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Banking Cannabis Businesses

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Marijuana – Agenda

- **The Marijuana Industry Players**
- **Overview of Legal Regime**
- **Hemp**
- **Farm Bill**
- **Defining MRB's**
- **Cash Intensive / Unbanked**
- **Case Study**



Marijuana Industry Players

Direct Businesses

- Growers (Medical, Recreational)
- Dispensaries (Medical, Recreational)

Indirect Businesses

- Lights, Fertilizer, Packaging Providers, Cleaning Services, Armored Cars
- Insurance, Accountants
- Lawyers, Real Estate
- Private Equity / Hedge Funds

Other

- Native American Tribes
- Other Financial Institutions (i.e., Casinos)
- States
- Foreign MRBs

Regulators

- State Regulators
- Banking Regulators (OCC, Federal Reserve Bank, FDIC, NCUA)
- Securities Regulators
- FinCEN

Law Enforcement

- DOJ, US Attorney's Offices
- State and Local Prosecutors

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Marijuana – Overview of Legal Regime

- Forty-six states and the District of Columbia have some level of legalized or de-criminalized medical marijuana:
 - Medical – 30 states and DC **and Puerto Rico**
 - Recreational – 9 states and DC
 - CBD – 16 states
 - None – 4 states
- However, the manufacture, distribution, and dispensing of marijuana for any purpose continues to be a violation of the federal Controlled Substances Act, 21 U.S.C. § 801 et seq., (“CSA”), **even in states where recreational or medical marijuana sales are legal.**



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Marijuana – Overview of Legal Regime

- Federal Money Laundering Statutes
- Bank Secrecy Act – Criminal/Civil Liability
- BSA Regulatory Risk
- Money Laundering Forfeiture
- The Cole Memo
- FinCEN Guidance
- Other Guidance



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Marijuana – DOJ Cole Memo

- August 29, 2013 - Primary Guidance for Federal Prosecutors Regarding Marijuana Enforcement
- Eight Enforcement Priorities:
 - Preventing distribution to minors
 - Preventing revenue from sale of MJ from going to criminal enterprises, gangs, cartels
 - Preventing diversion of MJ from states where it is legal under state law to others
 - Preventing state – authorized MJ activity from being used as a cover or pretext for the trafficking of other illegal drugs or other illegal activity



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- Enforcement Priorities Cont'd:
 - Preventing violence and the use of firearms in the cultivation and distribution of marijuana
 - Preventing drugged driving and the exacerbation of other adverse public health consequences associated with marijuana use
 - Preventing the growing of marijuana on public lands and the attendant public safety and environmental dangers posed by marijuana production on public lands
 - Preventing marijuana possession or use on federal property



Marijuana – 2014 FinCEN Guidance

- FinCEN Guidelines for FIs that Provide Services to MRB Operating in States Where MJ Sales are Legal. *BSA Expectations Regarding Marijuana-Related Businesses*, Fin – 2014 – G001 (February 14, 2014)
- Guidance Intended to “clarif[y] how financial institutions can provide services to marijuana-related businesses consistent with their BSA obligations [and] enhance the availability of financial services for, and the financial transparency of, marijuana-related businesses.”
- FinCEN Guidance - Customer Due Diligence Standards May be Difficult for FIs to Meet:
 - Conduct enhanced due diligence to assess whether services should be provided to MRB
 - Conclude that the business does not “implicate” one of the eight priorities in the Cole Memo.



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Marijuana: 2014 FinCEN Guidance – Cont'd

- SAR Filing Requirements:
 - Marijuana Limited SAR
 - Business does not implicate a Cole Memo priority
 - Business does not violate state law
 - Marijuana Priority SAR
 - Business implicates a Cole Memo priority
 - Business violates state law
 - Marijuana Termination SAR

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Marijuana – Trump Administration

- Attorney General Jeff Sessions rescinded the Cole Memo on January 4, 2018
- The 2014 FinCEN guidance is under review by FinCEN
- Any change in enforcement policy may permit increased federal enforcement of marijuana laws and further constrict banking access



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Hemp

- So what is hemp? *Cannabis sativa L.*
- The same plant as “marihuana”, which is defined in 21 USC § 802(16).
- This fact has generated a long history of enforcement by the Drug Enforcement Agency (“DEA”) and associated litigation, which continues to the present.





