



The Evolving Cannabis Industry: Employment, Regulatory Requirements and Strategic Growth

THURSDAY, SEPTEMBER 9, 2021

Alicia R. Ashcraft
Vance O. Knapp
Eric M. Walter

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The Evolving Cannabis Industry: Survey of State Regulatory Issues

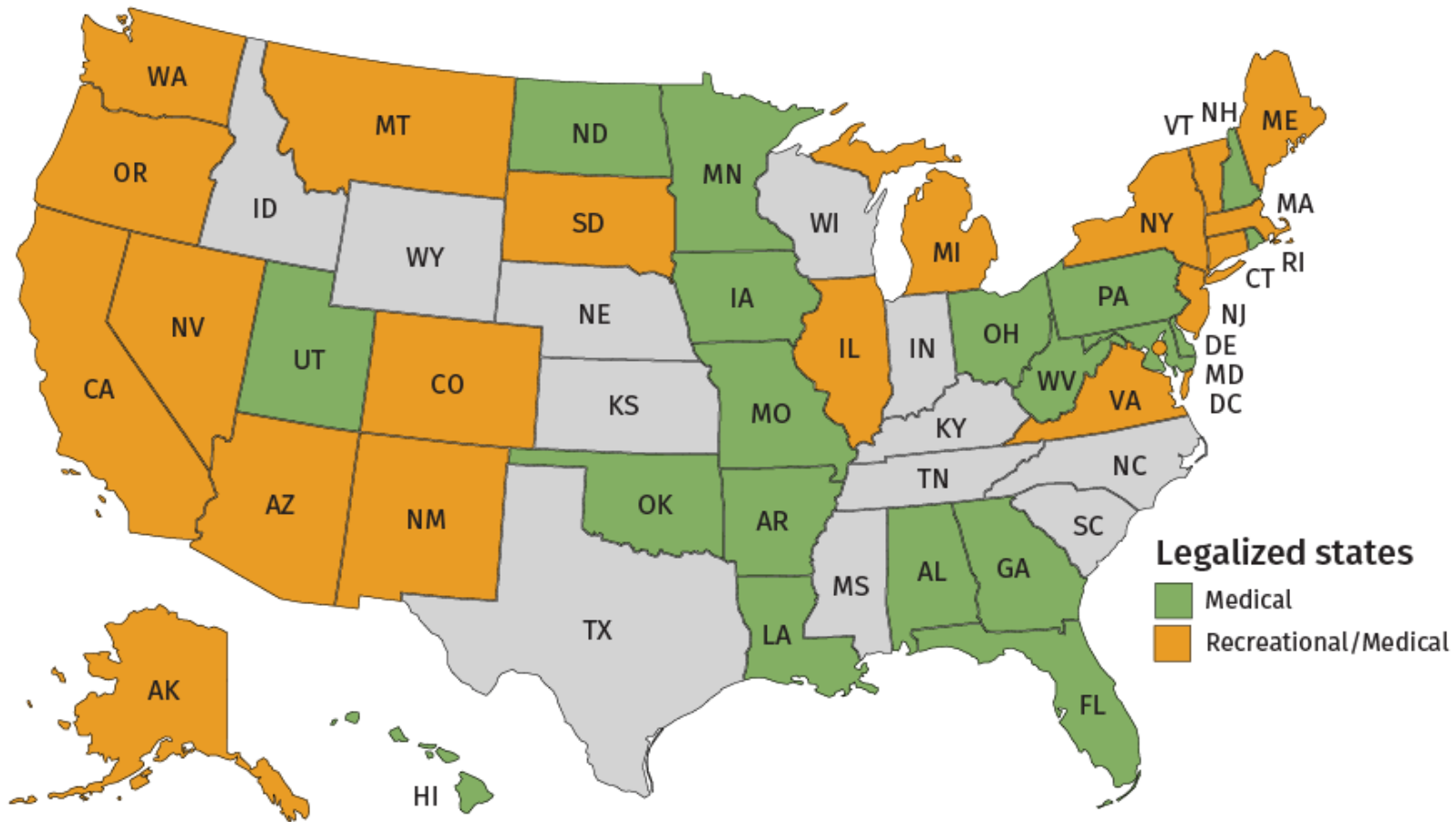
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Eric M. Walter, Partner
Chair, Marijuana and Hemp Law
Practice Area

St. Louis

ewalter@atllp.com 314.342.8061

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Source: MJBizDaily research

Note: Does not include states that have legalized only CBD-based oils.

