KAUFMAN MCGOWAN PLLC
Attorneys-at Law

190 Motor Parkway, Suite 200
Hauppauge, New York 11788
(631) 972-0042
(631) 410-1007 fax
nkaufman@kaufmanmcgowan.com
smcgowan@kaufmanmcgowan.com
www.kaufmanmcgowan.com

August 13, 2024

The Honorable Kathy Hochul
Governor of New York State
NYS State Capitol Building
Albany, NY 12224

Re: New York State Adult Use Cannabis Industry

Governor Hochul:

We applaud your recent efforts to address the challenges faced by the New York cannabis industry (the "Industry"). We provide this letter in an attempt to facilitate these efforts by identifying several actions that we believe can be taken to maximize positive impact on the Industry without significant cost to the State. Please note that this letter is not submitted on behalf of any of our dozens of clients in the Industry, but rather in our capacity as concerned citizens trying to help our home state improve the Industry as quickly and effectively as possible.

We are a New York-based boutique corporate and securities law firm that over the past ten (10) years has developed a significant national and New York corporate cannabis practice. We have participated in over Two Billion Dollars ($2,000,000,000) of cannabis industry transactions across the U.S.A., including in New York, primarily in structuring and restructuring cannabis corporate groups, private and public offerings of securities, mergers and acquisitions, commercial contracts, license applications and legal compliance. We represent, have represented or otherwise have worked with many leading cannabis companies in California, Colorado, Nevada, Washington, Oregon, Maryland and other states, as well as with cannabis industry-leading investors, investment funds and investment banks. As a result of our experiences, we believe that we have gained insights that may be helpful to you, the legislature, the New York Cannabis Control Board (the "CCB") and the New York Office of Cannabis Management (the "OCM") in addressing the urgent challenges faced by the Industry. For context, a further summary of our background is set forth below.

1. We participated in the OCM's Cannabis Compliance Training & Mentorship ("CCTM") and CHIP academy training programs, in connection with which we provided training sessions to social and economic equity ("SEE") licensees and prospective applicants selected by OCM with respect to corporate structure, financing, contract, intellectual property and other cannabis-related legal matters.
2. We participated in OCM's Cannabis Hub and Incubation Program, offering pro bono license application assistance to SEE applicants.

3. We provided detailed comment letters on the proposed and final New York adult-use cannabis regulations (the "Cannabis Regulations"), the first of which we have been advised by (now former) OCM officials was the most helpful comment letter received by OCM.
4. Our partners have several qualifications that have provided particularly relevant experiences, including:
    a. Neil M. Kaufman serving as:
        i. Chairman and chairman *emeritus* of the Long Island Capital Alliance, a non-profit organization which has:
            1. assisted dozens of local companies in raising over $150 million in growth capital, and
            2. hosted five (5) annual cannabis capital forum conferences featuring industry leaders (twice including Chair Wright) and thirty (30) aspiring cannabis companies.
        ii. Director of the Long Island Cannabis Coalition, a non-profit organization devoted to developing the Industry on Long Island, where we live.
        iii. Advisory Board member of the International Cannabis Bar Association, where he has been invited to participate in multiple panel discussions at its annual Cannabis Law Institute.
    b. Sean J. McGowan serving as the founder and co-chair of the Cannabis Committee of the Suffolk County Bar Association.

As we have previously (repeatedly) noted, we remain concerned about the short- and long-term viability of a legally-imposed two-tier structure which prohibits full vertical integration of New York adult-use cannabis businesses, a structure that is used by only one other state and which has resulted there in a market led by companies financed by local billionaires. We note that many states require vertical integration, and that all states except Washington at least permit vertical integration, which we believe is a rational approach that permits market forces to operate in this capital-intensive industry in a manner that promotes development of the state-legal industry, rather than facilitating the illicit market. However, for current purposes we recognize that is unlikely to change and thus we have confined our suggestions to improvements within the existing two-tier structure.