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Hemp Under the CSA

- Under the Controlled Substances Act the focus is on the parts of the plant:
 - “The term ‘marihuana’ means all parts of the plant *Cannabis sativa* L., whether growing or not; the seeds thereof; the resin extracted from any part of such plant; and every compound, manufacture, salt, derivative, mixture, or preparation of such plant, its seeds or resin. . . .





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Hemp Under the CSA

- “ . . . Such term does **not** include the mature stalks of such plant, fiber produced from such stalks, oil or cake made from the seeds of such plants, any other compound, manufacture, salt, derivative, mixture, or preparation of such mature stalks (except the resin extracted therefrom), fiber, oil, or cake, or the sterilized seed of such plant which is incapable of germination.” (Emphasis added).





Hemp under the CSA

- This confusing statutory definition in the CSA drove DEA enforcement and resulted in litigation challenging the DEA, including DEA rulemaking related to hemp.
- Congress attempted to resolve the confusion wrought by the DEA's enforcement efforts in 2014.

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Hemp under the Farm Bill

- The Agriculture Act of 2014 (aka the “Farm Bill”)
- 7 USC § 5940 – the introductory clause of this statute says “[n]otwithstanding the Controlled Substance Act . . . or any other Federal law . . .”

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Hemp under the Farm Bill

- Defines “industrial hemp” to mean:
 - “the plant *Cannabis sativa* L. and any part of such plant, whether growing or not, with a **delta-9 tetrahydrocannabinol concentration of not more than 0.3 percent** on a dry weight basis.” (Emphasis added).
 - Very different from the CSA definition – the focus is on THC content, not the part of the plant.

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Hemp under the Farm Bill

- Authorizes a “pilot program” to study the growth, cultivation, or marketing of “industrial hemp” in States that permit the growth or cultivation under state law.
 - Institutions of higher education; or
 - State Departments of Agriculture
 - Licensing and registration required under State law





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Hemp under the Farm Bill

- National Conference of State Legislatures (“NCSL”) – listing of State Industrial Hemp Statutes:
 - <http://www.ncsl.org/research/agriculture-and-rural-development/state-industrial-hemp-statutes.aspx>
 - At least 34 states of passed laws related to industrial hemp

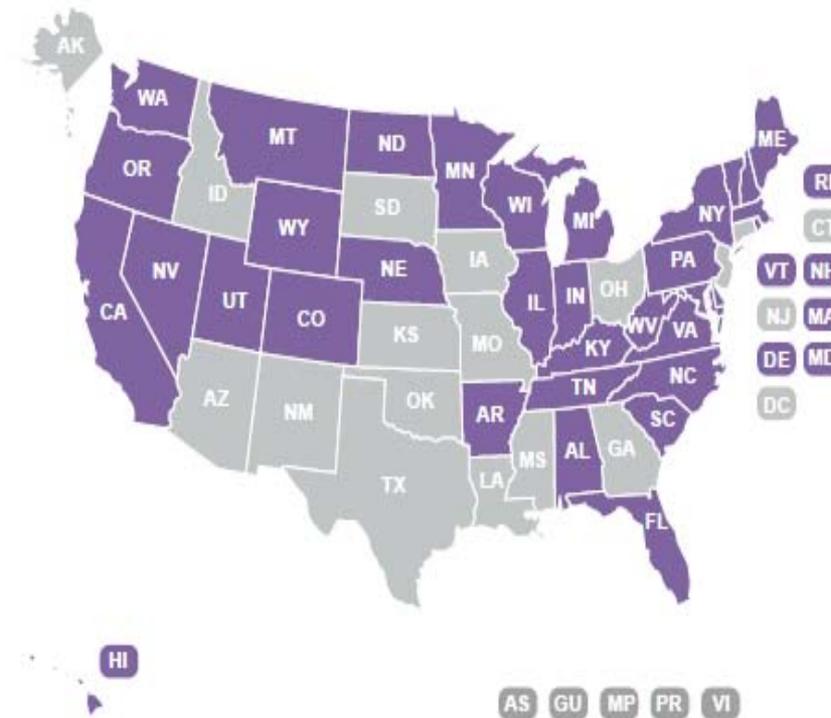




NCSL Map

State Laws Related to Industrial Hemp

Purple	Gray
Allows cultivation of hemp for commercial, research or pilot programs	Does not allow cultivation of hemp.