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<https://mjbizdaily.com/map-of-us-marijuana-legalization-by-state/>

Missouri

- **Regulator: Department of Health and Senior Services, Section for Medical Marijuana Regulation**
- **Five license types: cultivation, manufacturing, dispensary, testing and transportation**
 - Cultivators and manufacturers distribute directly to dispensaries
 - Dispensaries or transporters can handle delivery
 - Vertical ownership permitted (except testing)
- **Allows vertical ownership but limits to 3/3/5**
- **Adult use initiatives for the November 2022 ballot have been filed – signatures due early May 2022**

New Jersey

- **Regulator: Cannabis Regulatory Commission**
- **Eight license types: cultivator, manufacturer, wholesaler, distributor (wholesale transport), retailer, delivery (consumer), testing and microbusiness**
 - Prohibits most vertical ownership until 2023
 - Microbusinesses can be any of the above but limited in size, plus:
 - 100% ownership by NJ residents
 - 51% of owners/employees be residents of microbusiness' municipality
- **Municipalities can opt out but only if they adopt a new ordinance between Feb. 22, 2021, and Aug. 22, 2021**
 - Older ordinances barring cannabis businesses are invalid
 - Absent a new ordinance, the municipality must permit cannabis businesses for at least five years

Illinois

- **Three Regulators:**
 - Dept. of Financial and Professional Regulation (dispensary)
 - Dept. of Agriculture (cultivation/infusion)
 - Dept. of Public Health (patients)
- **Multiple rounds of licensing and more to follow**
 - Statute grants additional application points and other benefits to “social equity applicants”
 - Dispensary licensing has been marred by scoring problems and lawsuits
- **Craft grower license – small cultivation, with ability to also seek licenses to infuse and dispense at the same location**

New York

- **Regulator: Office of Cannabis Management, to be governed by the Cannabis Control Board**
- Rules and applications will be available late 2021 or early 2022
- License types include “nursery” and “on-site consumption”
- Statute generally prohibits ownership of multiple license types to discourage concentration of licenses in vertical conglomerates
- 50% of licenses will go to “social and economic equity applicants,” defined as those:
 - from communities disproportionately impacted by cannabis enforcement; and
 - who qualify as a minority- or women-owned business, distressed farmers, or service-disabled veterans.
- “Social equity licenses” cannot be sold or transferred for three years, unless recipient **meets same qualifications**

California

- **July 2021 – Department of Cannabis Control created to regulate, license, and oversee the state cannabis industry**
- Previously, three different agencies with complex (sometimes conflicting) regulations:
 - Bureau of Cannabis Control (Consumer Affairs)
 - Manufactured Cannabis Safety Branch (Public Health)
 - CalCannabis Cultivation Licensing (Food and Agriculture)
- DCC will combine the regulations in one place and work to improve and streamline them
- This year, California began requiring Prop 65 warnings on smokable cannabis (cancer and developmental toxicity) and certain other products with THC (developmental toxicity)

Delta-8 THC

- Chemically similar to “regular” THC (delta-9) but less potent
- Created from hemp, which the federal government legalized in the 2018 federal Farm Bill
- Numerous states have banned the sale of products containing delta-8, mostly due to lack of regulation and research
- Where not banned, can be produced and sold without regulatory oversight or testing
 - Pulls market share from regulated cannabis businesses
 - Presents public health risks as tests have found heavy metals and other harmful compounds

State Residency Requirements

- Many cannabis laws and ballot initiatives include requirements or preferences favoring residents of that state
- Courts have begun striking down these laws within the industry as violating the U.S. Constitution’s “dormant commerce clause”
 - Prohibits laws that discriminate or unduly burden interstate commerce
 - If a law is found to be discriminatory, it is *per se* invalid unless the state can show that the law “is narrowly tailored to advance a legitimate local purpose”
- States have been unable to carry that burden...
 - August 2020 – city ordinance granting preferential licensing treatment to long-time Maine residents
 - June 2021 – constitutional provision requiring each facility license be majority-owned by Missouri residents
 - June 2021 – city ordinance granting preferential treatment for Detroit residents
 - August 2021 – law requiring dispensary officers and directors to be Maine residents



The Evolving Cannabis Industry: Federal Law Update and Mergers and Acquisitions

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Alicia R. Ashcraft, Partner
Corporate Services Group
Las Vegas

aashcraft@atllp.com 702.473.7079

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What Makes Cannabis Illegal Under Federal Law?

