

YEOMAN
TIMBER

TERRACLES

LANDLORDS & MEDICAL MARIJUANA BUSINESSES

By

Mike Widener

**Yeoman Timber, LLC
Phoenix, Arizona**

Copyright 2012© Yeoman Timber, LLC and Mike Widener

Dedicated to my Gardenia ladies – daily “natural highs.”

Publisher’s Cataloging – in – Publication data

Widener, Michael N., 1950-

Joint Tenancies: Landlords and Medical Marijuana Businesses/Mike Widener
1st ed. c. 2012

v., 95p. cm.

Includes bibliographic references and index

ISBN- 978-0-675-61783-1

1. Commercial leases--United States 2. Building leases--Government policy
3. Marijuana industry 4. Cannabis--Law and legislation 5. Marijuana--Law and legislation--
United States I. Widener, Michael N., 1950- II. Title

KF 593.C6.W5 2012

346.7304'3462 W5 2012

Yeoman Timber, LLC
512 West Gardenia Drive
Phoenix, Arizona 85021

Cover Photo Credit: Burnzwell Medical Marijuana Center, Denver, Colorado. Attribution:
O'Dea at WikiCommons, licensed under the Creative Commons Attribution-Share Alike 3.0
Unported License, 2011.

CONTENTS

Prefacev

1. A Budding Tenant Niche? - Overview1

2. Spaced Out – Government Control of Authorized Marijuana Operations3

3. Straight Dope on Private Land Use Covenants 6

4. Grass is Greener, or Maybe Not - Premises Environmental Hazards10

5. Ganja See The Warning Signs? - Landlords’ Economic Risks12

6. Bogarting a Landlord’s Joint – Forfeiture Statutes15

7. Buzz Kill – Lender Angst with MME Leases19

8. Hashing Out Major Lease Terms22

9. MME Sticky Issues – Additional Lease Clauses27

10. Bhang for the Buck – Is MME Leasing Viable?30

Endnotes33

Appendix One (Form of Letter of Intent)51

Appendix Two (Form of MME Tenant Lease)54

About the Author94

Acknowledgements94

Index95



PREFACE

Joint Tenancies is the only American book that invites careful thinking about the commercial landlord's risk and reward scenarios in leasing to medical marijuana businesses. This book is not written to be a page-turner or to offer readers entertainment. I make no apologies for that. Possession, transportation and sale of *Cannabis* are federal crimes today under the Controlled Substances Act of 1970 - a law of the United States. Until *Cannabis* is rescheduled under that Act, the operation of a medical marijuana dispensary or grow site is a federal crime punishable under the federal courts' sentencing guidelines, which impose fines and jail time. As I explain in the main text, leasing to a medical marijuana business very possibly exposes a landlord to civil and criminal penalties. Among the penalties available is forfeiture of a landlord's property. Forfeiture means the government takes away your real estate and doesn't give it back, and doesn't give you money or other consideration for the forfeiture. Nothing light – hearted or entertaining there, correct?

Leasing to a medical marijuana business is a serious undertaking. While such a lease may have significant potential financial upside while the federal government chooses not to enforce current federal laws, the government is not obligated to adhere to any policy statement or position paper issued by the White House or the Department of Justice. Policy statements and position papers don't have the force of law. If the government decides later to enforce to the letter the Controlled Substances Act or other federal laws applying to medical marijuana operations, a landlord of that type business could be ruined, financially and socially, as I describe below. The decision to lease to a medical marijuana facility operator is not for risk-adverse landlords.

Toward the end of *Joint Tenancies*, I've attached some forms, offering ideas for how a landlord might treat this type of transaction. I promise you that using these forms, or anything like them, *won't* guaranty that a landlord will be rescued from the loss of its property by forfeiture or from personal criminal prosecution. So, a potential commercial landlord has to proceed with extreme caution. Part of that process is to obtain competent legal advice from an experienced attorney in your local community. Listen carefully to this advice – don't be seduced by potential rent rewards and simply ignore a variety of risk factors. Warning signals to landlords may come from the office of your state's United States Attorney's or the United States Marshals

Service's Offices, or from the federal Drug Enforcement Agency regional office closest to the subject property. Read the signals: Landlords must be sure they make informed decisions to lease to medical marijuana business *before* signing anything committing them to lease.

