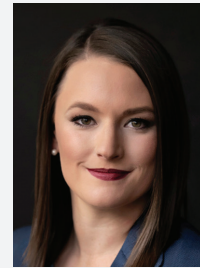


Cannabis in Commercial Mortgage Lending: High Risk, High Reward

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Introduction

Nearly half of U.S. states have fully legalized cannabis usage both recreationally and medicinally.¹ This rapid growth has led an increasing number of commercial mortgage lenders to reconsider financing properties involved in the cannabis industry. After all, the cannabis industry is projected to generate \$57 billion in sales revenue by 2026, creating massive opportunities for investment and interest rate returns.² However, the Controlled Substances Act (“CSA”) still classifies marijuana as a Schedule I drug, making it federally illegal to “knowingly or intentionally...manufacture, distribute, or dispense a controlled substance” or to aid and abet in facilitating that activity.³

Not only is the legalization of marijuana conflicted at the state and federal levels, but other federal statutes make even indirect involvement with cannabis-related business activities unattractive for lenders. Namely, the Money Laundering Control Act (“MLCA”) and the Bank Secrecy Act (“BSA”) impose obligations on lenders to report the uses of controlled substances like marijuana.⁴ And although there have been recent political indications that marijuana may be reclassified as a Schedule III drug at some point in the future, significant regulatory requirements of the aforementioned federal laws continue to impact commercial lenders today.⁵

The contradiction between federal and state cannabis laws generally

results in traditional banks and credit unions entirely abstaining from lending to companies operating within the broader cannabis sphere. A big reason is that the vast majority of financial institutions are federally insured by the FDIC, and therefore subject to federal law.⁶ Moreover, no generally accepted underwriting principles exist to guide the financing of cannabis-related transactions.⁷ Still, an increasing number of lenders are not shying away from loans on properties with licenses cannabis-related uses due to the rapid growth in the industry and the significant potential interest revenue for lenders willing to shoulder the inherent risks of the industry.

Life Insurance Company Lenders and Cannabis

Commercial real estate loans offered by life insurance companies encounter a lot of the same challenges as traditional banks when it comes to financing properties tied to the cannabis industry. However, lending on properties with cannabis-related use can make good sense from a business perspective—especially when the loan-to-value (LTV) ratio is low or other favorable deal points start to outweigh the risks in cannabis lending. The potential financial upside—and an increased push from borrowers who want to freely lease to cannabis tenants—is leading more commercial mortgage lenders to engage with the industry. A particularly favorable deal structure may arise when a cannabis-related tenant occupies a small suite in a large, otherwise attractive retail

center or industrial park. For lenders willing to move toward the cannabis industry, some upfront considerations include (i) the LTV ratio, (ii) the status of state-specific marijuana laws and regulations (including the maturity of the local market and overall success rates of cannabis businesses within such market), and (iii) the type of property being financed.

The inherent risk in cannabis lending typically caps out LTV ratios on cannabis-related loans around 60%.⁸ Therefore, any transactions involving cannabis with a higher LTV ratio should be heavily scrutinized by lenders. Furthermore, a state with a well-developed marijuana jurisprudence (e.g., California, Michigan or Colorado) provides more comfort for lenders regarding the potential success of a cannabis-related tenant. And if a particular state provides higher confidence in the expected investment return, then it is more attractive for a lender to become involved to the cannabis industry.

The type of property being financed often determines whether a lender is willing to consider a particular loan involving a cannabis tenant. To illustrate, commercial mortgage lenders are very unlikely to loan on single tenant properties where the primary use is a cannabis grow or cannabis manufacturing facility. Typically, that is because the failure rate of the tenant’s business is too high, which potentially swallows expected returns and heightens resale concerns due to the specific

buildout requirements of many cannabis facilities. The same is often true for a multi-tenant property where the largest tenant operates in the cannabis industry. As alluded to above, however, a large multi-tenant commercial property with one minor lease to a licensed cannabis dispensary may be palatable, depending on the terms of the specific cannabis lease, confirmation of tenant licensing, and underwriting review of the overall property.

The Hurdle—Obtaining Title Insurance

A major hurdle for lenders considering commercial mortgages involving a cannabis tenant is title insurance. Large, multi-national title insurers typically will not issue policies on properties being used for cannabis-related purposes⁹—even in states where recreational marijuana usage is legal—because they are still subject to personal liability under federal law.¹⁰ Therefore, lenders must exercise careful due diligence during the closing process to ensure that a title company (likely a local or regional insurer) can provide appropriate title coverage for the transaction.¹¹ A direct discussion about cannabis-related coverage between lender’s counsel and the underwriter early in the due diligence process can help address potential title insurance concerns head on.

