

## The Business of Marijuana: How Will It Affect The Real Estate Sector?

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Marijuana use for medicinal purposes can be traced to 2737 BC China where it reportedly was used to treat multiple ailments. Its use as a recommended treatment for certain conditions can be found in U.S. medical journals by the late 1700s. The landscape changed, however, and marijuana ultimately became, and remains, a Schedule I drug under the federal Controlled Substances Act. Nevertheless, as of this writing, 29 states have legalized marijuana for medicinal purposes and 9 states and the District of Columbia have legalized marijuana for recreational use. It is predicted that the field will grow to a \$50 billion industry by 2026.

The impact of the cannabis industry on real estate markets with legalized recreational use has been extraordinary. Industrial rents are reported to have risen 33% from the first quarter 2014 through May 2017 in Denver, and 27% in Seattle and Portland, compared with a 19% increase in 54 of the other largest U.S. markets. Sales price premiums are reported between 20% - 40%.

Although New Jersey legalized medical marijuana in 2010, only 6 facilities have been licensed to date. Governor Murphy is clear on his intention to legalize recreational marijuana, and the expectation is that New Jersey will rapidly become one of the major cannabis markets in the country.

Legalization will present a number of issues impacting the use, growing, selling and dispensing of marijuana. As marijuana remains illegal under federal law, landlords and tenants will have to properly address lease provisions that are otherwise "boilerplate," including compliance with laws, permitted use, maintenance, common area responsibility, default, termination, abandonment and indemnity. Property managers need to consider a host of issues, including, as an example, tenants' rights to reasonable accommodations, the right to grow and smoke marijuana, and security concerns. Marijuana operations also pose unique insurance

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issues that stem from the high usage of water, the highly flammable nature of certain processing techniques, and the increased need for security. There also are title insurance issues, as title insurers have indicated they will not close or insure a transaction involving land associated with the marijuana industry.

Tax and other economic issues must also be addressed. Section 280E of the I.R.C. disallows deductions for expenses incurred in the business of producing or selling marijuana. There were a series of Justice Department guidance documents that enabled the industry to exist. On January 4, 2018, however, Attorney General Sessions rescinded these guidance documents but left actual prosecution to individual federal prosecutors' determination, consistent with chapter 9-27.000 of the U.S. Attorneys' Manual. The manual requires federal prosecutors to examine a number of factors in determining whether to bring a prosecution, including federal law enforcement priorities, the seriousness of a crime, the impact of a crime on the community and the deterrent effect of prosecution. The Financial Crimes Enforcement Network (FinCEN) has issued guidance for banks to provide services to the marijuana industry while abiding their obligations under the Bank Secrecy Act. Although tied to the rescinded Justice Department guidance documents, the FinCEN guidance has not been rescinded by the Department of the Treasury - perhaps not unmindful of the tremendous taxes generated at the federal level by the marijuana industry. And recent federal appropriations bills (set to expire at midnight on March 23) have barred the Department of Justice from utilizing appropriated funds to interfere with states implementing their own medical marijuana laws. It will be important to keep abreast of any change in federal prosecutions, whether the Department of the Treasury amends or rescinds its guidance and Congressional appropriations.

A comprehensive bill presently is pending (S830 - Scutari) to legalize recreational marijuana in New Jersey. State Assemblyman Reed Gusciora also introduced a bill (A1348). Although a host of issues will require resolution before final legislation is enacted and regulations promulgated, there are preparatory measures that should be examined now by those contemplating entry into the field.