We further note that some of the particularly problematic aspects of New York's current regulatory structure appear to be premised on the assumption that federal legalization of and interstate commerce in cannabis are inevitable. As much as we would love to see this, we are concerned that the inherent complexities of the cannabis industry, the massive cannabis infrastructure investments made in many states and political gridlock in Washington D.C. make the prospects of federal legalization not at all inevitable, and interstate commerce even less likely, for at least an extended period.

We respectfully request and appreciate your consideration of the following concerns and resolutions to address these matters.

1. Retail Tier Investment.

We note that the impaired development of the retail sector of the New York cannabis industry has been a primary bottleneck in the growth of the Industry, and a primary driver of the exorbitant growth of the illicit retail cannabis sector in New York, which we believe is a market-driven response to the inability of the state-legal Industry to satisfy the estimated $6 Billion of inelastic demand for cannabis in our State. We believe that this impaired development has resulted in significant part from a severe

lack of investment capital available to New York retail licensees. We think that there is a way to address this shortage of capital in a substantial way quickly and at no cost to New York State, and hope that doing so will unleash significant growth in the Industry.

Section 123.9(j) of the Cannabis Regulations prohibits any retail dispensary or its true parties of interest ("TPIs") from holding a direct or indirect interest (including by ownership or contract) in any supply-side business (the "Supply Tier"). Accordingly, **any** ownership of New York retail dispensaries is limited to those persons who have **no interest whatsoever** in any non-retail cannabis business **anywhere in the world**. This prohibits investment in a New York retail cannabis business by anyone that owns any interest in an out-of-state supply side business, including any vertically integrated business. This precludes investment in New York retail by any experienced cannabis investor if any of their investments touch the supply side anywhere in the world, which is highly likely considering the nature of the industry. The smallest passive investment in almost any operating company, even a public company or an investment fund, where they have absolutely no influence on management, would preclude their investment in New York retail, even though this would pose absolutely no risk of undue influence. The result of this prohibition has been that thousands of the most likely prospective investors in New York retail cannabis—those that have experience in the cannabis industry—are precluded from so investing. We believe that there are currently at least dozens of family offices, venture capital and private equity funds, and very many individual investors, that have existing cannabis investments that would be willing and able to deploy non-predatory growth capital into New York retail licensees but are completely prohibited from providing this capital unless they divest their entire cannabis portfolio (which is of course impracticable).

We note New York State's initial intent was to provide financing to New York retail cannabis licensees through the Cannabis Social Equity Investment Fund, but that fund has apparently turned out to be unviable. As a result of the lack of capital from the Cannabis Social Equity Investment Fund and the above-described severe restriction on investment by existing cannabis investors, the supply of investment capital available to New York retail licensees is inordinately suppressed. This lack of capital, particularly at such a sensitive stage in the New York industry's growth, has stunted the development of the New York adult-use cannabis market. In turn, this has exacerbated competition from the illicit market, while also forcing well-intended but desperate New York retail licensees to resort to predatory investors to finance their businesses, or to give up on their dream of operating a business with their cannabis license (often after having lost much or all of their net worth).

We understand that the rationale for imposing these investment restrictions is to preclude undue influence on New York retailers by Supply Tier businesses. We believe that the Cannabis Regulations independently contain sufficient protections against such undue influence, and that these overly broad restrictions are unnecessary. Applying these restrictions to out-of-state Supply Tier investments seems to be particularly inappropriate. We understand that such application is based on concerns about protecting the two-tier structure in a future national industry with interstate commerce. As set forth above, we are skeptical about the likelihood of interstate commerce in cannabis. Accordingly, we view these severe limitations on investment capital, which are currently causing severe distress in our nascent New York cannabis market, as an illogical sacrifice resulting from a false binary choice that unnecessarily risks the development of the Industry.