Useful Contractual Provisions in Commercial Loans Regarding Cannabis

Absolute Prohibition

Because of the risks associated with commercial mortgages involving cannabis-related businesses, the default language in a security instrument is typically an absolute prohibition on cannabis use at the property. An outright bar on marijuana-related activities may involve a representation and warranty in the mortgage similar to

the following: The Premises are not being used and will not be used for the production, distribution or sale of marijuana, cannabis, or their byproducts, and no tenant of the Premises is permitted to use, and to Borrower’s knowledge, no tenant of the Premises has used or is using, the Premises for such purposes.

Illegality Clauses and Incidental Use Limitations

However, lenders intending to prohibit borrower involvement in the cannabis industry can further protect themselves by supplementing an absolute prohibition on cannabis-related uses with (i) illegality clauses and (ii) incidental use limitations.

An illegality clause simply states that marijuana use is prohibited regardless of the legality or illegality of the same, which offers additional protection to a lender loaning on a property in a state with a mature cannabis market where cannabis uses may be more commonplace. Separately, an incidental use clause prohibits any type of marijuana-related business from being conducted on the property, even if such use is tangential to the borrower’s overall business (e.g., whether or not marijuana and/or cannabis is a dominant or incidental use or element of such business or space).

Protecting Lenders Through Indemnification and “Bad Boy” Carveouts

If a lender indeed decides to finance a property that allows cannabis-related uses, it will want to indemnify itself from any potential liabilities arising from federal law. The gold standard is a broad indemnity provision holding the lender harmless against all losses, claims, costs, expense or damages arising from any violation or alleged violation of covenants relating to cannabis use.

Additionally, because commercial loans issued by life insurance companies are generally nonrecourse, lenders can negotiate a specific carveout for any lender loss, cost, damage or expense related to the cannabis use at the property if such a use exists.

Conclusion

Given the murkiness of federal law, an absolute prohibition on cannabis-related activities is still commonplace for many commercial mortgage lenders. For lenders with the larger appetite for risk, however, a loan to a sophisticated borrower that includes available title coverage and adequate protections in the security instrument to help shift the inherent risk of the industry can be very attractive. We are interested to monitor future developments in the industry and across the political realm that may make commercial mortgage financing more widely available to borrowers involved in the cannabis industry in the next few years.

End Notes

¹ MARIJUANA STATE LEGAL STATUS CHARTS: OVERVIEW (2025), Westlaw W-022-1732.

² Heidi Urness, *Marijuana & Banking: What’s the Hold Up? Pt. 1 – Conflicting Legal Landscapes*, MCGLINCHY STAFFORD (March 27, 2023), <https://www.mcglinchey.com/insights/marijuana-banking-whats-the-hold-up-pt-1-conflicting-legal-landscapes/#1>.

³ 21 U.S.C. § 841 (2018).

⁴ MARGARET E. TAHYAR & JEANINE P. MCGUINNESS, FINANCIAL SERVICES AND THE US CANNABIS SECTOR (2019), Westlaw W-019-846.

⁵ Larry K. Houck, *Schedule III Marijuana Would Still Be Regulated Marijuana*, FDA LAW BLOG (March 25, 2025), <https://www.thefdalawblog.com/2025/03/schedule-iii-marijuana-would-still-be-regulated-marijuana>.

⁶ Tracy A. Gallegos & Michael D. Schwamm, *Debt Financing in the Cannabis Industry*, BLOOMBERG LAW (Dec. 2022), <https://www.bloomberglaw.com/external/document/XFAEEE8000000/finance-professional-perspective-debt-financing-in-the-cannabis->

⁷ *Why is it so Difficult to Find Cannabis Financial Services?*, GREEN CHECK (March 5, 2024), <https://greencheckverified.com/cannabis-financial-services-difficult>.

⁸ Stacy Litke, *The Road Ahead for Cannabis Lending in 2025*, MJBIZ DAILY (March 27, 2025), <https://mjbizdaily.com/cannabis-lending-prospects-for-2025/#:~:text=To%20mitigate%20these%20risks%2C%20lenders,to%20concerns%20about%20resale%20value>.

⁹ Dennis R. Baranowski, *Three Things All Lenders Must Consider When Making a Cannabis Loan*, GERACI LAW FIRM (Feb. 3, 2021), <https://geracilawfirm.com/cannabis-loans-three-things-all-lenders-must-consider-when-making-a-cannabis-loan>.

¹⁰ CANNABIS: TITLE INSURANCE AND ESCROW CONSIDERATIONS (2025), Westlaw W-038-3084.

¹¹ *Id.*