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# The Policy Barriers to Marijuana Banking

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# The Policy Barriers to Marijuana Banking

## Summary

Although cannabis-related businesses have thrived in the localities that have legalized marijuana as a consumer product, the industry has suffered from crippling uncertainty, in the form of limited access to the banking system. The cannabis industry thus has been forced to operate in a cash-intensive “gray market,” which is a problem. An entire industry conducting all of its business in cash cannot be fairly taxed or regulated and, historically, has been associated with lawlessness—everything from security concerns, transportation and currency problems, money laundering, and cash hoarding. This brief reviews and analyzes the issues that surround marijuana banking and offers several policy options for addressing the tension between federal enforcement and state sovereignty as it related to marijuana banking.

## Disciplines

Business Administration, Management, and Operations | Business Law, Public Responsibility, and Ethics | Economic Policy | Public Policy

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# The Policy Barriers to Marijuana Banking

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ISSUE BRIEF

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In the last five years, eight states and the District of Columbia have legalized marijuana for recreational use.

Industry analysts forecast that revenues from cannabis-related taxes alone will eclipse one billion dollars in 2018.<sup>1</sup> The industry has suffered from crippling uncertainty, however, in the form of limited access to the banking system, even before the Trump Administration's apparent reversal of earlier accommodations of these state experiments. And without access to banking, marijuana businesses are difficult to regulate and tax with any accuracy.<sup>2</sup> An audit in 2017 by the city of Sacramento, for example, found that because of the cash-intensive nature of the medical marijuana business, some dispensaries there were not sharing proper receipts or were filing inaccurate or misleading financial statements. The head of the city's Office of Cannabis Policy & Enforcement estimated that the consequent tax revenue loss totals \$9 million annually—which dwarfs the \$5 million that Sacramento actually collects from fees and taxes on annual reported marijuana sales.<sup>3</sup> As we look to the future, state experimentation with legalized marijuana will remain small, uncertain, and unsafe, and the potential tax revenue benefits of it will not be maximized, until there is a national, legislative resolution of this national, legal problem.

## SUMMARY

- Although cannabis-related businesses have thrived in the localities that have legalized marijuana as a consumer product, the industry has suffered from crippling uncertainty, in the form of limited access to the banking system.
- The cannabis industry thus has been forced to operate in a cash-intensive “gray market,” which is a problem. An entire industry conducting all of its business in cash cannot be fairly taxed or regulated and, historically, has been associated with lawlessness—everything from security concerns, transportation and currency problems, money laundering, and cash hoarding.
- This brief reviews and analyzes the issues that surround marijuana banking, paying particular attention to the example of Colorado's Fourth Corner Credit Union, chartered in 2014 to serve the “unique financial needs” of cannabis-related businesses, but whose application for a master account from the U.S. Federal Reserve System was denied because of marijuana's continued illegality at the federal level.
- Several policy options are available for addressing the tension between federal enforcement and state sovereignty as it relates to marijuana banking. On the extreme ends, Congress could do nothing until the tension reaches a crisis point; or, it could follow the lead of states like Colorado and legalize marijuana completely. But there are several reasonable “middle ground” options as well, laid out in the conclusion of the brief.



This Issue Brief outlines some of the history around the issue of marijuana banking and offers suggestions to the federal and state governments that continue to navigate a world where marijuana is a recreational consumer product according to the laws of some states and an illicit drug according to the law in the United States.<sup>4</sup> The upshot is simple: so long as the U.S. government, in states and at the national level, speak with contradictory voices, those who participate in the marijuana industry will continue to introduce the social harms often associated with gray markets. This is particularly acute given the vital necessity to any business, large or small, to have access to a functioning financial system.<sup>5</sup> With the national government moving in one direction and states moving in another, marijuana-related businesses and the banks that might serve them cannot cohere on a viable business plan. The result will continue to be legal, practical, economic, and social dysfunction. This federalist experiment divides the governmental house against itself. We either must embrace the experimental nature of our federalist form of government and allow the states their right to embark on this new business, or else forcibly eliminate the

experiment with legalized marijuana altogether.

It is in Colorado that we find perhaps the clearest case of what happens when a legitimate institution tries to provide financial services directly to the cannabis industry and nevertheless fails when it comes up against obstacles imposed by federal statutes and regulations. After a brief recap of marijuana enforcement, with a particular focus on recent history, I will analyze the precedent set in the case of Colorado's Fourth Corner Credit Union. Its lessons are integral to any discussion about marijuana banking. I will then address the problems with the status quo and examine the proposal—along with its major implications and policy barriers—that the federal government get out of the business of regulating and prosecuting marijuana altogether, leaving the states to do as they will with marijuana.