This book is not legal advice delivered or offered to anyone. I cannot represent medical marijuana businesses and keep my law practice license. My oath of office as an Arizona attorney requires me to support the laws and the Constitution of the United States. Possession, transportation and sale of *Cannabis* are federal crimes under the Controlled Substances Act of 1970. I don't pick which federal laws I wish to support. So, if you're a medical marijuana business owner, from my perspective, you're entirely on your own, no matter what you've gained by reading this book. I don't represent any commercial landlords among you readers, either – not unless we've signed a representation letter on the letterhead of my law firm. I'm not brazen enough to think I know the law sufficiently in any of the 16 American states that have adopted medical marijuana use statutes except Arizona, where I live. I can't – and I don't – give you even basic advice in this book about leasing to a medical marijuana business, even within the Grand Canyon State. Purchasers and readers should take my statements in this book any way they want, except as legal advice, which no statement in this book represents. This book seeks to educate you, and I hope it succeeds in that mission.

On that note, notice that on the first page of this Preface and each chapter through Chapter Seven, you'll find a Quick Response Code. When you've downloaded the correct scanner application to your tablet computer or smart phone, you can point the camera feature on your device to the Code and be led by the app to a Webpage with a core document helping you grasp why federal government agencies are equally involved in your leasing decisions as are your state government, your local government, the neighboring property owners and the board of your commerce or industrial park.



Chapter One: A Budding Tenant Niche?

Overview

Sixteen states and the District of Columbia have approved the sale to licensed patients of ingestible versions of the genus *Cannabis*.¹ Another eighteen states' legislatures have members proposing legislation permitting medicinal *Cannabis* use as of March 8, 2012.² It seems that if the federal law enforcement community maintains its present "threats without action" posture, retailing to prescription holders will continue. Today, the federal posture on enforcement is in flux notwithstanding the Controlled Substances Act of 1970.³ That Act schedules *Cannabis* as a drug that cannot be sold, transported or possessed for sale without felony liability for the actor. In October of 2009, the Justice Department issued a letter⁴ stating the Obama Administration's preference that U.S. District Attorneys not prosecute purveyors and users of *Cannabis* acting in clear compliance with the requirements of state law. In February, 2011, however, the U.S. District Attorney for the District of Northern California advised the Oakland City Attorney and the California Attorney General that it would not stand idle while the city licensed commercial scale (unattached to a dispensary operation, and growing in bulk) *Cannabis* cultivators.⁵ (No doubt Oakland was peeved by this response, since the licensing fees (including application fee) for the six growers Oakland hoped to license would have raised more than One Million Dollars in fees for the city.⁶) U.S. Attorney Melinda Haag's warning to Oakland and the Attorney General triggered a wave of aggressive federal prosecution threats, including claims against owners for the forfeiture of real property; and these threats are continuing through the date of this book's publication.⁷ This spate of warning shots from federal prosecutors has created an environment of confusion and resentment among medical marijuana entrepreneurs.

Despite ambiguity about federal government enforcement policy of anti-drug laws,⁸ in difficult economic conditions, state governments will continue to seek new sources for sales tax revenues.⁹ At one time, some federal authorities perceived that temporary non-prosecution of licensed medical marijuana enterprises might reduce the incentive to export American firearms to Mexican drug cartels.¹⁰ Recent federal prosecutor saber-rattling seems to indicate that belief has eroded. But criminal enforcement of drug laws by federal law enforcement is not the only weapon against medical marijuana entrepreneurs. An IRS campaign of aggressive audits of medical marijuana retailers was launched in 2010. The Service uses Section 280E of the Internal Revenue Code to deny marijuana dispensaries deductions for legitimate business expenses such

