

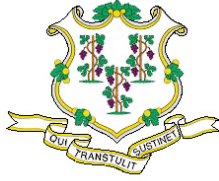


Connecticut Insurance Department

**Report on Access to Insurance by Connecticut
Cannabis Establishments
Pursuant to PA 21-1, JSS, § 64**

**Submitted to The Governor and the Insurance &
Real Estate Committee**

January 1, 2022



STATE OF CONNECTICUT

INSURANCE DEPARTMENT

Pursuant to PA 21-1, JSS, § 64 passed by the legislature in 2021, the Insurance Department is submitting the following report to the Governor and the Insurance & Real Estate Committee regarding access to insurance by Connecticut's cannabis establishments.

Regulators in the Connecticut Insurance Department worked with subject matter experts from National Association of Insurance Commissioners and the insurance industry in preparing this report. The Insurance Department has undertaken a thorough review of potential insurance options for Connecticut's cannabis establishments. The information gathered by the department is consistent with the requirements of PA 21-1, JSS, § 64.

If you have any questions regarding this report, please do not hesitate to contact my office.

Commissioner, Connecticut Insurance Department

Sincerely

A handwritten signature in blue ink, appearing to read "A. Mais", is positioned above a horizontal line.

Andrew N. Mais
Commissioner

I. Executive Summary

Insurance is a necessity for the security and risk balancing for any business. With cannabis industry entrepreneurs, investors, large corporate businesses, new companies going public and executives entering the market, there is a new level of sophistication to the cannabis industry.

As more states legalize either or both medicinal and recreational cannabis use throughout the U.S., legalized cannabis businesses, like any other business, face a variety of risks and require access to insurance to mitigate these risks. It is important to understand the insurance needs of the cannabis industry and to consider appropriate steps to address their insurance needs in the respective state markets.

Several state insurance regulators have taken steps to encourage insurers to provide insurance for state-legalized cannabis businesses. However, major cannabis insurance gaps exist in many states, even in those states that have successfully encouraged the entrance of insurers into the cannabis insurance market. The Connecticut Insurance Department (CID) has been working closely with the National Association of Insurance Commissioners (NAIC) Cannabis Insurance (C) Working Group and the industry to identify insurance issues, gaps and opportunities facing the cannabis industry, and identify the best regulatory practices to address those issues.

One of the most complex issues facing the cannabis industry is the different treatment of cannabis under federal and state law in states that have legalized cannabis. Despite being legal in many states, at the federal level, cannabis is illegal as a schedule I drug. Many financial institutions and insurers are hesitant or unwilling to work with cannabis companies as a result of the federal law. Most banks prohibit cannabis-based businesses from opening accounts, which has led to the cannabis industry being mostly cash-based. This proves problematic as cannabis businesses often find it difficult to engage in standard business practices that other businesses operate by.

Many states that have legalized cannabis, such as California¹ and Massachusetts,² have indicated insurance as a requirement for licensing marijuana businesses. If Connecticut follows that approach, insurance will be required for a cannabis-related business. As the cannabis industry continues to expand in states and U.S. territories, insurance availability lags behind the needs of the cannabis industry. Sectors of the cannabis industry that need to be insured include ancillary cannabis businesses, cannabis-infused product manufacturers, cannabis dispensaries, cannabis events, cannabis growers and harvesters, cannabis landlords, cannabis distributors and transporters, cannabis medical physicians, cannabis waste facilities, cyber liability, and more. Insurance companies have hesitated to enter the admitted market due to little data, as well as the unknown risk factors. There is not only an increased need for insurance by the cannabis industry, but there is also a need for insurance to comply with state licensing requirements.

A significant issue is there are no “admitted” companies writing coverage today. Coverage is only available on the non-admitted market. Surplus lines “admitted” insurers mainly focus on the development of new coverages and the structuring of policies and premiums appropriate for risks. New and innovative insurance products for which there is no loss history are difficult, if not impossible to appropriately price using common actuarial methods. Often, after a new

¹ Cal. Code Regs. Tit 16, § 5008, 5308, 5312, 5709.

² 935 Mass. Code Regs. §§ 500.101(c)(5); (6); § 500.105(10).

coverage has generated sufficient data, the coverage eventually becomes a standard product in the admitted market but that has not yet happened the emerging cannabis market.

Currently, emerging companies in the cannabis industry have limited options in securing appropriate coverage to establish and grow their business. The cannabis sector is still in its infancy and insurers are cautious and event reluctant to enter this new market. Many insurers point to current federal laws as one main reason for not offering coverage.