- Marijuana is **ILLEGAL** under the **Controlled Substances Act of 1970 (CSA)**
 - 21 USC Code § 841
 - “Except as authorized by this subchapter, it shall be unlawful for any person knowingly or intentionally to manufacture, distribute, or dispense, or possess with intent to manufacture, distribute, or dispense, a controlled substance.”
 - Cannabis is **(still)** listed on Schedule I of Controlled Substances
 - Schedule I substances have “**no currently accepted medical use** and a **high potential for abuse.**”
 - Examples include: heroin, LSD, ecstasy and peyote.

CSA Violations – Penalties

- Penalties for violating the CSA are severe

- Simple possession of marijuana:

- Misdemeanor, punishable by up to **one year in prison** and a **minimum fine of \$1,000**.

- Manufacture, distribution or possession with intent to distribute marijuana:

- Felony, punishable by up to **five years in prison** and fines up to **\$250,000 for individuals and \$1 million for entities**.

(Repeat offenders face more severe penalties)

- Whoever assists or aids in the commission of a federal offense is **punishable as a principal**

State Legalization Efforts

- **Currently, 19 states, the District of Columbia and Guam have legalized the recreational use of cannabis, and 36 states, the District of Columbia, Puerto Rico and the U.S. Virgin Islands permit some form of medical use.**
 - Despite the federal prohibition, a majority of Americans live in states where some form of legal cannabis use is permitted.
 - Even states that have not yet legalized adult-use, have decriminalized possession of small amounts of cannabis.
- **Fifteen states have either legalized recreational cannabis but have not yet started sales or have legislation that is pending.**

Federal Law – Limited Exemption from Prosecution

▪ United States v. McIntosh Case

- The 9th Circuit Court of Appeals decision explains, in reference to the Rohrabacher spending bill, that even though “the rider is not a model of clarity” it “prohibits DOJ from spending funds from relevant appropriations acts for the prosecution of individuals who engaged in conduct permitted by the **State Medical Marijuana Laws** and who fully complied with such laws.”
- Supreme Court Justice Clarence Thomas recently opined that federal laws against cannabis no longer make sense because of the scattered federal and state statutes: “A prohibition on intrastate use or cultivation of marijuana may no longer be necessary or proper to support the Federal Government’s piecemeal approach.”

Possible Legislative Initiatives Currently in Congress

▪ Incremental Reform

- **SAFE** Banking Act (Secure And Fair Enforcement)
- **CLAIM** Act (Clarifying Law Around Insurance of Marijuana)
- Veterans Access
 - Veterans Cannabis Use for Safe Healing
 - VA Medicinal Cannabis Research Act

▪ Comprehensive Reform

- **MORE** Act (Marijuana Opportunity Reinvestment and Expungement Act) (Waiting for reintroduction)
- Bill led by Schumer/Wyden and Booker (Waiting for introduction)
 - The Cannabis Administration and Opportunity Act

Possible Legislative Initiatives Currently in Congress

▪ Appropriations

- Adult-Use Cannabis Protections
- **SAFE** Banking Appropriations
- Medical Cannabis Protections
- District of Columbia Adult-Use Sales
- Transfer of Funds Provision within Department of Justice Division B, Title II (2020)

Possible Policy Updates from Federal Administrative Agencies

- **Federal Administrative Agency Action**
 - FinCEN Guidance
 - Cole Memo
 - Cole Rescindment
 - Internal Revenue Service

The Cannabis Administration and Opportunity Act

- **Decriminalization; Recognition of State law Controlling Cannabis** – The legislation removes cannabis from the Controlled Substances Act and transfers jurisdiction from the Drug Enforcement Administration to the Food and Drug Administration, the Alcohol and Tobacco Tax and Trade Bureau, and the Bureau of Alcohol, Tobacco, Firearms and Explosives. Additionally, the proposed law recognizes state law controlling cannabis, but retains federal criminal penalties for illegal diversion. Finally, it also authorizes regulations to track cannabis products, and it establishes a minimum purchase age at 21 years old.
- **Research, Training, and Prevention** – The bill directs the Comptroller General to evaluate the societal impact of state legalization; it directs the Department of Health and Human Services to research cannabis's effects on health conditions and directs the Department of Transportation to collect data on cannabis-impaired driving.
- **Availability of Small Business Administration Programs and Loans** – The legislation allows the SBA guarantee loans to eligible small businesses that are cannabis-related businesses.
- **Restorative Justice and Opportunity Programs** – The draft law requires expungement of certain federal cannabis convictions and requires resentencing. It encourages states to follow suit. It bars convictions from adversely affecting immigration and provides three grant programs to address the effects of the War on Drugs.
- **Medical Cannabis Recommendations by the Department of Veteran Affairs** – The proposed bill allows VA-employed physicians to recommend cannabis to their patients.
- **Federal Taxation** – The law imposes an excise tax on cannabis products, like taxes imposed on alcohol and tobacco and requires a federal permit to sell wholesale cannabis products.