as rent, payroll, and all other necessary business expenses. These denials result in astronomical “back tax” bills for the affected dispensaries. If legislation is not implemented to allow these businesses to deduct legitimate business expenses, these unpaid taxes, with interest and penalties, threaten to destroy the financial viability of every medical cannabis dispensary in the United States. For instance, in October, 2011, the IRS billed Oakland’s Harborside Health Center \$2.5 Million in back taxes for calendar years 2007 and 2008, based on a federal law prohibiting marijuana dispensaries - unlike other businesses - from deducting payroll, insurance, rent, workers' compensation and other operating costs from its revenues.¹¹

Whatever the federal motivations may be today,¹² medical marijuana prescribing appears trending toward acceptance in a solid minority of American states by this decade’s end. This trend presents both opportunities and risks for commercial landlords in communities adopting ordinances governing growing and dispensing activities in states where medical marijuana laws apply. No readable book comprehensively can analyze each state (and applicable local) government’s rules for establishing and monitoring businesses I call “medical marijuana enterprises” -- initialized here as “MMEs.” Numerous thorny real property issues face landlords deciding whether – and how – to rent space in their buildings to MMEs. In the following chapters, I outline these issues in some detail and suggest ways to cope with the difficult choices confronting the landlord in allowing a medical marijuana tenancy. In Chapter Two, the reader will be introduced to the regulatory framework that governs medical marijuana businesses. In Chapter Three, the reader learns about private mandates that at times dictate if a medical marijuana business is permitted on certain tracts of land. In Chapter Four, the biological impacts of cultivated marijuana on indoor environments are outlined, along with their impact on multi-tenant buildings. In Chapters Five and Six, the economic risks of these types of tenancies are summarized, and in Chapter Seven, third party issues troubling a landlord’s lender are described. These plentiful risk factors introduce Chapters Eight and Nine, in which the reader discovers suggestions on how landlords should approach documenting a medical marijuana lease to minimize their risks.

In any state where medical marijuana cultivation and dispensing are permitted by its legislature, the landlord’s initial step is to become familiar with the state statutes and accompanying administrative regulations affecting real estate matters. Essentially, these consist of physical occupancy requirements for growers and retailers. Arizona, among the most recent adopters of medical marijuana enterprise statutes and regulations, illustrates a typical pattern of governance in terms of the legislative and local administrative regulatory coverage. The landlord’s second step is to acquaint itself with the zoning ordinance in the city, town, or county where its property is located. The zoning ordinance will advise the landlord whether the zoning class for its land allows MME operation as well as what other zoning adjustment is required.

CHAPTER ONE

¹Readers can find a scorecard at

<http://medicalmarijuana.procon.org/view.resource.php?resourceID=000881> that comprehensively charts the 16 states' and the District of Columbia's medical marijuana laws, including the years and methods of adoption of the legislation.

² See <http://medicalmarijuana.procon.org/view.resource.php?resourceID=002481> for a comprehensive chart mapping pending legislation in the 18 states during their 2012 legislative sessions.

³The Controlled Substances Act appears in 21 U.S.C. § 801 *et seq.* The reader can search the United States Code online at <http://uscode.house.gov/search/criteria.shtml>. *Cannabis* is a “Schedule I” substance, a category reserved for the supposedly most dangerous and addictive substances that possess no medicinal value. Marijuana specifically is excluded from the Food, Drug and Cosmetic Act by 21 U.S.C. § 321(v) (3). On April 20, 2006, the FDA declared that “no sound scientific studies” supported the medicinal use of smoked marijuana. See the FDA News Release of April 20, 2006 at