II. Coverages Cannabis Establishments Need to Operate:

There are important insurance coverages cannabis businesses, and all businesses need in order to operate, and include:

1. Agriculture Insurance

Cannabis cultivation is like most crop harvests because they face similar risks such as weather, theft, and damage. The major difference, however, is that cannabis is illegal on the federal level. Nevertheless, all cultivators rely on insurance to maintain their land and business, and some insurers have covered damages for destroyed cannabis plants.³ On the other hand, some states, like Delaware, have yet to have an insurer cover cannabis crop damage.⁴

2. Liability Insurance

Liability insurance in the cannabis industry includes commercial general liability (CGL), director and officer liability, errors and omissions, general liability, product liability, cyber liability, and premises liability. The NAIC Cannabis Insurance Working Group of the Property and Casualty Insurance Committee (“NAIC Working Group”) issued a regulatory guide for insurers regarding the Cannabis Market, and provided some guidance regarding insuring and rating CGL exposure for cannabis-related businesses.⁵ The recommendation stated, “Within a schedule-rating plan, underwriters may consider such criteria of individual risks as: 1) the experience of the management; 2) internal controls; 3) structural features and condition of the building; 4) compliance with safety protocols; 5) types of equipment; and 6) the selection, training and experience of employees.”⁶ In addition to the CGL policy, the NAIC Working Group suggests additional coverages could be available to the cannabis industry in exchange for additional premiums, including: (1) “Coverage for risks arising from employment of security guards,” (2) “Hired and non-owned automobile coverage,” (3) “Assault and battery coverage,” (4) “Terrorism (federal Terrorism Risk Insurance Act [TRIA] coverage),” (5) “Waiver of subrogation,” (6) “Product withdrawal expense coverage,” and (7) “Special event coverage, which may be considered short-term coverage for which premium is fully earned.”⁷

³ See, e.g., K. Brugger, Cannabis Farmer Gets Over \$1 Million Insurance Payout, SANTA BARBARA INDEP. (2018), www.independent.com/news/2018/mar/19/cannabis-farmer-gets-over-1-million-insurance-payoff/; B. Kennedy, The Cannabist Article: California Cannabis Company Received Historic \$1 Million Insurance Payout Following Fire, CANNABIS INSUR. PROFS. (2018), www.cannabisinsuranceprofessionals.com/news.

⁴ NAIC, Regulatory Guide: Understanding the Market for Cannabis Insurance, 6-7 (July 9, 2019), https://www.naic.org/documents/pending_final_action_cannabis.pdf.

⁵ *Id.* at 35.

⁶ *Id.*

⁷ *Id.* at 36.

In terms of products liability, the NAIC Working Group recommends that rating factors can include: (1) “Compliance with testing protocols,” (2) “Operational maturity of the business,” (3) “Management experience in the industry,” (4) “Presence of a compliance officer,” (5) “Compliance with packaging standards,” (6) “Counterfeit products,” (7) “Cleanliness of water supply,” (8) “Location of suppliers,” (9) “Use of petroleum gases during the extraction process,” (10) Existence of prior product recalls or regulatory infractions,” (11) “Existence and quality of documentation of standard operating protocols,” and (12) “Whether the product needs to be applied topically or is vaporized.”⁸

In enforcing liability policies, courts generally respect the insurance contract as enforceable and not against public policy when insurers have argued that covering an illegal substance is in opposition to the public interest.⁹ Thus, the presence of cannabis does not—despite federal or state law—deny all coverage automatically.¹⁰

3. Property Insurance

Insuring products in a cannabis-related business can include marijuana related products and activities, harvested crops, equipment, and other produced substances. The NAIC Working Group has stated, “[f]or products or completed operations coverage, gross sales are a possible exposure base” and “[r]ates vary by type of operation.”¹¹

For coverage of the harvested crop, “coverage limits may be set up to a fixed dollar amount per unit of weight (e.g., per pound).”¹² Additionally, the working group suggests that other property coverage may be available in exchange for additional premiums for: (1) “money and securities,” (2) “accounts receivable,” (3) “personal effects,” (4) “valuable papers,” (5) “property of others,” (6) “signs,” (7) “tenant glass,” (8) “robbery and safe burglary,” and (9) “loss arising from employee dishonesty.”¹³

Courts have been inconsistent in deciding whether a harvested cannabis product which is legal under state law is considered covered property under an insurance policy.¹⁴ Importantly, the *Green Earth* court noted their disapproval of the *Tracy* decision due to the “continued erosion of any clear and consistent federal policy,” and because the insurer assumed the risk of a cannabis-related business “of its own will, knowingly and intelligently.”¹⁵ Thus, there is a general trend of enforcing insurance contracts despite potential federal illegality.

⁸ *Id.* at 38.

⁹ *Keckler v. Meridian Sec. Ins. Co.*, 967 N.E.2d 18, 28 (Ind. Ct. App. 2012).