Trends for Cannabis Mergers and Acquisitions

- **2017** – Approximately 163 deals accounting for \$1.9 billion
- **2018** – Approximately 324 deals totaling more than \$7 billion
- **2019** – Approximately 249 deals totaling \$5 billion
- **2020** – Approximately 124 deals valued at \$615 million (excluding Aphria and Tilray Inc. - \$4 billion)

- **2019** – More than 92 deals terminated, totaling approximately \$2.2 billion
- **2020** – Approximately 64 canceled deals, valued at \$650 million

Notable Mergers and Acquisitions in 2021

- Cresco Labs (CRLBF), a Chicago-based MSO in nine states, acquired Bluma Wellness for \$213 million
- Verano, a Chicago-based MSO in 12 states, bought Florida-based Alternative Medical Enterprises (AltMed) for an undisclosed amount
- Ayr Strategies (AYRWF), previously based in New York, acquired Florida-based Liberty Health Sciences (LHSIF) for \$290 million, and moved its headquarters to Florida

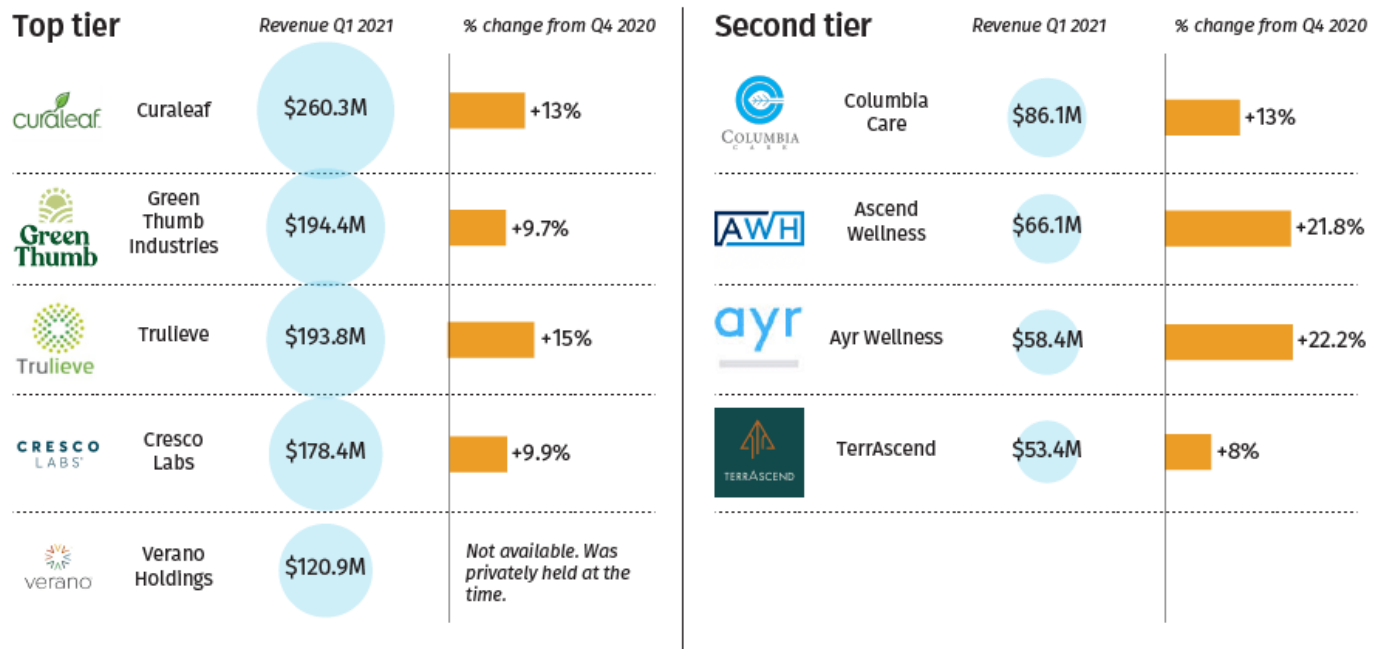
Mergers and Acquisitions Announced in 2021