<http://medicalmarijuana.procon.org/sourcefiles/FDA2006Statement.pdf>, and Gardiner Harris, *FDA Dismisses Medical Benefit from Marijuana*, NEW YORK TIMES, April 21, 2006, available at <http://www.nytimes.com/2006/04/21/health/21marijuana.html>. After a period of non-engagement while states (other than California, which was ahead of its time) passed medical marijuana statutes and the public voted in its use by referendum in others, the Ogden Memorandum gave medical marijuana proponents a false sense of momentum. U.S. Deputy Attorney General David Ogden in an October 19, 2009, letter to federal prosecutors (“Ogden Memorandum”) questioned the use of limited federal resources in prosecuting individuals complying with state medical marijuana laws, see United States Department of Justice: Memorandum for Selected United States Attorneys, October 19, 2009; but the memorandum does not ban all such prosecutions, see <http://blogs.usdoj.gov/blog/archives/192>. Instead, it served as a “guide to the exercise of investigative and prosecutorial discretion.” *Id.* The printed text of the letter is available in Robert A. Mikos, *A Critical Appraisal of the Department of Justice's New Approach to Medical Marijuana*, 22 STAN. L. & POL'Y. REV. 633, Appendix (2011). The Ogden Memorandum notes that prosecution of “commercial enterprises that unlawfully market and sell marijuana for profit” continues to be an enforcement priority. *Id.* The Department warned that “claims of compliance with state or local law may mask operations inconsistent with the terms, conditions, or purposes of those laws.” *Id.* Furthermore, the Ogden Memorandum reminds its readers that compliance with state law does not create a legal defense to a violation of the Controlled Substances Act.

Rescheduling *Cannabis* was revisited by the FDA in the summer of 2011; but that agency ruled that marijuana has “no accepted medical use” and should therefore remain illegal under federal law — regardless of conflicting state legislation allowing medical marijuana and despite dozens of modern studies and centuries of medical practice attesting to the drug's benefits. See Basis for

the Recommendation for Maintaining Marijuana in Schedule I of the Controlled Substances Act, available at <http://medicalmarijuana.procon.org/sourcefiles/DEA-denial-of-petition-2011.pdf>. Next, the Justice Department in June, 2011 issued a memorandum suggesting that tough prosecution of the Controlled Substances Act was forthcoming, see note 8 below. According to a San Francisco Chronicle story by Dan Freedman on February 24, 2012, Justice Department officials have always insisted enforcement of federal drug law policy did not change, pointing to language in the 2009 Ogden Memorandum stating that "commercial enterprises that unlawfully continue to market and sell marijuana for profit" remain a federal law enforcement priority. Still, advocates and drug-policy experts continue to insist the Justice Department did an about-face from the Ogden Memorandum position. Marijuana "users and operators went forward in good faith and felt burned" by the U.S. Attorneys in California who announced a wave of tough enforcement actions on Oct. 7, 2011, said Craig Reinerman, a sociologist at UC Santa Cruz. "People are confused and bewildered." See Dan Freeman, *Justice Dept.: 'No regrets' on medical pot stance*, February 24, 2012, available at <http://www.sfgate.com/cgi-bin/article.cgi?f=/c/a/2012/02/24/MNL51NB4K6.DTL>

⁴ The printed text of the Ogden Memorandum is available in Robert A. Mikos' article in note 3 above. Prof. Mikos' papers, several of which deal with drug law and the U.S. Constitution, are available online at the Social Sciences Research Network Website, http://papers.ssrn.com/sol3/cf_dev/AbsByAuth.cfm?per_id=272612.

⁵ See February 1, 2011, letter from Melinda Haag, United States Attorney for the Northern District of California, to John Russo, the City of Oakland's City Attorney, available at <http://www.cannabistherapyinstitute.com/legal/feds/doj.haag.memo.pdf> (herein, the "Haag Letter"). In the Haag Letter, she announced her office's intention to enforce the Controlled Substances Act's prohibitions against "manufacturing and distribution activity involving marijuana, even if such activities are permitted under state law." See *id.*

⁶ See Mallia Wollan, *Oakland's Plan to Cash in on Marijuana Farms Hits Federal Roadblock*, NEW YORK TIMES March 3, 2011, at A16; available at http://www.nytimes.com/2011/03/03/us/03oakland.html?_r=1&src=twrhp; see generally CITY OF OAKLAND, CALIFORNIA, ORDINANCE No. 13033, available at <http://clerkwebsvr1.oaklandnet.com/attachments/25723.pdf>.

