana plants and harvested product that was found by flight reconnaissance. The street value was estimated at \$1 billion dollars. This is just one example, however, of how big the cannabis business is and that there is money to be made in this industry. Note that cannabis differs from CBD in that cannabis has a THC level of 0.3% or more. On a federal level, hemp and CBD are permitted under the federal 2018 Farm Bill.¹

You and your clients want to do it legally. New Jersey now presents that opportunity. In New Jersey, Governor Phil Murphy signed into law a bill in February 2021 which lays out a path for a legal recreational cannabis market. New Jersey voted to approve legalization of recreational marijuana in late 2020, becoming the 14th state to make cannabis legal. Since New Jersey is not the first, the experiences from other states will not only help regulators but will provide guideposts for potential New Jersey cannabis businesses.

As with any legitimate business, business owners want to protect the business, their interests and the assets from both first-party losses and third-party claims. Protection (via insurance) to cover such losses or claims is also a growing (*pun intended*) business. Despite the recent change to New Jersey law to allow the legitimate sale of recreational marijuana, a number of insurers, along with retail and surplus lines insurance producers, are at the ready to quote and bind first-party and third-party liability coverage for New Jersey businesses.

Insurance Application(s)

The insurance procurement process for a cannabis business, like any other business concern, starts with a policy application. For general liability coverage, typical applications will inquire whether the business is licensed for the marijuana operations in which it is involved. In fact, the insurer will typically require license numbers to be provided along with identification of whether the business is licensed as a:

- Dispensary/Retailer
- Grower/Cultivator
- Manufacturer/ Processor
- Distributor/Wholesaler
- Testing Lab
- Special Event or club
- Home Delivery
- Microbusiness

While many of the above categories are self-explanatory, it is important to examine all definitions in the *New Jersey Cannabis Regulatory, Enforcement Assistance, and Marketplace Modernization Act*² (CREAMMA). By way of illustration, CREAMMA defines “cannabis,” “Cannabis consumption area,” “Cannabis cultivator,” “Cannabis delivery service” and “micro-business” etc. For example, the act provides that a “microbusiness” means a:

Person or entity licensed under P.L. 2021. C. 16 (C24:61-31 et al.) as a cannabis cultivator, cannabis manufacturer, cannabis wholesaler, cannabis distributor, cannabis retailer or cannabis delivery service that may only, with respect to its business operations, and capacity and quantity of product: (1) employ no more than 10 employees; (2) operate a cannabis establishment occupying an area of no more than 2,500 square feet, and in the case of a cannabis cultivator, grow cannabis on an area no more than 2,500 square feet measured on a horizontal plane and grow above that plane not higher than 24 feet; (3) possess no more than 1,000 cannabis plants each month, except that a cannabis distributor’s possession of cannabis plants for transportation shall not be subject to this limit; (4) acquire each month, in the case of a cannabis manufacturer, no more than 1,000 pounds of usable cannabis; (5) acquire for resale each month, in the case of a cannabis wholesale, not more than 1,000 pounds of usable cannabis, or the equivalent amount in any form of manufactured cannabis product or cannabis resin [also a defined term], or any combination thereof; and (6) acquire for retail sale each month, in the case of a cannabis retailer, no more than 1,000 pounds of usable cannabis, or the equivalent amount in any form of manufactured cannabis product or cannabis resin, or any combination thereof.

Adding to the requirements to obtain a license for a microbusiness is that 100% of the ownership interest in the

microbusiness shall be held by current New Jersey residents who have resided in the state for at least the past two consecutive years. Also, the act requires “at least 51 percent of the owners, directors, officers, or employees of the microbusiness shall be residents of the municipality in which the microbusiness is located, or to be located, or a municipality bordering the municipality in which the microbusiness is located, or to be located.” What is obvious from the act is the legislature’s intent to help New Jersey residents open businesses and not have this industry in New Jersey completely *smoked out* by large multi-state businesses.

While there will certainly be “T”s to cross and “I”s to dot for the creation of any New Jersey cannabis business as the Cannabis Regulatory Commission (established by the act) develops, *rolls out* and regulates the industry, it behooves those seeking cannabis licenses or conditional licenses to examine the insurance market and available products.

