

## MARIJUANA AND OUT OF STATE INVESTORS

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Colorado does not allow out-of-state ownership of licensed marijuana businesses (stores/dispensaries; cultivation facilities; makers of marijuana-infused products (aka edibles); and testing laboratories). State regulations only allow individuals who have been residents of Colorado for at least two years to hold equity (in any amount) in a licensed marijuana business. Since Colorado opened up the retail marijuana market in January 2014, out of state investors have been trying to find clever ways to lock in a future chance at equity.

In the early months of 2014, the Colorado Marijuana Enforcement Division (the “MED”) permitted out-of-state investors to hold convertible debt in licensed businesses, convertible at the option of the lender when he becomes eligible for ownership. Soon thereafter, the MED only permitted conversion at the option of the borrower, and by the early fall, the MED was not allowing any convertible debt. The MED appears not to have ever approved options or warrants for out-of-state investors.

After a push by parts of the industry, at the end of this year’s legislative term in early May, the Colorado legislature passed, and Governor Hickenlooper is expected to sign, House Bill 1379. The bill creates a new category of interest in a licensed marijuana business known as a “Permitted Economic Interest,” or “PEI.” The bill will permit natural persons who cannot currently qualify as owners of a licensed marijuana business to hold convertible debt, options, warrants, and the like in such businesses, where the right to convert is contingent upon the holder qualifying for and obtaining a license.

“Permitted Economic Interest” means any unsecured convertible debt instrument, option agreement, or any other right to obtain an ownership interest when the holder of such interest is a natural person who is a lawful United States resident and whose right to convert into an ownership interest is contingent on the holder qualifying and obtaining a license as an owner under this Article [statutes concerning medical or retail marijuana] or such other agreements as may be permitted by rule by the State licensing authority.

Most likely, investors can apply to the MED to hold PEIs beginning August 5, 2015, when the law goes into effect, but the MED might not approve any PEIs until it promulgates rules in final form, which it is required to do by January 1, 2016. FGMC will send an update on this issue.

A few important points:

- Only natural persons, not entities, can hold PEIs. Non-U.S. citizens can hold PEIs, so long as they are lawful residents. Colorado residents may also hold PEIs
- As is the case with MED approval to become an owner, MED approval will be necessary to hold a PEI. Persons who will hold PEIs must go through a process, yet to be determined, similar to persons who wish to become owners. Expect the process to be similar in some ways to the process for owners. In particular, the prospective PEI-holder must pass a criminal history record check.

- Other rights to convert to ownership that do not qualify as a PEI (whatever those rights might be) will almost certainly require the holder of that interest to be licensed as an owner, not as the holder of a PEI.