## THE ENFORCEMENT PENDULUM

In 1970, President Richard Nixon signed into law the Comprehensive Drug Abuse and Prevention and Control Act. Title II of the law is known as the Controlled Substances Act.<sup>6</sup> Under this statute, the federal

government classifies each drug under one of five Schedules that are based on a drug's established medical value and its potential for abuse. Since 1970, Congress has given much of the regulatory authority for enforcing the CSA to the Drug Enforcement Administration (DEA), with some assistance from other federal agencies, including the Department of Justice, the Food and Drug Administration, and the Centers for Medicare and Medicaid Services.

These statutes are exercises of national law-making authority, but state governments have retained their own drug-enforcement authority. For decades, the federal and state governments cooperated in drug enforcement. But by the late 20th century and more robustly in the 21st, several states began treating different kinds of drugs differently. The main focus of that "legalization" movement, as it has been called, is on various forms and various uses of marijuana.

In 1996, California voters passed Proposition 215, or the Compassionate Use Act, which legalized—for the first time anywhere in the U.S.—the use of medical marijuana. Soon thereafter, instances arose in which the DEA seized cannabis from medical marijuana users, who took the federal

## NOTES

- 1 Debra Borchardt, "\$1 Billion in Marijuana Taxes is Addictive to State Governors," *Forbes*, April 11, 2017.
- 2 See, e.g., Susan Cleary Morse, Stewart Karllinsky and Joseph Bankman (2009), "Cash Businesses and Tax Evasion," 20 *Stanford Law & Policy Review* 37; and Sam Kamin (2014), "The Limits of Marijuana Legalization in the States," 99 *Iowa Law Review Bulletin* 39, 47.
- 3 Scott Thomas Anderson, "Up in Smoke: Audit Shows Some Sacramento Dispensaries Aren't Paying Up," *Newsreview.com*, October 5, 2017.
- 4 For other useful summaries of the legal and policy issues

addressed here, see Julie A. Hill (2015), "Banks, Marijuana, and Federalism," *Case Western Reserve Law Review*, Vol. 65, No. 3, pp. 597-647 and Lee Reiners and John W. Matthews, "Federal Law Leaves Banks Shying Away from Marijuana Businesses," *The FinReg Blog*, December 5, 2016, available at <https://sites.duke.edu/thefinregblog/2016/12/05/federal-law-leaves-banks-shying-away-from-marijuana-businesses/>.

- 5 Marijuana-related businesses must "rely on short-term loans from individuals, usually with higher interest rates" that also must be in cash. See Serge F. Kovaleski, "Banks

Say No to Marijuana Money, Legal or Not," *The New York Times*, January 11, 2014.

- 6 Controlled Substances Act, available at <https://www.law.cornell.edu/uscode/text/21/812>.
- 7 *Gonzalez v. Raich*, 545 U.S. 1 (2005), available at <https://supreme.justia.com/cases/federal/us/545/1/>.
- 8 James M. Cole, Deputy Attorney General, Memorandum for All United States Attorneys: Guidance Regarding Marijuana Enforcement, August 29, 2013. Available at <https://www.justice.gov/iso/opa/resources/3052013829132756857467.pdf>.

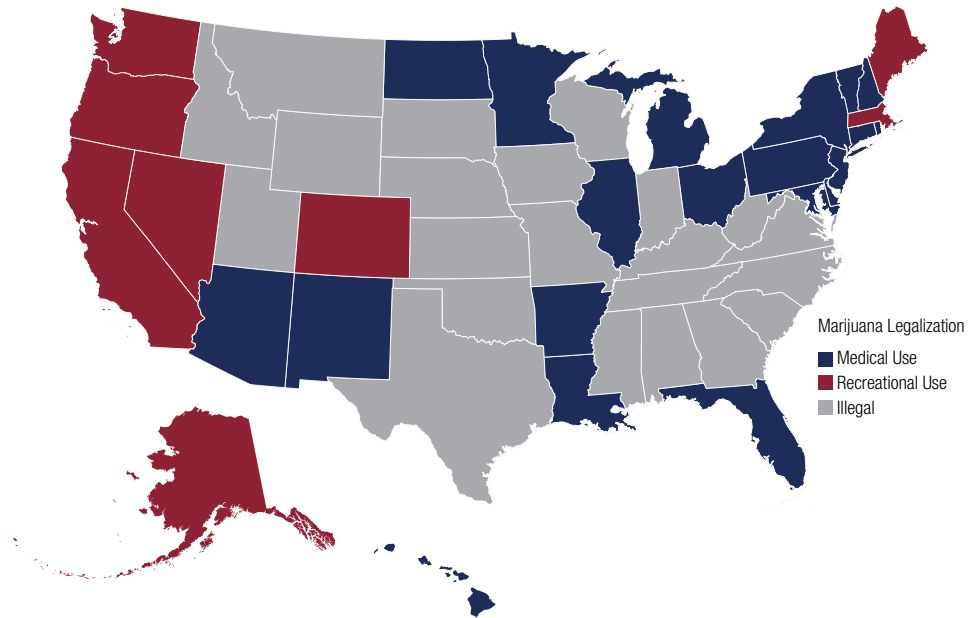


government to court. In the 2005 landmark *Gonzalez v. Raich* case, the Supreme Court held that Congress' Commerce Clause authority includes the power to prohibit the local cultivation and use of marijuana in compliance with California law, even if states approve its use for medicinal purposes and even if the use is entirely intrastate.<sup>7</sup> Despite this ruling, fourteen other states and the District of Columbia joined California by the end of 2012 in legalizing medical marijuana, and two states (Colorado and Washington) had voted to legalize the recreational use of the drug.

