

Cannabis Industry D&O Insurance: Spotting the Red Flags

As the cannabis industry matures, more companies are navigating complex corporate structures, regulatory oversight, and investor expectations. Alongside growth comes an increased demand for Directors and Officers (D&O) insurance, which protects executives and board members from personal financial liability in lawsuits related to their decisions and management actions.

But not all D&O policies are created equal, and for cannabis businesses, the stakes are particularly high. Given the industry's ongoing federal illegality, the heavy involvement of regulators, and heightened litigation risks, exclusions buried in the fine print of a policy can mean the difference between being covered in a lawsuit or facing crippling legal bills alone.

This article explores key D&O exclusions that cannabis executives and investors should carefully watch for, as they often represent red flags signaling inadequate or risky coverage.

Why D&O Insurance Is Critical in the Cannabis Sector

D&O insurance is essential for any company, but in the cannabis space, it becomes even more critical. Leaders in cannabis businesses face lawsuits from investors, regulators, competitors, and even other executives. Common claims include misrepresentation, breach of fiduciary duty, regulatory noncompliance, and failure to disclose risks to shareholders.

The evolving legal landscape adds another layer of complexity. State-legal businesses still operate under the cloud of federal prohibition, leaving them more vulnerable to disputes and scrutiny. As a result, cannabis executives cannot afford to take D&O policies at face value—every exclusion needs to be reviewed with care.

Conduct Exclusions: The Subtle Language That Matters

Nearly all D&O policies include **conduct exclusions**, which deny coverage for fraudulent or criminal behavior. On the surface, this may seem straightforward—illegal conduct should not be covered. However, in cannabis insurance, the challenge lies in how the exclusion is worded.

Subtle phrasing differences can determine whether coverage applies to allegations versus proven misconduct. For instance, if a policy excludes claims based merely on allegations of fraud or dishonesty, executives may be left without defense coverage even before a court makes a ruling. The best protections ensure exclusions only apply after a final adjudication of wrongful conduct, preserving defense coverage until liability is established.

Regulatory Exclusions: Risky in a Heavily Regulated Industry

Regulatory exclusions are particularly concerning in the cannabis industry. These provisions rule out coverage for claims brought by regulators, banking authorities, or self-regulatory bodies.

For cannabis companies, this is a serious limitation. Interactions with regulators are routine and disputes are not uncommon, given the ever-changing compliance requirements across states. A regulatory exclusion can leave executives exposed in some of the most likely claim scenarios, undermining the very purpose of D&O insurance.

While some limitations are standard, cannabis companies should negotiate for carvebacks that preserve coverage in cases involving regulatory investigations or settlements, especially when allegations are not tied to intentional misconduct.

Insured vs. Insured Exclusions: Evolving Carvebacks

An **insured vs. insured exclusion** prevents coverage when one insured individual (such as a director or officer) sues another. Insurers include these to avoid coverage for internal disputes.

In practice, however, these exclusions can create problems. Cannabis companies often have dynamic leadership teams and investor groups where disputes arise. Without careful carvebacks, this exclusion may wipe out coverage for shareholder derivative suits, bankruptcy-related claims, or whistleblower actions.

Because the cannabis industry is still young and governance disputes are common, executives must carefully review insured vs. insured exclusions and ensure that carvebacks keep pace with modern legal realities.

“Laser” Exclusions: Targeting Specific Risks

Underwriters sometimes issue **“laser” exclusions**, which carve out specific risks they are unwilling to cover. In cannabis, this might include certain regulatory exposures, securities actions, or even specific individuals with prior legal issues.

While some targeted exclusions may be unavoidable, they should always raise questions. A laser exclusion could mean that the very risk your company is most likely to face is excluded from coverage. Cannabis executives should carefully weigh whether a policy with significant laser exclusions is worth the premium, or whether it signals an insurer’s reluctance to provide meaningful protection.

Antitrust or Competition Exclusions: A Growing Concern

Some D&O policies exclude coverage for **antitrust or competition-related claims**, especially those involving securities offerings and public trading.

For cannabis businesses preparing for rapid growth, mergers, acquisitions, or eventual public listings, these exclusions are dangerous. Antitrust scrutiny and investor lawsuits are real possibilities as the industry consolidates. Excluding these claims removes protection exactly when companies need it most.

Executives should confirm that their policy provides coverage for securities and competition-related claims, particularly if they plan to expand into new markets or attract institutional investors.

Oddball Exclusions: Commissions and FTMI

In addition to common exclusions, there are rare but notable ones that cannabis companies should not ignore.

- **Commissions Exclusions:** These deny coverage for claims tied to payments made to agents or foreign officials. While rooted in anti-bribery concerns, these exclusions are typically outdated and unnecessary for most businesses. For cannabis companies, their presence may be a red flag that the insurer is recycling old policy language without tailoring coverage to industry realities.
- **Failure to Maintain Insurance (FTMI) Exclusions:** Another outdated exclusion, this denies claims if a company fails to keep other insurance policies in force. For cannabis executives, this creates unnecessary risk since gaps in ancillary coverage should not void D&O protection.

Both exclusions are signs that a policy may not be designed with modern cannabis operations in mind.

The Next Step: Negotiating Smarter Coverage

Identifying red flag exclusions is only half the battle. The next step is ensuring your policy offers the right protections. Business leaders in the cannabis sector should:

1. **Work with Experienced Brokers:** Specialized brokers who understand cannabis risks can negotiate better policy terms and carvebacks.
2. **Scrutinize Exclusions Closely:** Don't accept vague or overly broad exclusions—push for precise language that protects executives until liability is proven.
3. **Prioritize Regulatory and Securities Coverage:** Given the cannabis industry's exposure to regulators and investors, these are critical areas where exclusions should be minimized.
4. **Avoid Outdated Exclusions:** Be cautious of policies that recycle old, irrelevant exclusions like commissions or FTMI.

In a fast-evolving industry, D&O insurance must be more than a compliance checkbox. It should be a tailored safeguard that gives executives the confidence to lead without fearing personal financial ruin from litigation.

D&O insurance is indispensable for cannabis companies, but the wrong exclusions can gut its value. From regulatory carveouts to insured vs. insured limitations, every clause deserves close attention. By spotting red flags early and negotiating smarter coverage, cannabis businesses can secure policies that truly protect their leaders.

For a sector built on navigating risk, ensuring strong D&O coverage isn't just prudent, it's a strategic advantage.

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