We believe that this unnecessary and harmful problem can be easily addressed by the CCB amending Section 123.9(j) to permit persons to invest in New York retail cannabis licensees, delivery licensees

and onsite consumption licensees (the "Retail Tier") so long as such person does **not control a New York Supply Tier business**. We note that many states apply a **control standard** for many purposes; as do the Cannabis Regulations themselves, and there is no compelling reason that OCM and CCB cannot do so here. We believe that this would properly calibrate the competing interests in protection against unfair trade practices (which we believe has been over-estimated and is already sufficiently addressed elsewhere in the Cannabis Regulations) with the scarcity of available capital which is crippling New York Retail Tier licensees and thus the entire New York cannabis industry. This approach would have the added benefit of allowing market forces to substantially address the lack-of-capital problem without government funding. We think this would thus provide a significant benefit to New York Retail Tier licensees, and the entire New York cannabis industry, quickly and with minimal cost to the New York State government and New York taxpayers.

Proposed Resolution:

The best solution, which would allow passive investments in both the Retail Tier and Supply Tier, would be for the CCB to amend Section 123.9(j) of the Cannabis Regulations to read as follows:

(j) In addition to any other restrictions or prohibitions in this Part, no adult-use retail dispensary or its true party of interest (except for passive investors) is permitted to ~~hold a direct or indirect interest, including by being~~be a true party of interest~~,~~ (except for a passive investor~~,~~) in or having a goods and services agreement with,~~ or by any other means, in~~ an adult-use cultivator, processor, distributor, cooperative or collective, microbusiness, ROD, ROND, registered organization registered under article 3 of the Cannabis Law, or cannabis laboratory licensee or permittee, ~~or any person outside of New York State, otherwise licensed to conduct the activities authorized under such licenses, registrations, and permits~~in the State of New York.

Alternatively, if only the out-of-state problem is to be addressed, the CCB would amend Section 123.9(j) of the Cannabis Regulations to read as follows:

(j) In addition to any other restrictions or prohibitions in this Part, no adult-use retail dispensary or its true party of interest is permitted to hold a direct or indirect interest, including by being a true party of interest, passive investor, or having a goods and services agreement with, or by any other means, in an adult-use cultivator, processor, distributor, cooperative or collective, microbusiness, ROD, ROND, registered organization registered under article 3 of the Cannabis Law, or cannabis laboratory licensee or permittee, ~~or any person outside of New York State, otherwise licensed to conduct the activities authorized under such licenses, registrations, and permits~~in the State of New York State.

2. Unreasonably Impracticable Zoning Restrictions Imposed by Municipalities.

The Marihuana Regulation and Tax Act (the "MRTA") and the Cannabis Regulations prohibit municipalities from imposing unreasonably impracticable local laws and regulations. Notwithstanding this, many municipalities in New York, particularly on Long Island, have flagrantly violated the MRTA by imposing unreasonably impracticable zoning requirements such as (i) banning retail cannabis stores in all retail areas, and (ii) imposing distance requirements from houses of worship, schools, public youth facilities, residential zoned areas and other areas not contemplated by

MRTA or the Cannabis Regulations that effectively prevent or extraordinarily restrict a retail dispensary from opening in such municipalities. As a result, the actions taken by these municipalities have had the chilling effect of preventing retail licensees (both CAURD and adult-use retail dispensary licensees) from finding a location to establish their operations, with the corresponding depressive impact on the supply of state-legal cannabis to consumers and outlets for Supply Tier businesses.

A. Permitted local zoning restrictions should be no more stringent than those applied to licensed businesses under the New York Alcoholic Beverage Control Laws ("ABC")

We understand that MRTA and the Cannabis Regulations have been modeled, in substantial part, on the ABC and the regulations promulgated thereunder applicable to licensed alcoholic beverage businesses. To be more consistent with that approach, we believe that the zoning and distance requirements imposed by localities on cannabis licensees should be no more stringent than the stricter of (i) those specified in MRTA and the Cannabis Regulations, and (ii) those applicable to licensed liquor stores under applicable local zoning rules, ordinances or regulations.