- Jazz Pharmaceuticals PLC (Nasdaq: JAZZ): \$7.2 billion deal to acquire British pharma company GW Pharmaceuticals PLC
- Hexo Corp. (NYSE: HEXO): \$768 million acquisition of Redecan — a privately owned producer in Canada
- Curaleaf Holdings Inc. (OTC: CURLF): \$67 million to acquire Colorado-based Los Suenos Farms – one of the largest outdoor cultivation facilities in the U.S.
- Trulieve Cannabis Corp. (OTC: TCNNF): announced a \$2.1 billion acquisition of Harvest Health and Recreation, a Florida-based brand

2021 MSO Performance

Marijuana MSOs Report Solid Financials

Most U.S. marijuana multistate operators enjoyed strong revenue growth during the first three months of 2021. A second tier of smaller MSOs, based on revenue, also has emerged.



Source: Company earnings reports

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Projections for the Cannabis Industry

- Over \$50 billion industry, anticipated to triple by the end of the 2029
- Likely not see further PTC significant consolidation for a year or so, until some of the federal law issues are resolved
- Companies have earmarked cash for strategic acquisitions
- Despite strong first quarter results, cannabis stock prices are still experiencing great volatility

Tips for Transactions

- **Company Investigation** – Verify that the target is licensed to operate and at the planned locations. Evaluate the acquiror’s financial health to ensure they can complete the transaction. Each may perform background investigation and company research.
- **Change of Control and Licensing** – Confirm how the transaction may be accomplished. Many state regulators only permit sale of a portion of the ownership interest in the licensed entity, not the license itself. Check requirements for transfer including background investigations and timing – which in some states may take a year or more. Don’t assume that the Seller is knowledgeable of the regulatory requirements of the state.
- **Debt and Liabilities** – Evaluate the company’s financials and contracts – existing performance under both can have a strong impact on the transaction.
- **Purchase Consideration** – As cash is tight across the industry, many buyers are using stock for consideration. Sellers should take care to understand the securities laws and how or when the stock may be sold. Also, the basis and methodology for valuing the stock may be key, especially in consideration of the length of the transaction before closing.



The Evolving Cannabis Industry: Employment Issues

THURSDAY, SEPTEMBER 9, 2021

Vance O. Knapp, Partner
Employment and Labor Practice—
Denver

vknapp@atllp.com 303.575.4004

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Background Concerning Marijuana

- Unlike industrial hemp, marijuana contains appreciable amounts of delta-9-tetrahydrocannabinol (THC), a psychoactive cannabinoid, which is the main ingredient that creates a “high” in users. The plant also contains several other, non-psychoactive cannabinoids such as cannabidiol (CBD).
 - Marijuana is currently a Schedule I drug under the federal Controlled Substances Act, which defines Schedule I drugs as substances that have no currently accepted medical use in the United States, a lack of accepted safety for use under medical supervision, and a high potential for abuse.
- **Bottom line: Cultivation, distribution, possession and use of marijuana are still criminal acts under federal law, and marijuana is in the same category as cocaine, heroin, etc.**

Can you get a Prescription for Medical Marijuana?

- Marijuana is currently a prohibited Schedule I drug under the federal Controlled Substances Act.
- Prescription has legal meaning within context of DEA regulations and state Board of Pharmacy regulations. By its nature, a Schedule I substance cannot be prescribed because it has no currently accepted medical use in the United States.
 - Physicians do not “prescribe” marijuana as they do other medications such as opioids, painkillers and other drugs.
- Under the various state laws, physicians are authorized to do a variety of things such as “certify,” “recommend,” or “authorize” a qualifying patient to use marijuana or cannabis products for medicinal/medical purposes.

