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Thornton



Tenner

Legalized Marijuana and Insurance Law

By Timothy M. Thornton, Jr. and Erin K. Tenner, *Gray•Duffy, LLP*

Background

In 1996 California voters approved Proposition 215, legalizing use of marijuana for medical purposes. Many states followed that lead. Yet, federal criminal law continued to classify marijuana as a Class 1 controlled substance. Under the Federal Controlled Substances Act, [21 U.S.C. section 841](#), it is illegal to manufacture, distribute or dispense marijuana. A Class 1 substance is defined as one having no medical value and posing a high risk of abuse. [21 U.S.C. section 812](#).

The US Supreme Court held in 2005 that federal agencies could continue under federal law to prosecute individuals who possess or use marijuana for medical purposes, even if legal under a state law. In 2012 Colorado and Washington became the first states to vote to legalize marijuana for recreational purposes. Six more states have legalized recreational use of marijuana. Washington, D.C. voted to allow possession, growing, and gifting; but sales for recreational use are not allowed.

In 2013 the U.S. Department of Justice ("USDOJ") issued a memorandum stating its general policy not to interfere with the medical use of marijuana pursuant to state laws, provided the state tightly regulates and controls the medical marijuana market. *See Memorandum from James M. Cole, Deputy Attorney General, to All United States Attorneys, Guidance Regarding Marijuana Enforcement* (August 29, 2013) ("Cole Memorandum"). The Cole Memorandum does not override federal law enacted by Congress or grant immunity to individuals or businesses from federal prosecution.

On January 4, 2018, Attorney General Jefferson B. Sessions III found this memo unnecessary and rescinded it. The Attorney General directed prosecutors to follow the well-established principles that govern all federal prosecutions in deciding which marijuana activities to prosecute given the Department's finite resources. These principles require federal prosecutors "to weigh all relevant considerations,

including federal law enforcement priorities set by the Attorney General, the seriousness of the crime, the deterrent effect of criminal prosecution, and the cumulative impact of particular crimes on the community." [January 4, 2018 Memorandum For All United States Attorneys from Jefferson B. Sessions, III, Attorney General, Subject: Marijuana Enforcement; see U.S. Attorneys' Manual, Chapter 9-27.000](#).

According to the A.G. summary of Proposition 64, the DOJ chooses not to prosecute most marijuana users and businesses that follow state and local laws if those laws are consistent with federal priorities. Those priorities include preventing minors from using marijuana and preventing marijuana from being taken to other states.

In 2016 California voters approved Proposition 64. Prop 64 makes it legal under California law for individuals 21 years of age or older to use marijuana for recreational purposes starting in 2017. This proposition also allows commercial manufacture and sale starting in 2018. It imposes state taxes on sales and cultivation, provides for licensing the industry, and establishes standards for marijuana products.

However, under Federal Controlled Substances Act, [21 U.S.C. section 841](#), it is illegal to manufacture, distribute, or dispense marijuana. Marijuana is classified as a Class 1 substance – meaning it has no medical value and poses a high risk of abuse. [21 U.S.C. section 812](#).

Confidentiality

A San Francisco Bar opinion offers this important warning to lawyers who counsel their clients regarding marijuana:

The lawyer should counsel the client about limitations on confidentiality. One of the duties of a California lawyer is to "maintain inviolate the confidence, and at every peril to

himself or herself to preserve the secrets, of his or her client.”

Bus. & Prof. Code § 6068(e)(1). The lawyer should warn the client that their communications may not be privileged in the event of litigation. The “crime fraud” exception to the attorney-client privilege applies if the lawyer’s services are obtained to help the client to plan or to commit a crime. **Evid. Code § 956.** The client’s mere disclosure of his or her intent to commit a crime is privileged. *People v. Clark* (1990) 50 Cal.3d 583, 621-23. But where the client seeks legal assistance to plan or to perpetrate a crime, the privilege is eviscerated. *Id.* Thus, the lawyer should warn the client that, if the client becomes involved in civil or criminal litigation, there is a risk that the communications between them will not be held to be privileged and thus be subject to disclosure in testimony.

Third parties face legal issues as well, and their lawyers, landlords who lease property, banks who lend to or provide banking services to, security companies and armored car companies who provide such services to marijuana-related businesses, have to consider the impact of this conflict in federal and state law.

Insurance Cases

There have been a few insurance cases concerning the medical and recreational marijuana industries. Most of these cases have focused on first party property losses, but there have been cases concerning use of other controlled substances, and the effect on coverage where policies contain controlled substances exclusions.

In *Am. Nat'l Prop. & Cas. Co. v. United Specialty Ins. Co.*, No. CV 11-1137 LFG/RHS, 2012 WL 12549878, at *8 (D.N.M. Sept. 24, 2012), *rev'd and remanded sub nom. Am. Nat. Prop. & Cas. Co. v. United Specialty Ins. Co.*, 592 F. App'x 730 (10th Cir. 2014), there were lessons for employers of drivers, if the employer's insurance policy contains a controlled substances exclusion.