Available Types of Insurance Coverage and Exposure Considerations

According to Senior Brokerage Specialist Kevin Engelke of licensed New Jersey Surplus Lines Producer JIMCOR Agency, Inc., the evaluation of risk for a cannabis business is essential to obtain insurance. A typical cannabis business will, therefore, likely require first-party property coverage, workers compensation coverage for employees, general liability coverage, products liability coverage and commercial auto coverage. There will be an emphasis on evaluation of the operations exposure. Certainly, security and theft exposures due to the cash nature of the business need to be considered. For example, a grower in New Jersey falls within the definition of CREAMMA as a “cannabis cultivator.” That cannabis cultivator will need crop coverage. Crop coverage is not a new type of coverage but here is being

applied to a new crop. Valuation of the crop plants and the number of plants will impact the premium. A cultivator that grows indoors, which provides more security and control, may be more attractive to an insurer than an outdoor crop.

If your new cannabis business is that of an extractor or “cannabis manufacturer” (another defined term in CREAMMA), that uses a high heat process, the cannabis business should expect higher property rates because of the increased fire risk.

A cannabis distributor (defined in part in New Jersey under CREAMMA as “any licensed person or entity that transports cannabis in bulk intrastate from one licensed cannabis cultivator to another licensed cannabis cultivator...or ...from one class of licensed cannabis establishment to another class...”) may require higher limits because of the value of transport of bulk goods.

On the retail side, there is also professional liability exposure. If your business’s dispensary clerks are providing recommendations or advice about the products, budtenders errors and omissions coverage should be considered.

As the market expands, an insurer will identify its company’s appetite (more than the munchies) as far as cannabis business size, specifications, and controls.

A typical general liability insurance application will likely inquire about the percentage of gross sales by product type, e.g. an edible infused with recreational marijuana, a concentrate or oil, the more commonly known leaf. Due to the value of the product and risk of theft, an insurance application for a cannabis business will inquire about security protocols and whether a third-party security service is used. No different than other businesses, the insurer will inquire about risk transfer and whether there are written contracts, indemnification provisions and additional insured procurement clauses. Obtaining a quote for liability insurance

for a retail cannabis establishment will require providing information about the retail space, whether any drive thru sales occur there and whether there are online sales.

A cannabis business should anticipate that the general liability coverage it obtains may be Claims Made coverage.

Potential Exclusions

As with most general liability policies, the coverage afforded by a standard form is often modified by exclusions. Business and insurance litigators regularly grapple with specific business or product exclusions. That situation will no doubt arise in the cannabis industry as well. By way of illustration, but not limitation, the added exclusions may exclude insurance for bodily injury arising out of the design, manufacture, distribution, sale, serving, furnishing, use or possession of “marijuana” in which “marijuana” is a defined term. The definition may, in turn, exempt “industrial hemp.” On at least one policy form used in the industry, the definition of “industrial hemp” would mean having no more than 0.3% THC. Given that CREAMMA uses the term “cannabis” and a procured insurance policy may use the word “marijuana,” comparing definitions and what coverage is afforded and excluded is *highly* recommended. Other potential exclusions are Health, Nutrition and Lifestyle Exclusions with a schedule that designates certain products, supplements and additives as excluded such that the policy will not apply to bodily injury, property damage or personal and advertising injury arising out of (or described as “caused by,” “connected with,” etc.) the listed products. Security for the product and cash at a cannabis business may include utilization of firearms. Any claims involving the use of firearms may be excluded. A general liability policy or products policy may also exclude products manufactured, distributed or sold in violation of any regulation or law. State

laws are rapidly changing. Federal law may soon change as well. In July 2021, Majority Leader Senator Chuck Schumer proposed legislation to legalize marijuana at the federal level. The major point is that the Cannabis Administration and Opportunity Act would remove marijuana from the Controlled Substances Act and introduce regulations to tax cannabis products. If an exclusion for “violation of any regulation or law” is in the policy, the cannabis business may obtain modification of that language to limit the exclusion to one for violation of state regulation or law.

In August 2021, the New Jersey regulations implementing CREAMMA were adopted. They can be found at N.J.A.C. 17:30-1.1 et seq. They provide direction and guidance. With regulations now in place, cannabis businesses should carefully evaluate them. The regulations do contain some insurance requirements. For example, pursuant to N.J.A.C. 17:30-12.8 (r) provides “a cannabis retailer and cannabis delivery service shall maintain current hired and non-owned automobile liability insurance sufficient to insure each delivery vehicle in the amount of at least \$1,000,000 per occurrence or accident.”

Insurance is risk control. Business operates best when risk is controlled. While the above generally describes the types of questions an insurer will ask in an application, underwriting considerations, types of coverage that may be appropriate for a cannabis business and some limitations to that coverage, the take-away is that insurers and producers in New Jersey are positioned to place coverage for New Jersey cannabis business. ☺

Endnotes

1. Agricultural Improvement Act of 2018, Public Law No. 115-334, 132 Stat 4490.
2. 2020 Bill Text NJ A.B. 21, C24:61-31.