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Post Farm Bill – DEA actions

- The DEA attempted several enforcement actions against Farm Bill Compliant industrial hemp pilot programs, including one involving the University of Kentucky in May 2014.
 - Who are the Senators from Kentucky?
 - Majority Leader Mitch McConnell and Rand Paul, MD

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Hemp under the Spending Bill

- In response, Congress passed a provision in the Appropriations Bill in 2016 that prohibits the DEA from interfering with the interstate transportation of industrial hemp grown pursuant to the Farm Bill.
 - Pub. L. No. 114-113, § 763, 129 Stat. 1175, 2285 (2016)





Post Farm Bill – DEA actions

- August 12, 2016 – DEA, FDA and USDA consulted and published a non-binding “Statement of Principles on Industrial Hemp”
- Interpreted the Farm Bill very narrowly
 - Example, no transportation across state lines.
- 81 Fed. Reg. 53395 (August 12, 2016)

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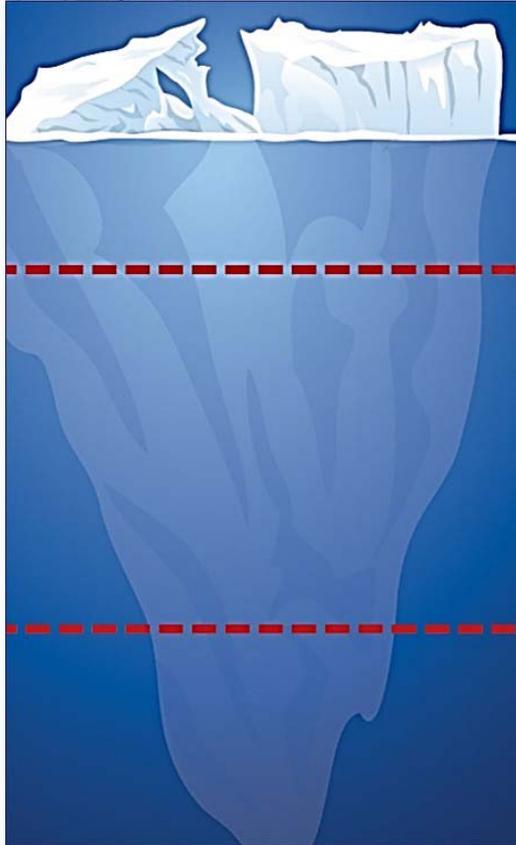
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Future of Hemp

- Majority Leader McConnell on March 26, 2018 announced that he would introduce a bipartisan bill that would “legalize hemp, legalize hemp as an agricultural commodity and remove it from the list of controlled substances.”
 - Stay tuned . . .



Defining “MRB”



Tier 1 (aka “Direct”)

- Plant-Touching (cultivation, production, testing, retail)
- Generally licensed by gov’t agency

Tier 2 (aka “Indirect” or “Ancillary”)

- Non-Plant-Touching
- Generally not licensed by gov’t agency
- Focus on marijuana industry and derive “most” of their revenue from Tier 1 MRBs