⁷ See Meghan Hall, *Buzz Kill: Federal Warnings Hit Medical Pot Boom*, May 28, 2011 available at <http://www.npr.org/2011/05/28/136726993/buzz-kill-federal-warnings-hit-medical-pot-boom>, where Hall's story is available in a Weekend Edition audio version and in print. U.S. Attorney Melinda Haag in San Francisco continues to pursue dispensaries located within her jurisdiction, as noted in Chapter 6 of the text. The collected letters threatening federal prosecutions, beginning with Haag's, are found at the Website <http://medicalmarijuana.procon.org/sourcefiles/DOJ-Threat-Letters.pdf>.

⁸ See Mikos, note 3 above; an apparent advocate for the "legalization" of marijuana for all purposes, Mikos predicted that the Department of Justice would have difficulty ensuring local

federal prosecutors comply with the “hold your fire” guideline contained in the Ogden Memorandum. Mikos’ view has been confirmed by a letter of June 29, 2011 to United States Attorneys from James M. Cole, Deputy Attorney General (“Cole Memorandum”). The Cole Memorandum stated that prosecution of significant traffickers of illegal drugs – including marijuana – remains a core priority of the Justice Department, and that the increase in “commercial cultivation, sale, distribution and use of marijuana for purported medical purposes” was not shielded from federal enforcement action and prosecution by the Ogden Memorandum, as such activities violate the Controlled Substances Act. Since that date, Melinda Haag, U.S. Attorney for the Northern District of California, warned five dispensaries that the real property would be forfeited unless the dispensaries shut down. All five dispensaries closed, although two became delivery only services. See Chris Roberts, *DEA Digging into San Francisco’s Medical Marijuana Dispensaries*, sfexaminer.com post of February 2, 2012, available at http://www.sfexaminer.com/local/2012/02/dea-digging-san-franciscos-medical-marijuana-dispensaries#disqus_thread. On October 7, 2011, the four United States Attorneys for California announced a coordinated federal crack-down on medical marijuana retailers. The result is that dozens of medical marijuana dispensaries have closed, primarily in Sacramento and San Diego counties and in San Francisco. *Id.*

⁹ See, e.g., Proposition M (“Taxation of Medical Marijuana Collectives”) which, on March 8, 2011, was approved by a vote of 59.3% to 40.7%, available at <http://cityclerk.lacity.org/election/Results.htm>. The ordinance will impose a tax of five percent on all “gross reimbursements” Los Angeles-based dispensaries receive from their patients. This tax could generate, according to city sources, as much as \$10 million annually. In 2010, Colorado and the City of Denver each collected \$2.2 Million in dispensary sales taxes through November, see Libby S. Kaiser, *Cannabusiness Comes to Town*, PLANNING, March, 2011, at 13. Vallejo, California, has a 10% tax on medical marijuana sales. To read about revenue generation in other cities and states, see Michael Cooper, *Struggling Cities Turn to a Crop for Cash*, THE NEW YORK TIMES February 11, 2012, at A22, available at <http://www.nytimes.com/2012/02/12/us/cities-turn-to-a-crop-for-cash-medical-marijuana.html>

¹⁰ Compare Steve Fainaru and William Booth, *Cartels Face an Economic Battle*, WASHINGTON POST, October 7, 2009 (market forces as much as law enforcement can damage criminal organizations), available at <http://www.washingtonpost.com/wp-dyn/content/article/2009/10/06/AR2009100603847.html>, with Legalizing Marijuana in California Will Not Dramatically Reduce Mexican Drug Trafficking Revenues, Press Release of October 12, 2010, by RAND Drug Policy Research Center, available at <http://www.rand.org/news/press/2010/10/12.html> (RAND study entitled “Reducing Drug Trafficking Revenues and Violence in Mexico: Would Legalizing Marijuana in California Help?” concludes that Mexican cartels’ loss of California marijuana market would only reduce by three percent these cartels’ total revenues from drug exports to the United States.)