Proposed Resolution:

The CCB should amend Section 119.2 by adding new subdivisions (b) and (c) as follows

(b) It shall be deemed unreasonably impracticable for any municipality to impose:

(1) Any prohibition which has the effect of prohibiting applicants or licensees from operating in areas in which retail businesses licensed under and pursuant to the Alcoholic Beverage Control Law would be permitted to operate, subject to clause (2) below; and

(2) Any distance requirement with respect to a house of worship, school or public youth facility that exceeds any distance requirement applicable to such a house of worship, school or public youth facility as set forth in Section 119.1(a).

(c) Any violation of this Section 119.2 shall be presumptive evidence that such law, regulation, rule or ordinance violates the Cannabis Law and the municipality shall be preempted from adopting, implementing or otherwise enforcing such law, regulation, rule or ordinance, and shall be subject to Section 119.5 of this Part.

B. CCB Advisory Opinions

Section 119.5 of the Cannabis Regulations permits the CCB to review and issue advisory opinions that would constitute presumptive evidence that the local law violates subdivision 2 of section 131 of MRTA. We understand, however, that the CCB does not have the resources at this time to review these claims, issue advisory opinions and otherwise perform its functions under Section 119.5. We believe it is critical for the CCB to issue these advisory opinions as they are a critically powerful tool available to an applicant or licensee in combatting unreasonably impracticable (and thus illegal) local restrictions on the Retail Tier. In that respect, we suggest permitting or requiring the Office of the New York State Attorney General and/or other governmental agencies, such as perhaps the New York

State Liquor Authority, to loan or provide employees as secondees to the OCM and CCB for this purpose.

C. Empowering the New York State Attorney General

We have been told by certain third parties that they have been informally advised by certain municipal officials that while they would be disposed to cooperate in loosening some of their unreasonably impracticable zoning restrictions, they would be far more likely to do so in response to litigation. Unfortunately, many Retail Tier licensees, especially CAURD and other SEE licensees, do not have the resources to fund litigation with their local municipalities. In addition, under N.Y. C.P.L.R. 5519 (the "Appeals Stay Law"), even if a licensee were to prevail in any such litigation, the municipality is entitled to a stay pending appeal. The litigation and appeals process likely would take longer than the provisional period by the end of which the licensee would have to secure a location before losing its license. As a result, the prospect of successfully obtaining a location through litigation is remote for the substantial preponderance of Retail Tier licensees.

We believe that these problems can be addressed by:

1. Similar to the authority granted to the OCM and CCB in Sections 16 and 138-a of the MRTA (as amended), the OCM and CCB should have the ability to request that the NYS Attorney General enforce or bring an action or proceeding against the municipality to obtain judicial enforcement of any CCB advisory opinion, if, within sixty (60) days thereafter, the applicable municipality has not conformed its zoning requirements to the advisory opinion.
2. Any such litigation instituted by the NYS Attorney General should be subject to expedited judicial review, including pursuant to *ex parte* injunctive relief.
3. These proceedings must be exempt from or preempt the Appeals Stay Law.

Proposed Resolution:

CCB should amend Section 119.5 by adding a new subdivision (d) as follows:

(d) In the event a municipality adopts a local law, regulation, rule or ordinance or takes any action that violates any provision of the Cannabis Law or this Part or is in contravention of an advisory opinion issued pursuant to this Section 119.5, then the Office shall have the ability to refer to, request or direct the New York State Attorney General to enforce such provision of the Cannabis Law or this Part or such advisory opinion and take any action necessary, including legal proceedings and ex parte injunctive relief, against the municipality in connection with such non-conforming law, regulation, rule or ordinance or contravening action.

The New York legislature should amend Section 138-a of the MRTA (or create a new section) by adding new subdivisions (15) and (16) as follows:

[The board or the office of cannabis management shall, in accordance with the authority otherwise conferred in this chapter, have the authority to:…]

15. request that the attorney general obtain judicial enforcement of a determination by the board made pursuant to or in connection with subdivision two of section one hundred thirty-one of this

chapter or bring an action or proceeding for the enforcement of any such determination by the board, against a county, town, city, village or municipality which fails to comply with such determination within sixty days after the board's issuance thereof, and for any relief otherwise authorized under this chapter, for a violation contemplated by this section or of this chapter, including the recovery of any applicable civil penalties.

