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IN CONVERSATION

Marijuana is becoming increasingly legal under state laws, but is still firmly illegal under federal law. As a result, insurers are faced with many complex issues concerning coverage for marijuana—particularly claims involving individuals and businesses who legally cultivate or possess marijuana under state law. Rolfes Henry's J. Patrick Schomaker recently sat down with his colleague, insurance coverage attorney Matthew F.X. Craven, CPCU, to discuss examples of how marijuana legalization is impacting coverage determinations and resulting litigation.



**J. PATRICK
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Q: Earlier this year, New Jersey legalized the possession of up to six ounces of marijuana by individuals 21 years of age and older. In doing so, it became the latest state to legalize the recreational use of marijuana (New Jersey previously legalized marijuana for medical use in 2010). What general trends are emerging in marijuana legislation being enacted by state legislatures throughout the country?



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A: Under the Controlled Substances Act of 1970, marijuana with over 0.3 percent THC is classified as a Schedule I drug. Schedule I drugs (also including heroin, LSD, ecstasy, and quaaludes) are defined as those with no currently accepted medical use and a high potential for abuse.

Marijuana legalization has been trending throughout the states in the past 25 years—and particularly in the last decade. More states move toward legalization seemingly every election cycle, and, at some point in the not-too-distant future, we may very well reach a tipping point where the federal government removes marijuana from the Schedule I drug list. In 1996, California became the first state to legalize medical marijuana. Most states have ultimately followed suit. Then, in 2012, Washington and Colorado became the first states to legalize marijuana for recreational use. More states are doing the same or, failing that, passing decriminalization legislation. As of today, all but two states—Idaho and Nebraska—have legalized marijuana in at least some form. While most states have legalized marijuana only for medical use, it appears almost inevitable that widespread legalization for recreational use is on the horizon.

SCHOMAKER: Have insurers drafted specific policy provisions or exclusions that address legalized marijuana?

CRAVEN: Historically, the “criminal acts” and related exclusions would apply to preclude coverage for marijuana-related losses or liability, so no marijuana-specific exclusion was necessary. However, with state-level legalization, some courts have found these exclusions inapplicable. Consequently, a year or two ago, ISO published several marijuana-specific policy forms (generally endorsed on business owner policies), which add marijuana to the property and liability coverage exclusions.

SCHOMAKER: Would a typical homeowner's policy provide coverage for the loss of a legally owned marijuana plant resulting from theft or fire?

CRAVEN: Homeowner's policies provide coverage for physical loss of or damage to covered property caused by or resulting from a covered cause of loss, limit coverage for several categories of property, and contain many exclusions and conditions. The unambiguous terms of an insurance policy will generally be enforced as written, but any ambiguity in or contradiction between policy provisions will be interpreted in favor of the insured. In the California state court case, *Mosley v. Pacific Specialty Ins. Co.*, an unambiguous exclusion for the growing of plants or manufacture of plant materials was the basis for the insurer's determination that no coverage was available for a fire loss caused by a tenant's improper re-routing of electric lines to support a marijuana growing operation.

SCHOMAKER: With many states legalizing marijuana to some degree, but it remaining illegal under federal law, how have insurance companies reacted?

CRAVEN: Probably the most significant implication of federal law is that marijuana businesses legalized under state law are generally not able to access federally regulated banks, credit unions, or other financial institutions—and insurance-claims payments are usually transmitted through federally regulated accounts. Because of the conflict between state and federal law, many insurance companies have traditionally avoided offering insurance to marijuana businesses. Consequently, specialty lines and single-state insurers have arisen to fill the void and offer such coverage.

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On a more basic level, any insurance coverage contrary to public policy is unenforceable—and many courts have relied upon this to conclude that no coverage can be available for marijuana claims because state law is superseded by federal law. A good discussion of this issue can be found in the Hawaii federal court case, *Tracy v. USAA Cas. Ins. Co.*, involving an insurer's determination that no coverage was available for the loss of marijuana plants legally possessed under Hawaii state law.

The specific risks underwritten by an insurer may also be at issue. In the Michigan federal court case, *Nationwide Mut. Fire Ins. Co. v. McDermott*, the insured property was destroyed by an accidental fire caused by the manufacture and smoking of marijuana, but the insured homeowner was licensed by the state to grow marijuana plants. The insurer determined no coverage was available for the loss because it was not informed of the marijuana-growing operation by the insured, and such use of the insured property constituted an increase in risk that was not underwritten or included in calculating the premiums.

SCHOMAKER: What are some interesting issues that courts have faced in reviewing marijuana business-insurance claims?

CRAVEN: Obviously, there have been a wide variety of issues addressed throughout the country stemming from insurance claims made by marijuana businesses, so I'll just mention several federal court cases that seem to highlight a trend in navigating the state law versus federal law dichotomy.

A federal court in Colorado addressed several matters in *Green Earth Wellness Ctr. v. Attain Specialty Ins. Co.* This case is especially interesting because it was undisputed that the insurer knew about the nature of the insured's business prior to issuing the policy. The court examined the difference between marijuana plants themselves and the resulting "flowers" or "buds" and determined that, while the plants

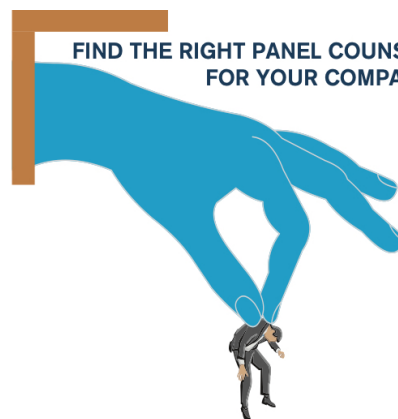
themselves were excluded from coverage under the "growing crops" exclusion, the resulting "flowers" or "buds" were potentially covered as business inventory. Significantly, the court expressly refused to apply the "contraband" exclusion because the insurer knew it was insuring a marijuana business. The court also referenced "an erosion of clear and consistent federal public policy" against marijuana in reaching its decision.

A federal court in Oregon considered a labor and employment dispute involving a marijuana business in *Greenwood v. Green Leaf Lab* when an employee was fired after questioning the employer about its failure to pay minimum wages and overtime pay. The primary question of law involved whether an employee of a marijuana business could avail himself of the protections afforded by the Federal Fair Labor Standards Act (FLSA) given that marijuana is illegal under federal law. Although the court did not determine the legitimacy of the FLSA claim itself, it did rule that the FLSA does not categorically exclude medical marijuana workers from its protections.

I think these cases may need to be taken with a grain or two of salt because the deciding courts are located in Colorado and Oregon—but they are quite notable in that the courts recognized the potential legal rights of marijuana businesses and their employees instead of unilaterally relying on the illegality of marijuana under federal law as being determinative.

The topics discussed here only scratch the surface of some of the many issues facing insurance professionals and attorneys when dealing with marijuana claims, and the developing nature of marijuana law across the country makes such claims incredibly complicated. The bottom line is that we all need to be aware that the law impacting marijuana claims is ever-changing and needs to be continually analyzed to ensure correct coverage decisions are being made.

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