¹¹In 2011, Congressman Pete Stark (D-CA) introduced the Small Business Tax Equity Act (H.R. 1985), which would create an exception to I.R.C. 280E for legal medical marijuana businesses, allowing them to take the full range of business expense deductions on their federal tax returns. Read more at <http://www.seattlepi.com/business/press-releases/article/IRS-Threatens-to-Shut-Down-Medical-Cannabis-3355413.php#ixzz1nKOTRszK>. The Harborside Health Center's \$2.4 Million plus levy is reported in a story by Lisa Leff in the Huff Post San Francisco October 2, 2011 edition, available online at http://www.huffingtonpost.com/2011/10/04/harborside-health-center-tax-bill_n_995139.html.

¹ “Federal motivations” are complicated by the apparent intention of individual United States Attorney’s Offices to provide separate statements of policy as to enforcement of federal law in their respective jurisdictions. *See, e.g.*, note 5 above. On May 2, 2011, United States Attorney Dennis K. Burke announced that the District of Arizona will carefully watch the implementation of Arizona’s Medical Marijuana Act for evidence that cultivation of modest amounts for dispensary use does not turn into to “large marijuana production facilities” operations. Burke clarified that even landlords will be prosecuted for knowingly facilitating “the actions of traffickers,” which one infers means facilitating growing large quantities of *Cannabis* in the chain of distribution to licensed users purchasing through dispensaries. *See* May 2, 2011, letter from Dennis K. Burke, United States Attorney for the District of Arizona, to Will Humble, Director of the Arizona Department of Health Services (herein, the “Burke Letter”), *available at* http://www.justice.gov/usao/az/reports/USAO_Medical_Marijuana_May_2011_Letter.pdf. *About February 16*, 2012, Burke’s successor, Ann Birmingham Scheel, wrote to Governor Brewer of Arizona, asserting that state employees might not be immune from prosecution; but the letter added little else to the Burke Letter in terms of federal prosecutorial policy in the state. In the Eastern and Western Districts of Washington, the United States Attorneys notified the Governor of Washington that they intended to enforce the Controlled Substances Act if that state diverted from the non-profit course it had set in 1998 in favor of a regime of for-profit dispensaries. Perhaps responding to the substance of the two Washington U.S. Attorneys’ letter to her of April 14, 2011, on April 29, 2011, Governor Chris Gregoire partially vetoed SB 5073, her veto effectively rendering illegal all dispensaries in Washington that theretofore had operated in metro Seattle, Tacoma and Spokane as for-profit enterprises run like retail stores. Prior municipal tolerance had been predicated upon the state’s statutory description of the patient-provider relationship that incorporated certain vague definitions. *See* Jonathan Martin, *Medical-pot dispensaries fear raids*, SEATTLE TIMES, May 3, 2011, *available at* http://seattletimes.nwsourc.com/html/localnews/2014951007_potpreneuers04m.html, and letter to Christine Gregoire from Jenny A. Durkan and Michael C. Ormsby, Unites States Attorneys for the Western District and Eastern Districts of Washington, *available at* <http://seattletimes.nwsourc.com/ABPub/2011/04/14/2014778917.pdf>. Contemporaneously with the controversy that erupted in Washington State, U.S. Attorneys in the Districts of Colorado, Montana, Rhode Island, Vermont Hawaii, New Hampshire and Maine sent letters threatening to

prosecute persons implementing state cultivation and/or distribution programs. These letters have been collected at this URL: <http://medicalmarijuana.procon.org/sourcefiles/DOJ-Threat-Letters.pdf>. These letters indicate that the U.S. Attorneys across the country are free to pursue their own courses of action while acting within the Controlled Substances Act and federal forfeiture statutes parameters.