



Portfolio Media, Inc. | 111 West 19th Street, 5th floor | New York, NY 10011 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

An 11th-Hour Obstacle For Retail Cannabis Licensing In NY

By **Patrick Hines, Matthew Parker and Fallon Martin** (November 21, 2022, 5:47 PM EST)

On the verge of an expected award of the first licenses under New York's Conditional Adult Use Retail Dispensary, or CAURD, program, a federal judge has enjoined the issuance of licenses in the Finger Lakes, Central New York, Western New York, Mid-Hudson and Brooklyn regions.

The injunction prohibits the state from issuing licenses pending the outcome of a lawsuit alleging that New York's rules requiring applicants to have certain state connections run afoul of the dormant commerce clause.

New York's plan to begin retail sales of adult-use recreational cannabis by the end of the year has come to a screeching halt in the five affected regions, and may also impact the other regions of the state.



Patrick Hines

New York's CAURD Program and Variscite's Lawsuit

New York's Marijuana Regulation & Taxation Act, and the regulations creating the CAURD program, require the applicant to be incorporated in New York, maintain residence in New York by a majority of its owners or otherwise have a significant presence in New York.

The CAURD licensing requirements also require majority ownership and sole control of the applicant by one or more justice-involved individuals. To be justice-involved, the individual or their spouse, parent, guardian, child or dependent must have been previously convicted of a cannabis-related offense in New York.



Matthew Parker

In addition, one justice-involved individual must own 30% or more of the applicant, have sole control of the applicant and have a significant presence in New York state.

The New York regulations also outline criteria for evaluating applicants, including among other things whether the justice-involved individual lived in areas with high rates of prosecution for cannabis-related offenses, in areas with low median income or in public housing in New York.

Finally, the regulations permit the New York Office of Cannabis Management, or OCM, to create regional geographic zones among which applicants are asked to rank their preferences.



Fallon Martin

Variscite NY One Inc. is a New York corporation 51% owned by an individual with no substantial presence in New York, and a prior cannabis conviction that occurred in Michigan under Michigan law.

In September, as the window for applications closed, Variscite sued in the U.S. District Court for the Northern District of New York. Variscite alleges that the CAURD program places an undue burden on interstate commerce by requiring applicants to have a New York conviction and a significant presence in New York.

Variscite also sought a preliminary and permanent injunction preventing the OCM from issuing CAURD licenses in the regions for which Variscite stated a preference in its application: Finger Lakes, Central New York, Western New York, Mid-Hudson and Brooklyn.

Just days before the first CAURD licenses were set to be awarded, on Nov. 10 the court granted the preliminary injunction and prevented the issue of any licenses in those regions.

The Dormant Commerce Clause

Variscite's arguments rely on a constitutional concept called the dormant commerce clause. The commerce clause of the U.S. Constitution gives Congress the authority to regulate interstate commerce. The dormant commerce clause concept infers that the commerce clause also has a negative component, which prohibits states from discriminating against or unduly burdening interstate or international commerce.

In essence, the dormant commerce clause prohibits or restricts state economic protectionism. When a state requirement discriminates against out-of-state economic actors or goods, the requirement must be narrowly tailored to advance a legitimate local purpose.[1]

In granting the preliminary injunction Variscite requested, the court rejected the OCM's argument that the CAURD residency requirement did not unduly burden or discriminate against interstate commerce.

The court held without much analysis that the facial requirements of a significant presence in New York and a New York cannabis-related conviction would have a discriminatory effect on out-of-state residents seeking a CAURD license.

Variscite's lawsuit is not the first to challenge state cannabis programs that attempt to favor in-state applicants. In August of this year, the U.S. Court of Appeals for the First Circuit affirmed a decision striking down provisions of Maine's medical cannabis program that required all officers and directors of medical dispensaries to be residents of Maine.[2]

In that case, the court rejected the argument that the restriction comported with the dormant commerce clause because the cannabis market is federally illegal. The First Circuit ruling added to a string of similar judicial rulings in cases out of Illinois,[3] Michigan[4] and Missouri,[5] which found that residency requirements of state cannabis programs discriminated against interstate commerce.

Major Industry Impact

While the preliminary injunction is limited to just five of the 14 geographic regions delineated by the OCM, other aggrieved applicants may now bring lawsuits seeking similar injunctions affecting the remaining regions.

New York could also face a broader challenge to its Cannabis Law, which requires all applicants for any type of license to have connections to the state that are substantially the same as CAURD's requirements, except for the prior conviction requirement.

It is unclear how long the injunction will hold up CAURD licenses. The OCM will have the opportunity to immediately appeal the injunction, but the appeal could still take several months or longer.

Meanwhile, the OCM has filed a motion to dismiss the case, which mostly raises arguments already rejected by the court. Even if the motion is successful, the same or other litigants could quickly file additional actions raising the same challenges under the dormant commerce clause.

In the alternative, New York could attempt to revamp its CAURD program to remove the challenged requirements. Some of that could be done with expedited rule changes, but some of it may require changes to the Cannabis Law.

It would also likely require the OCM to reopen the application window to additional applicants who previously did not qualify, and could result in far more applications that the OCM intended to consider. The OCM has not yet commented on how it plans to proceed.

The uncertainty will not just affect aspiring retail operators. It will also create headaches for existing participants in New York's cannabis program.

Starting halfway through this year, New York issued the first cultivation and processing licenses. There are now 261 licensed cultivators and 22 licensed processors in the state. The first crops are or will soon be ready for sale, but there may be no retailers to sell to.

One of the arguments the OCM raised in the Variscite case is that this excess product could go to waste at the expense of innocent market participants, or make its way into the still-thriving illicit cannabis market.

Conclusion

The preliminary injunction granted to Variscite has thrown a major wrench into New York's plan to begin adult-use cannabis retail sales by the end of this year.

The OCM is now prohibited from issuing CAURD licenses in five regions of the state, and may face additional lawsuits concerning the other regions. In addition to the CAURD program specifically, the injunction may have a broader impact on the entire Cannabis Law and its New York-based requirements for obtaining licenses.

The ball is now in the OCM's court to make the next move. For now, it appears that New York's long-awaited recreational cannabis program will have to wait at least a little longer.

Patrick J. Hines is a partner and co-leader of the hemp and medical cannabis practice at Hodgson Russ LLP.


Matthew K. Parker is an associate at the firm.

Fallon E. Martin is an associate at the firm.

The opinions expressed are those of the author(s) and do not necessarily reflect the views of their employer, its clients, or Portfolio Media Inc., or any of its or their respective affiliates. This article is for general information purposes and is not intended to be and should not be taken as legal advice.

[1] [Tenn. Wine & Spirits Retailers Ass'n. v. Thomas](#) , 139 S. Ct. 2449, 2459 (2019).

[2] [Northeast Patients Group v. United Cannabis Patients and Caregivers of Maine](#) , 45 F.4th 542 (1st Cir. 2022).

[3] [Finch v. Treto](#) , No. 22 C 1508, 2022 WL 2073572 (N.D. Ill. Jun. 9, 2022).

[4] [Lowe v. City of Detroit](#) , 544 F. Supp. 3d 804 (E.D. Mich. 2021).

[5] [Toigo v. Dep't of Health and Senior Servs. et al](#) , 549 F. Supp. 3d 985 (W.D. Mo. 2021).

All Content © 2003-2022, Portfolio Media, Inc.