In that case, Edward De La Paz, an employee of Endeavor Services, Inc., was driving a vehicle owned by Jimmy Cooper (Cooper financed Endeavor and was its director, and his children owned a majority of the stock) while in the course and scope of employment. He crossed the centerline and collided head-on with another vehicle. Both drivers died. De La Paz tested positive for methamphetamine. ANPAC issued a personal auto and commercial umbrella policy to Cooper, the vehicle owner. Great West issued commercial auto coverage to Endeavor, and United Specialty issued excess coverage to Endeavor. ANPAC's umbrella policy excluded “bodily injury arising out of the use, ... or possession by any person of a controlled substance.” Based on this exclusion, ANPAC asserted that the controlled substance exclusion applied. The court agreed, noting that the ANPAC umbrella policy exclusion for damages “arising out of” use of controlled substances was not ambiguous as applied to the accident as De La Paz was under the influence of methamphetamine, and the police report identified “driver inattention” as a contributing factor in the accident.

There are variations on wording of controlled substances exclusions.

The most typical reads:

Controlled Substance

“Bodily injury” or “property damage” arising out of the use, sale, manufacture, delivery, transfer or possession by any person of a Controlled Substance as defined by the Federal Food and Drug Law at 21 U.S.C.A. Sections 811 and 812. Controlled Substances include but are not limited to cocaine, LSD, marijuana and all narcotic drugs. However, this exclusion does not apply to the legitimate use of prescription drugs by a person following the lawful orders of a licensed health care professional.

Some policies have additional exclusions. In *Prudential Prop. & Cas. Ins. Co. v. Brenner*, 350 N.J. Super. 316, 321, 795 A.2d 286, 288 (App. Div. 2002), the exclusion added certain exceptions.

However, this exclusion does not apply to:

(2) The insured's [sic] who have no knowledge of the involvement with a controlled substance(s).

An insured's knowledge of such involvement must be shown by us by competent evidence of such knowledge.

Despite changes in the law of certain states, such as California, Colorado and Washington, marijuana continues to be a Schedule 1 drug, 21 U.S.C. section 812, and so within the exclusion.

These controlled substances exclusions have been applied to illegal drugs (*Westfield Nat'l Ins. Co. v. Long*, 811 N.E.2d 776 (2004) (methamphetamine)) and to controlled substances possessed under a prescription (*Forman v. Penn*, 945 N.E.2d 717, 719 (Ind. App. 2011) (methadone, used by another, not the person holding the prescription)). In the latter case, language in the exclusion stated that “this exclusion does not apply to the legitimate use of prescription drugs by a person following the lawful orders of a licensed health care professional.” Nonetheless, since the substance was not prescribed for the person who was injured by using it, the court held that the exclusion applied, since it applied to use by “any” person of a controlled substance. *See also Massachusetts Prop. Ins. Underwriting Ass'n v. Gallagher*, 75 Mass. App. Ct. 58, 911 N.E.2d 808 (2009) (overdose of prescribed medication negligently left in a place accessible to others, claim excluded by a controlled substances exclusion).

These exclusions, depending upon the wording, may not be limited in effect to an employee using a controlled substance. For example, in the *American National v. United Specialty* case discussed above the exclusion applied to “bodily injury arising out of the use, ... or possession by any person of a controlled substance.” The use of the phrase “any insured” is most often interpreted to apply to all insureds. So here, the exclusion would apply to the driver and to his employer as well since both were insureds. A business might want a narrower exclusion that applies to “the insured” which would then apply on an

insured-by-insured basis, so that the employer would not lose coverage if the employee used or possessed a controlled substance.

With medical marijuana, there is a complication as to the exception for prescription drugs: "However, this exclusion does not apply to the legitimate use of prescription drugs by a person following the lawful orders of a licensed health care professional." A doctor may not prescribe marijuana because it is a Schedule I drug. *Gonzales v. Raich* (2005) 545 U.S. 1, 14-15. However, under California law, a doctor may recommend use of marijuana and discuss treatment options with patients, even though that might lead to illegal conduct. *Cal. Health & Safety Code Ann. §§ 11362.5(d), 11362.7(h)*, noted in *Gonzales v. Raich, supra*, 545 U.S. 1, 55. While methadone and other drugs discussed in the case law above can be prescribed for medical use under federal law, the same is not so for marijuana. Arguably then, use of medical marijuana is not a use of a "prescription drug" following "lawful orders of a licensed health care professional."

These controlled substances exclusions are typically not found in business policies. If in the future there are adverse loss developments occasioned by use of marijuana, such exclusion may become more commonplace. In the automobile context this would most likely be at higher levels of coverage above primary, minimum financial responsibility limits levels.

Most published cases, and most claims arising from medical and recreational marijuana businesses, have related to first party coverage and not to third party coverage. Marijuana exclusions may be on the horizon. Make sure you have clear policies for dealing with marijuana use to avoid liability for prescription or non-prescription drug use.

For liability purposes, businesses seem to be protected for the time being, but personal exposure cannot be eliminated. The best bet is to treat marijuana as if you are aware of it, the same as alcohol use. ■

Timothy M. Thornton, Jr. is a Partner in the Encino office of Gray•Duffy, LLP. With more than 25 years' experience, Mr. Thornton provides legal counsel on insurance-related matters, such as mass torts, toxic torts and exposures, and environmental contamination. He may be contacted at 818-907-4000 and tthornton@grayduffylaw.com.

Erin K. Tenner is a Partner in the Encino office of Gray•Duffy, LLP. Ms. Tenner is particularly experienced in representing automotive dealers in the areas of employment law; commercial real property transactions and leases; shareholder, partnership and operating agreements; corporate, LLC and partnership formation; and mediation of business-related disputes. She may be contacted at 818-907-4000 and etenner@grayduffylaw.com.