¹⁰ *Id.* at 24.

¹¹ NAIC *supra* note 4, at 38.

¹² *Id.* at 39.

¹³ *Id.*

¹⁴ *See, e.g., Tracy v. USAA Cas. Ins. Co.*, No. 11-00487 LEK-KSC, 2012 WL 928186, at *13 (D. Haw. Mar. 16, 2012) (holding that the “Plaintiff’s possession and cultivation of marijuana, even for State-authorized medical use, clearly violates federal law”); *Green Earth Wellness Ctr., LLC v. Attain Specialty Ins. Co.*, 163 F. Supp. 3d 821, 833-34 (D. Colo. 2016) (explicitly disagreeing with *Tracy* and providing coverage despite a “contraband” exclusion).

¹⁵ *Green Earth*, 163 F. Supp. 3d at 835.

4. **Employment-Related Insurance**

Employment-related insurance may be the most important type of insurance for the cannabis business as the industry in America is predicted to employ approximately 292,000 individuals by 2021.¹⁶ Workers' compensation insurance—which provides essential benefits to individuals injured in the course of employment—is an essential part of a cannabis-related business.¹⁷ Currently, workers' compensation may be denied to an injured worker who is found to be under the influence of drugs unless they prove that it did not proximately cause the damage.¹⁸ This issue becomes further complicated with the legalization of recreational cannabis and the ability for individuals to qualify to receive benefits—of which cannabis may be a covered treatment.¹⁹

5. **Other Types of Important Insurance**

Other potentially important areas of insurance within the cannabis market include automobile, including distribution (auto and cargo), excess/umbrella, and surety bonds. Additionally, as the industry grows to include more varieties of products and activities, the coverage needs consequently expand.

III. **Actions at the Federal Level to Address Cannabis Business Issues:**

At the time of this report, there is pending federal legislation seeking to provide safeguards to financial institutions and insurers that provide services to certain cannabis establishments in states that have passed legislation permitting the use of marijuana for medical or recreational purposes or both.

There is federal legislation ([HR 365](#)) to remove marijuana from the list of Schedule I drugs in the federal Controlled Substances Act.

In addition, the House of Representatives recently passed the Secure and Fair Enforcement (SAFE) Banking Act of 2021 ([HR 1996](#)), which provides a safe harbor from penalties for financial institutions that provide services for legitimate cannabis-related businesses. At the time of this report, it is still unclear whether the bill will advance in the Senate.

Also, both the House and the Senate have introduced the Clarifying Law Around Insurance of Marijuana (CLAIM) Act of 2021 ([HR 2068/SB 862](#)), which proposes a safe harbor for insurers engaging in the business of insurance in connection with cannabis-related legitimate businesses in jurisdictions where such activity is legal.

Lastly, there have been indications that under Attorney General Merrick Garland, the Department of Justice may reinstate the Cole Memorandum or a version thereof. The Cole Memorandum was issued in 2013 by Attorney General James M. Cole which advised the Justice Department not to enforce the federal marijuana restrictions in states that had legalized marijuana in some form, except where a lack of federal enforcement would undermine federal priorities. The Cole Memorandum was rescinded in January 2018 by Attorney General Jeff Sessions.

¹⁶ Aaron Smith, The U.S. Legal Marijuana Industry is Booming, CNN (Jan. 31, 2018 4:03 PM), <https://money.cnn.com/2018/01/31/news/marijuana-state-of-the-union/index.html>.

¹⁷ Francis J. Mootz III & Jason Horst, Cannabis and Insurance, 23 Lewis & Clark L. Rev. 893, 908 (2019).

¹⁸ *Kendrix v. Hollingsworth Concrete Prods., Inc.*, 553 S.E.2d 270, 271 (Ga. 2001).

¹⁹ Mootz III & Horst *supra* note 17, at 916.

IV. CID Capabilities & Solutions:

Before cannabis becomes legal at the federal level, insurance availability issues may exist for cannabis establishments. Captive insurance may be a solution. Commercial carriers leave gaps such as exclusions of coverages, different limits, terms and conditions for captives to fill in. The Department may approve, if meeting certain requirements, cannabis captives that ideally would provide the cannabis industry protection as it develops consistent with any new industry laws and regulations. Therefore, the Connecticut Department of Insurance will approve, if meeting certain requirements, cannabis captives that provide this new industry protections from business risks.

The CID has spoken to most of the other states with mature cannabis markets who have indicated that the cannabis industry does have access to the necessary insurance coverage to operate their business. The CID is monitoring the situation closely to ensure the Connecticut cannabis industry has the same insurance options as cannabis businesses have in mature markets.