

## Outside Counsel

# Social Equity: The Driver Behind New York's Cannabis Program

The past several months have ushered in great change for cannabis companies, their investors, employees, consumers and service providers in the Northeast. New Jersey, New York and Connecticut have, in succession, approved adult-use cannabis programs in early 2021, adding a combined population of 33.4 million to states that have liberalized the cultivation, sale, possession and use of cannabis for adults. The adult-use cannabis market in New York is expected to exceed \$4.2 billion in revenue by 2027. Once fully implemented, Governor Cuomo's office expects more than \$300 million in annual tax revenue.

### Federal/State Dichotomy

Marijuana remains classified as a Schedule I controlled substance under the U.S. Controlled Substances Act of 1970, as amended, and is illegal

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under federal law for any purpose, and state and federal laws regarding marijuana often conflict. In mid-July, U.S. Senators Schumer, Wyden and Booker introduced, as a draft discussion piece, the wide-ranging and ambitious Cannabis Administration and Opportunity Act (CAOA), which would legalize cannabis on the federal level. The CAO faces an uncertain future and is beyond the scope of this article, which focuses on the social equity part of New York's cannabis program.

### New York's MRTA And Social Equity

In March, after several years of failed efforts, partly due to quarrels over what to do with the tax windfall and how the opportunities in

the industry would be apportioned across large and small businesses, New York adopted the Marijuana Regulation and Tax Act (MRTA) to legalize and create a comprehensive system to oversee and regulate cannabis. A new Office of Cannabis Management will be created to oversee the new adult-use program, as well as the State's existing medical and cannabinoid hemp programs. Additionally, the adult-use law will

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offer enhanced licensing opportunities and assistance to entrepreneurs in communities of color who have been disproportionately impacted by the war on drugs due to the state legislature's emphasis on social equity and justice and righting the wrongs of the war on drugs, which is increasingly being viewed as racist and disproportional in its impact

on communities of color and lower-income populations.

MRTA's legislative intent stated: "The intent of this Act is to regulate, control and tax marijuana, heretofore known as cannabis, generate significant new revenue, make substantial investments in communities and people most impacted by cannabis criminalization to address the collateral consequences of such criminalization ..." The legislature found that "Existing laws have been ineffective in reducing or curbing marijuana use and have instead resulted in devastating collateral consequences including mass incarceration and other complex generational trauma ... Existing marijuana laws have disproportionately impacted African-American and Latinx communities." Indeed, MRTA requires that criminal convictions of all those who would not be subject to prosecution under its regulations will be expunged within two years and favors those applicants for licenses with non-violent drug convictions.

Unlike other states where relatively few licenses have been granted and the established multistate operators (MSOs) have been able to secure dominant market share, New York's plan for cannabis is designed to grant a fairly large number of licenses (perhaps 1,000 or more) and to ensure that 50% of the licenses are awarded to socially and economically disadvantaged groups, and that barriers are placed to preclude vertical integration in the adult-use field (in contrast to the concentration of vertically

integrated medical marijuana licenses in New York in only 10 entities). MRTA uses a multi-tier regulatory system, in some ways similar to how alcohol is regulated in that retailers cannot have interests in other parts of the supply chain.

In New York, a social equity applicant is a person of color, a woman, a disable veteran, a farmer in defined financial distress and those persons from communities disproportionately impacted by the war on drugs. Priority is given to those earning 80% or less of their county's median income, are from an area disproportionately impacted by cannabis laws (high incarceration rates), or have a criminal conviction for marijuana-related offense (or has a family member with such a conviction). MRTA earmarks 40% of tax revenue from marijuana sales to be used for a community grant reinvestment fund to issue grants to non-profit organizations serving communities disproportionately affected by the war on drugs. Such grants will be used for: job placement and skills training, mental health and substance abuse, nutrition and financial literacy. An additional portion of the tax revenue will be used to fund a state-run incubator program for small businesses and social equity applicants, including no-interest loans. Social equity licenses are not transferable for three years except to another social equity licensee. Non-social equity applicants need to develop a social responsibility framework as part of their application process, adherence to which will be a determining factor in renewals of



Credit: Ian Miller/Adobe Stock

licenses. All licenses are initially for two years.

MRTA mandates a 9% state tax and 4% municipal tax on the sale of cannabis, which contrasts with NJ and CA which, through a pyramiding of sales tax, transfer tax and excise tax that exceed 20% all-in. Licensing fees were not established in MRTA and are awaiting rulemaking. The expectation is that social equity applicants will have nominal or waived application fees and micro-businesses will have reduced application fees. The 10 existing NY medical marijuana licensees (Registered Organizations or ROs), each of which is required to be vertically integrated for the medical program, will be allowed into the adult-use program as the only licensees with vertical integration (other than micro-businesses) in exchange for a seven figure fee which will subsidize the social equity applicants. Three adult-use dispensaries per RO are permitted, as well as co-location with medical-use dispensaries.

The key license types under MRTA are:

- Cultivator License (grow);
- Dispensary License (retail sales to public, capped at three stores per licensee);

- Processor License (refine, extract, manufacture products other than raw flower);
- Distributor License (move products from cultivators or processors to dispensaries);
- Delivery License (home delivery to consumers but limited to 25 delivery persons per license);
- Micro-Business License (an exception to the ban on vertical integration but as the name suggests, size limitations); and
- On-Site Consumption License (like bars).

Any town or village can prohibit cannabis dispensaries and/or on-site consumption lounges by Dec. 31, 2021, but that municipality will then not receive tax revenues related to the retail sale or transfer of cannabis products. Since local governments can opt out only prior to Dec. 31, but can opt-in later, the thinking is that many may do so. In addition, municipalities may pass local laws governing the “time, place and manner” of such cannabis businesses.

Limited home growing of cannabis for adult-use will be permitted 18 months after the first commercial sale in a dispensary in order to foster an economically viable industry and ensure the value of applying for a license.

Finally MRTA sets forth several new offices and boards whose seats will need to be filled in order for NY’s adult-use cannabis program to launch and succeed: a Cannabis Control Board (CCB) consisting of five members, three appointed by the Governor and one each by each legislative body; a Chairperson of

CCB with broad powers; an Office of Cannabis Management (OCM), an independent office within the State Liquor Authority to administer the program; the OCM will have an executive director; a Cannabis Advisory Board which will provide recommendations to CCB and is charged with administering the social equity program and community reinvestment; a Chief Equity Officer charged with ensuring that the social equity plans are working. Unfortunately,

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none of these seats have yet been filled and the legislative session has ended, casting great doubt as to whether NY’s adult-use program will proceed with any speed.

### **What Should Hopeful Applicants Be Doing?**

In short, applicants should roll up their sleeves and go after it. They should assemble a team of key professionals that includes lobbyists to deal with state and local governments, real estate brokers to scout suitable locations, insurance brokers, security experts, HR,

business plan writers, application writers and consultants. Also, they should find their financial partners (social equity applicants can issue 49% of their equity to others) and line up at least 12 months of cash requirements. Operating a cannabis business takes capital and staffers in Albany reviewing applications will favor those with the highest likelihood of success.

### **Conclusion**

Social equity concerns run deep throughout MRTA, resulting in legislation which in many ways is anti-big business and pro-small business. MRTA, and the new cannabis license applicants that it enables, will usher in hundreds of new businesses and create thousands of new jobs for New York. Cannabis industry participants are encouraged to consult with experienced cannabis counsel and other professionals at every stage of the life cycle of their venture in order to monitor and seek timely guidance with respect to developments at the federal, state, and local levels.