Tier 3

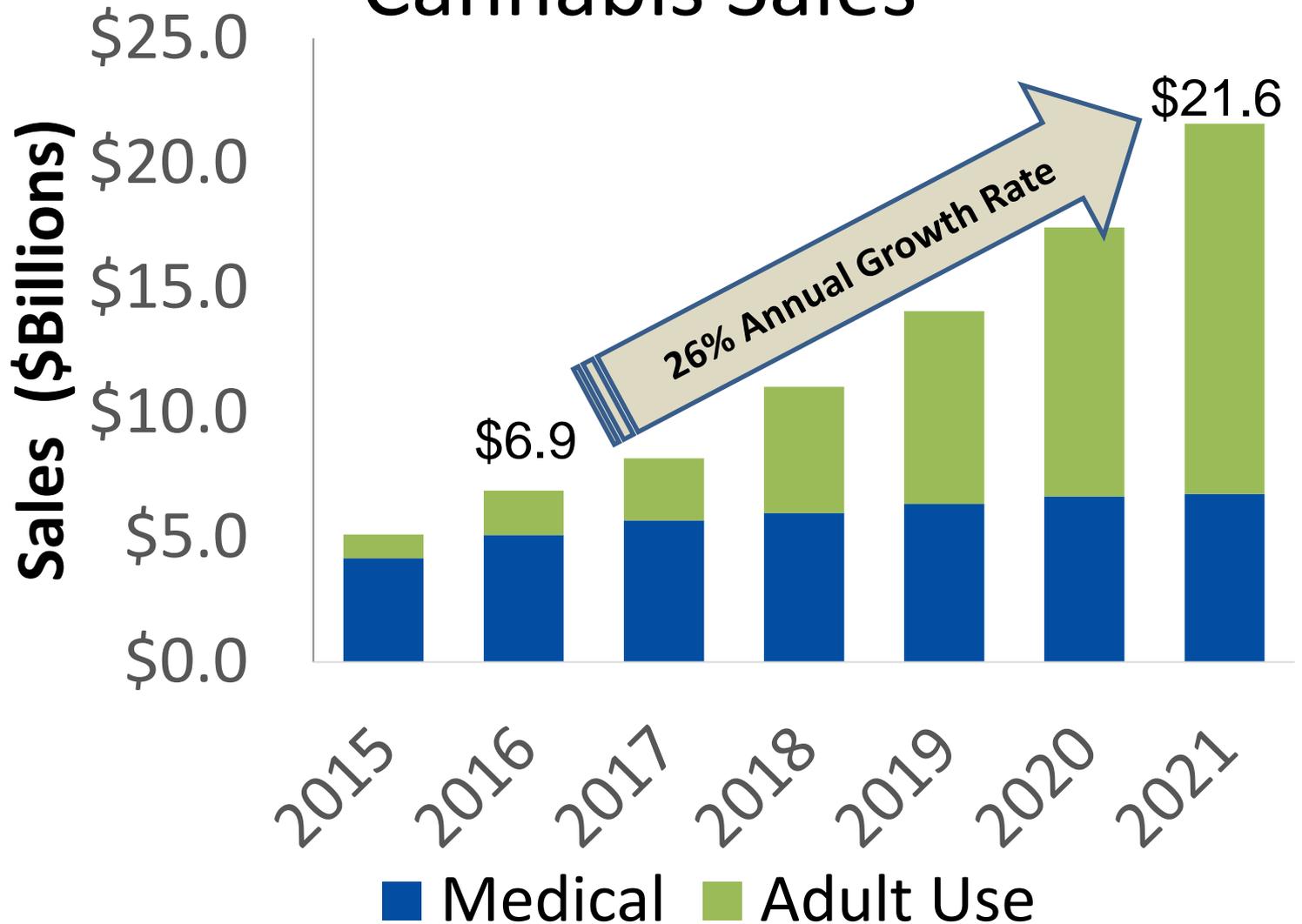
- Known to provide products/services to Tier 1, but ***incidental*** to their overall business
 - Landlords, CPAs, Attorneys, etc.



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Projected North American Legal Cannabis Sales



Source: "The State of Legal Marijuana Markets, 5th Edition" ArcView Market Research.



Cash Intensive ≠ “Unbanked”

- WA – “99%” non-cash MJ tax payments
 - “People say it’s a total cash business in CO and WA ...Quite the opposite.” *WA Director of Banks*
- Los Angeles – 80% non-cash tax payments
 - “...only about 20% of [MRBs] that pay taxes are doing so in cash...Most pay with checks, indicating that they have bank accounts — either openly or on the sly.” *L.A. Asst. Dir. of Finance*
- OR – 75% non-cash tax payments
- MA – 100% including active and applicants
 - ~95% of accounts are in the name of shell/investment company or beneficial owner
 - \$160 million identified at 100 FIs – almost all of which have “strict” no MJ policy

