2022 Cannabis insurance market update

By Steve Hallo
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The maturing legal cannabis industry's demand for professional and specialty lines insurance is growing alongside the push for legal clarity.

"A lot of clients tell me that adding D&O to their portfolio allowed them to attract board member X or investor Y," says Charles Pyfrom, CMO of CannGen Insurance Services, LLC. "Absent that coverage, they couldn't have accessed that growth." (Image: NU Property & Casualty, March 2022/Adobe Stock)

With a record $21 billion in sales during 2021 and annual sales projections of $70 billion by 2028, **the U.S. cannabis market** continues to show explosive year-over-year growth. The industry's insurance needs, however, have begun to outstrip coverage availability.

In addition to the myriad of challenges now facing any enterprise — including labor shortages, severe weather and mounting cyber perils — **the cannabis industry** also contends with a patchwork of state regulations as federal legalization continues to be the proverbial can that's constantly kicked down the road.

"The short end of it is policies for the cannabis industry have always been priced very high," says Jay Virdi, chief sales officer for **Hub International's cannabis specialty practice** in the U.S. and Canada. Larger operations have some price relief due to competition, he adds. But for mom and pop shops? "The rates are pretty level and not going down," Virdi says.

Jonathan Isaacson, co-chair of **the cannabis law practice group at Kaufman Dolowich Voluck (KDV)**, notes demand for coverages of all types in the cannabis market. "The industry probably needs insurance coverages in every way possible, with developed markets expanding and new markets coming online," Isaacson says. "There is constant pressure" for an array of coverages.

He adds that as more programs go live and more markets open, particularly in larger states such as New York, capacity is certain to tighten.

'Checking boxes'

For new operations, insurance purchases are mainly driven by price as these businesses are just trying to check a box, Virdi says. "That is usually a minimum mandatory requirement to get the license, get the keys from the landlord and maintain compliance."

Stephanie Bozzuto, co-founder & president of marketing at **Cannabis Connect Insurance Services**, notes there are a host of steps to opening a cannabis operation. "I've had clients with big general liability policies with me that just sat there while they were wrapping up the licensing and all the processing at state and local levels," Bozzuto notes.

Although new cannabis operations tend to focus on the coverages required by law, Bozzuto says by year two or three, many have the capital to start thinking more robustly about their insurance demands.

Professional lines policies are among the most pressing needs for established cannabis businesses, according to Isaacson. He adds that KDV has defended a number of professional line cases for attorneys and accountants who service the cannabis industry.

These types of concerns are leading companies to explore other coverages such as directors & officers (D&O) and employment practice liability insurance (EPLI). For 2022, D&O rates for cannabis operations are anticipated to increase 10%-20%, according to Hub International. EPLI rates are expected to see similar growth.

However, Bozzuto anticipates rates for professional lines to come down 5% to 10% from current levels in the coming years, “depending on claims and what is happening in the market.”

The allure of D&O

“The first few years for a business are about getting the licenses and securing funding. Once the business matures, clients realize that risk management and loss control are imperative,” Bozzuto says, adding that now many cannabis businesses voluntarily seek out D&O coverages.

In addition to protecting current executives and board members, D&O is becoming vital for securing top talent as well as attracting new investors, says Charles Pyfrom, CMO of **CannGen Insurance Services, LLC**.

“A lot of clients tell me that adding D&O to their portfolio allowed them to attract board member X or investor Y,” Pyfrom says. “Absent that coverage, they couldn’t have accessed that growth.”

Claims by investors of mismanagement of funds or taking actions that are not in the best interest of shareholders are the most common types of lawsuits these operators face, he says. D&O coverage can help with such issues.

Currently, only a handful of carriers will write D&O policies for the cannabis space. However, many insurance industry watchers predict other major insurance players will be rolling out programs in this market soon. This is anticipated to drive more competition in the sector, resulting in more policy forms and better retentions.

The market now is fairly segmented with high-end policies available from carriers that “are certainly getting their pound of flesh in pricing and retention limits,” Pyfrom says.

Cyber demands

As with every industry, the need for cyber insurance is growing for the cannabis sector, says one thought-leaders who spoke during a recent **Farella Braun + Martel LLP** webinar on the topic.

There’s an inaccurate perception that cannabis businesses are low-value targets for hackers.

“The reality is, we are starting to see more cyber incidents in the cannabis industry as a whole,” says Michael Peters, product leader and professional liability broker for the **cannabis division at PL Risk Advisors**. Even more worrisome, he adds, is the range of sectors covered by cannabis, spanning cultivation to retail, in addition to having a medical standpoint.

“You have to keep in mind that cannabis itself can find a home in a lot of industry types,” Peters reiterated. “There are a lot of moving pieces in the cannabis continuum that can drive claim frequency and severity.”

For example, if a cultivator is using a computer to monitor or regulate a watering system and a cyber event shuts down those systems, the product could be damaged and coverage in a cyber policy would typically not apply.

“In that case, the grower would have to look at their crop coverage, which, if they have it, typically includes a cyber exclusion,” Gerking says.

However, if a cannabis company is monitoring crops using a third-party system, and that vendor is breached rendering the business damaged or inoperable, there are certain elements of coverage that could be applied such as business interruption insurance.

Further, cannabis businesses may face cyber insurance limits due to the sensitive nature of the information they collect, according to Gerking.

“We saw it in the Ashley Madison breach four or five years ago,” he says. “Just the fact that someone’s name was associated with a company caused lawsuits and liability exposure to skyrocket… Limits get eaten up quickly by defense costs. Basically, you can spend all your limits defending a case and have nothing left for settlement or judgment at the end.”

As a result of such scenarios, cyber insurance rates for cannabis operations are anticipated to grow 30% or more during the coming year, according to Hub International.

Product liability fears

Among the biggest issues during the early years of cannabis-business insurance was the concern for product liability. However, sources agree that a wave of product liability claims has yet to materialize.

“Everyone was doom and gloom about product liability,” Virdi recalls. He notes that claims are more typically seen around property lines and coverages such as D&O. “That is where the claims are bulked. It is really on the property side and not the liability side, as we see it right now.”

Noting these fears were amplified as some states moved from medical-only to recreational use, Buzzuto says product liability coverage for the cannabis industry is a “broken system.”

“Product liability should eventually be rolled into general liability like for most industries,” she says. “That’s a problem on its own, because it gives the client an option to have it or not. What frustrates me with product liability is, because it is carved out as a monoline policy, every year there is a retroactive date and the client has to keep paying more and more to keep that date.”