

Medical Cannabis Landowner Considerations

With the increase in state-by-state cannabis legalization in the U.S., cannabis growing, processing and dispensing facilities are on the rise. Due to the fact that cannabis is still illegal on a federal level, landowners must take into account special practical and operational considerations when contemplating whether to lease to a cannabis tenant.

In Brief

Currently, 29 states have legalized cannabis in the U.S. (19 medical uses only; 10 medical and recreational uses permitted. **See attached map.**)

With space requirements for growing and processing facilities ranging from 20,000-100,000 sq. ft. (the average cannabis facility is generally in the 40,000-50,000 sq. ft range), and retail dispensaries ranging from 2,000-3,000 sq. ft., cannabis businesses can be an attractive tenant for landowners. Due to a range of legal issues and practical considerations, landowners can generally charge from 10% to 35% above market rental rates.

Types of Cannabis Growing and Processing Facilities

Cannabis growing and processing facilities generally fall into two types of facilities.

» Indoor grow facilities

- Existing facility conversions that are utilized for speed-to-market and security considerations
- Utilize a significant amount of electricity/water
- Require ability to control temperatures and humidity
- Landowners should focus on utility capacity (all expenses paid by tenant- including improvements to infrastructure) and facility environment (mold potential)

» Greenhouse facilities

- Generally build-to-suit facilities built specifically for cannabis cultivation and processing
- Facilities reduce energy costs and improve environmental controls (temperature and humidity) to enhance production and strain development

- Facilities may be required to utilize solid/secure sidewalls to comply with state regulations for security

Legal Considerations

Cannabis is still considered a Level 1 Narcotic under federal law. The Department of Justice made the decision in 2013 to not enforce federal law in states that have legalized cannabis (it is important to note that this position may change, as the Trump administration has made several anti-cannabis statements). Congress has also included a provision in recent budgets that no funds may be used to prosecute cannabis charges in states that have legalized cannabis.

Practical Considerations

As cannabis is still illegal on the federal level, there are several practical implications

» Opportunities for multiple facilities in each state

- Cannabis products must be grown and processed in the state where they will be sold legally. Products may not be transported across state lines, as this would be considered interstate commerce and drug trafficking under federal law.
- The practical impact is that each state generally has multiple growing and processing facilities, which provides opportunities for landowners to lease property to more cannabis growing & processing facilities.

» Banking issues

- Most banks will not do business with cannabis companies and will not accept funds or payments from these companies. Some small banks and credit unions will take cannabis-related deposits.
- The practical impact is that the cannabis industry is primarily a cash business. This may pose challenges for landowners in receiving rental payments, where checks may be rejected by the landlord's bank and/or the tenant may pay rent in cash.
- This issue is also important if the landowner has financing on the real estate leasing to a cannabis tenant would violate the covenants in the loan agreement (not to permit any violations of law) and could cause a default in the landowner's financing.

» **Insurance considerations**

- Many insurance companies will not insure cannabis businesses and will also consider having a cannabis business at a property to violate/void existing insurance coverage.
- Before leasing to a cannabis tenant, landowners and tenants must ensure insurance coverage.
- Major title companies will not take cannabis-related funds or provide title on sales to cannabis companies.

» **State licensing**

- Many cannabis tenants will need to obtain a license from the state. The licensing process may require the tenant to seek a lengthy option to lease the property prior to entering into the lease to account for the license application period.
- Many of the states limit the length of the license to one or at most several years, thus the tenant may want to negotiate for termination rights.

» **Zoning and land use approvals**

- For states that are new to the cannabis industry, zoning and land use approvals can be complicated. Local governments tend to be slow to adapt in providing zones and regulations for new “use” in their community.
- Recent experiences have been positive; some communities are embracing the cannabis industry and removing regulatory hurdles.

» **Security concerns**

- A cannabis tenant will require significant security for its growing and processing facility. This will commonly include installation of a large safe for products and cash.
- The facility will require significant security to secure the plants.
- The exterior of the facility will generally also require a high level of security to protect the transport process and employees.
- Landowners should focus on the tenant’s obligations to remove improvements at the expiration of the term.

» **Financial backing**

- As with many tenants, the cannabis tenant will most likely be a special purpose entity with little or no financial background or assets at the beginning of a lease. Landlords should attempt to obtain guarantees from the holding company (if one exists) or the primary financial backers.