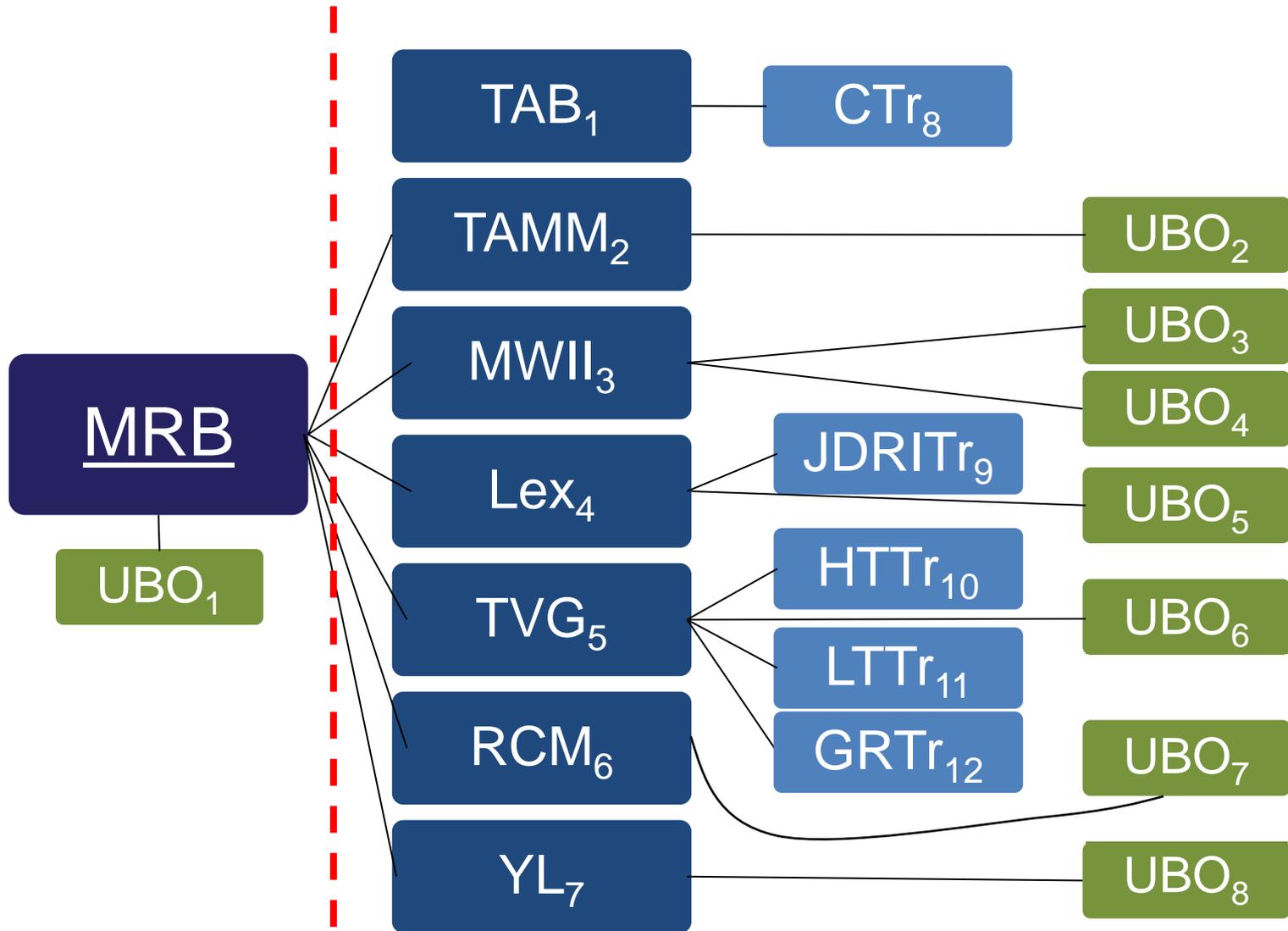
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Case Study: MRB Layering

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Reputational & Regulatory Risk

- *“Big banks worked with pot industry, records show”*
 - Largest US banks shown to have direct accounts with MRBs, despite policies
- *“Marijuana Business Burns Small Illinois Bank”*
 - Community bank put under **consent order** for not **effectively** identifying and managing marijuana-related accounts and risk
- *“New Weapon for Marijuana Opponents: Racketeering Laws”*
 - Large, regional bank named as a defendant in a marijuana-related racketeering lawsuit in CO

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Reputational & Regulatory Risk

- Per FinCEN, 400 DIs “actively” bank MRBs
- Far more **banks** than credit unions

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