16. in connection with any action or proceeding commenced pursuant to subdivision 15 of this section, apply or request that the attorney general apply for an ex parte order to the supreme court in the county in which the applicable county, town, city, village or municipality is located for an order restraining such county, town, city, village or municipality from taking any action adverse to a board determination made pursuant to or in connection with subdivision two of section one hundred thirty-one of this chapter. Any such action or proceeding shall be (a) decided by the applicable court within thirty days after the filing of any complaint, application, petition or order to show cause relating thereto, and (b) exempt from section five thousand five hundred nineteen of chapter eight of the consolidated laws. In connection with any such action or proceeding, a violation contemplated by this section or of this chapter shall be deemed to (i) cause severe irreparable harm to the applicable applicant or licensee, which cannot be adequately compensated by monetary damages, and (ii) be in contravention of a compelling public interest in the viability of the state's cannabis industry as authorized and contemplated by this chapter.

3. Cultivation Type and Size

The Cannabis Regulations currently authorize a cultivator or microbusiness to cultivate indoor, outdoor or with mixed-light (greenhouse). A cultivator or microbusiness may also choose to combine its cultivation capacity to include both outdoor and mixed-light, with varying square footage limits. For some reason that is not clear to us, there is no option for a cultivator or microbusiness to similarly combine **indoor** cultivation with outdoor and/or mixed-light cultivation.

This is particularly important to microbusinesses. Microbusiness licenses have become a popular choice among New York applicants, particularly SEE and legacy applicants. According to the OCM's report presented at the CCB meeting on August 6, 2024, 152 microbusiness licenses have been issued, of which 54% have been issued to SEE licensees. We have been advised by industry participants that permitting cultivators and microbusinesses to cultivate using any combination of the three cultivation types would significantly aid their businesses, especially in the early stages before expensive indoor facilities are fully constructed.

We are not aware of any compelling reason or public policy consideration that would justify prohibiting cultivators and microbusinesses from combining indoor with outdoor and/or mixed-light cultivation.

Proposed Resolution:

CCB should amend the Cannabis Regulations to:

1. permit indoor microbusinesses (which are currently permitted to have indoor canopy not to exceed 3,500 sq. ft.) to expand their canopy by an additional 2,500 sq. ft. comprised of outdoor and/or mixed-light canopy by adding a new subsection (v) to subsection (1) of subsection (c) of Section 120.3 of the Cannabis Regulations as follows:

(v) Combination canopy not to exceed indoor canopy of 3,500 square feet and outdoor and/or mixed-light canopy of 2,500 square feet.

2. permit indoor cultivators to allocate the square footage of canopy permitted in their tier to any combination of the three cultivation types. This would require changes to multiple Sections of the Cannabis Regulations.

We believe that the combined impact of resolving the foregoing issues would have a material favorable effect on the Industry by:

1. Significantly increasing the proportion of Retail Tier licensees who would be successful in launching their businesses, by increasing the likelihood of:
    a. Attracting the necessary investment capital; and
    b. Finding suitable retail locations, especially in the currently under-served regions of New York State, such as Long Island.
2. Materially facilitating the operational flexibility and success of cultivators and microbusinesses.

While we have additional concerns and ideas about how to address other issues plaguing the Industry, we have limited this correspondence to what we view as the most critical and addressable matters — the "low hanging fruit" that would bear the greatest harvest at the lowest cost to the State.

Should you have any questions, or if we can be of further assistance, please do not hesitate to contact Neil M. Kaufman or Sean J. McGowan at (631) 972-0042 or nkaufman@kaufmanmcgowan.com or smcgowan@kaufmanmcgowan.com, respectively.

Sincerely,

/s/ Neil M. Kaufman

/s/ Sean J. McGowan

cc: Tremaine Wright
Felicia A.B. Reid
Chelsea Davis
John Kagia
Sen. Jeremy Cooney