Drug Testing considerations – Marijuana

- Cannabinoids are chemicals related to *delta-9-tetrahydrocannabinol* (THC), marijuana's main mind-altering ingredient that makes people "high." The marijuana plant contains more than 60 cannabinoids.
 - Determining level of intoxication for alcohol is relatively straightforward. That is not the case for THC. Given the length of time that THC remains in the body, the THC levels measured in a screen may not be an accurate indication of impairment.
- **Bottom line: At this point, there is no reliable test to indicate level of impairment with respect to marijuana use.**

State Law Protections – Recent Developments

- **Over the past year, multiple states have enacted new laws protecting against discrimination and adverse employment action in connection with the legal use of cannabis, including:**
 - **New York:** Generally speaking, it prohibits employers from discriminating against employees solely based on the legal use of cannabis off-duty and outside the workplace.
 - **New Jersey:** Prohibits adverse employment action based on use or non-use of cannabis items and prohibits employees from being subject to adverse action solely due to presence of cannabinoid metabolites.
 - **Virginia:** Amended its medical cannabis law to prohibit discrimination against lawful users of medical cannabis oil pursuant to a valid written certification issued by a practitioner for the treatment or to eliminate the symptoms of the employee's diagnosed condition or disease pursuant to the state's cannabis oil law. In addition, recreational cannabis law goes into effect in July.

California Law

- **California law allows for medical marijuana and recreational marijuana by way of its Compassionate Use Act and Adult Use of Marijuana Act.**
 - However, an applicant or employee who uses medical marijuana is not protected as a qualified individual under the Fair Employment Housing Act when the employer acts on the basis of such use, and questions about current illegal drug use are not disability-related inquiries.
- **In 2008, in *Ross v. Raging Wire Telecommunications, Inc.*, the California Supreme Court held that California law does not prohibit an employer from refusing to employ, or accommodate, a medical marijuana user, even if the marijuana use is permitted under California law. The Court held that the state's disability discrimination laws do not require employers to accommodate illegal drug use (under federal law), even if prescribed for medical purposes.**
- **Assembly Bill 1256 was introduced in February 2021, which if passed, subject to certain exceptions, would prohibit employers from discriminating in hiring, termination, or any term or condition of employment because a urine drug test revealed the presence of THC.**

Can I Regulate My Employees' Use of Marijuana

- **YES!**
- **At a minimum, employers in all 50 states and the District of Columbia can regulate an employee's use of marijuana by:**
 - prohibiting marijuana possession and use at work; and
 - prohibiting an employee from reporting to work impaired or under the influence of marijuana.
- **As with recreational marijuana, no state that permits medical marijuana requires employers to accommodate on-duty marijuana use, possession, or impairment. States will often explicitly state that medical marijuana laws do not affect an employer's drug-free workplace policy.**

Courts Rulings – Private Cause of Action

- **Several courts in the last few years have concluded that state law creates a private cause of action for medical marijuana users.**
 - May 2017: Rhode Island Superior Court concluded that there is a private right of action for medical marijuana cardholders to pursue damages for discrimination based on their medical marijuana status.
 - July 2017: Massachusetts Supreme Judicial Court declined to recognize a private cause of action under the Massachusetts Medical Marijuana Act but also held medical marijuana users could assert a claim for handicap discrimination under the Massachusetts Fair Employment Practices Act.
 - August 2017: Connecticut District Court concluded that although the state's Palliative Use of Marijuana Act contained no express language providing for private right of action, the Act impliedly provided for individuals to bring claims.

Courts Rulings – Private Cause of Action

- December 2018: Delaware Court concluded that “a private right of action [wa]s the only means of effectuating the statute’s remedial purpose” and that the statute created an implied private right of action.
- February 2019: Arizona District Court holding that the Arizona Medical Marijuana Act creates an implied private cause of action for medical marijuana cardholders against their employer.
- November 2019: Pennsylvania Court held that employees can bring claims under the state’s Medical Marijuana Act determining that although the Act did not explicitly allow employees to file lawsuits, the statute implies a private right of action.

Considerations for Employers

- **As a result of the conflict between federal and state law with regard to the use of marijuana and with an employer's duty to provide accommodations for employees who use medical marijuana, employers should:**
 - Review marijuana laws in each state in which they have employees to evaluate whether there are lawful off-duty use protections, and to determine what, if any, duty the employer has to accommodate medical marijuana users.
 - Ensure that drug-testing and screening practices comply with emerging laws in relevant states and localities.
 - Carefully consider all adverse employment decisions involving marijuana users. In states that cover medical marijuana patients under disability laws, employers should confirm whether positive drug tests are connected to medicinal use before making employment decisions.



Alicia R. Ashcraft

702.473.7079 / aashcraft@atllp.com



Vance O. Knapp

303.575.4004 / vknappp@atllp.com



Eric M. Walter

314.342.8061 / ewalter@atllp.com