In 2013, in response to this spate of legalizations, the Department of Justice issued a memorandum—written by Deputy Attorney General James Cole—explaining the DOJ's enforcement priorities for the use, recreational or otherwise, of marijuana. Known as the Cole Memorandum,<sup>8</sup> the document was not a binding regulation of the Department of Justice but a “guidance” that individuals, private-sector institutions, and governments should follow with respect to marijuana enforcement.

The Cole Memo did not provide a *carte blanche* for the sale, distribution, or use of marijuana in the states that had legalized it, but it did instruct

**FIGURE 1 MARIJUANA LEGALIZATION STATUS BY STATE AS OF JANUARY 1, 2018**



U.S. attorneys to avoid seeking marijuana prosecutions in these states. It also called on these states to employ expansive compliance measures to ensure that other drug-enforcement priorities were met.<sup>9</sup> Under this guidance, states would have to meet eight criteria (i.e., enforcement priorities) to prevent federal interference—for example, blocking the drug from ending up in the hands of minors or from crossing state lines, and ensuring revenue did not end up in the hands of criminals.

A year later, in 2014, the Finan-

cial Crimes Enforcement Network (FinCEN), a joint operation of the DOJ and the Treasury Department, issued additional guidance governing the enforcement of anti-money laundering laws as relevant to the funding and distribution of marijuana by participants in the financial system. It attempted to facilitate a safe operating space for financial institutions to service the marijuana industry.<sup>10</sup> In the same year, the independent financial regulatory agencies—the Board of Governors of the Federal Reserve System, the Federal Deposit

**NOTES**

<sup>9</sup> Hill, *supra* note 4.

<sup>10</sup> The relevant guidance from FinCEN and the DOJ is available at [http://www.fincen.gov/statutes\\_regs/guidance/pdf/FIN-2014-G001.pdf](http://www.fincen.gov/statutes_regs/guidance/pdf/FIN-2014-G001.pdf) and [http://www.justice.gov/usao/waw/press/newsblog%20pdfs/DAG%20Memo%20-%20Guidance%20Regarding%20Marijuana%20Related%20Financial%20Crimes%20%202014%20\(2\).pdf](http://www.justice.gov/usao/waw/press/newsblog%20pdfs/DAG%20Memo%20-%20Guidance%20Regarding%20Marijuana%20Related%20Financial%20Crimes%20%202014%20(2).pdf), respectively.

<sup>11</sup> See the letter from the financial regulators to Governor Islee, located here: <https://www.dfi.wa.gov/documents/banks/letter-agencies-respond-inslee-marijuana.pdf>.

<sup>12</sup> Jefferson B. Sessions, Attorney General, Memorandum for All United States Attorneys: Marijuana Enforcement, January 4, 2018. Available at <https://www.justice.gov/opa/press-release/file/1022196/download>.

<sup>13</sup> Jesse Paul and Jon Murray, “Cory Gardner says AG Jeff Sessions’ decision to rescind marijuana policy ‘has trampled on the will’ of Colorado voters,” *The Denver Post*, January 4, 2018.

<sup>14</sup> Some banks, like MBank in Oregon, took initial steps towards servicing the marijuana industry, based upon the Cole Memo. MBank offered checking accounts to mari-

juana growers and distributors, but after several months, the bank closed all cannabis-related accounts. As the company’s CEO admitted, his bank was “not big enough” to deal with the regulations and due diligence required to service marijuana money. But other determined financial institutions made serious attempts at breaking the stalemate. See “MBank is Closing Its Marijuana Bank Accounts,” *Willamette Week*, Updated January 24, 2017.

<sup>15</sup> Credit union charters are given by the state, not by the federal government.

<sup>16</sup> Chris Morran, “Pot-Centric Colorado Credit Union Sues



Insurance Corporation, the National Credit Union Administration, and the Office of the Comptroller of the Currency—indicated a willingness—but not a commitment—to use the same guidances in their supervisory examinations.<sup>11</sup>

Then came the 2016 elections. One of the first nominations President-elect Donald Trump made was for the new Attorney General. In Republican Senator Jeff Sessions, President Trump installed a staunch critic of the legalization movement. And although marijuana policy was not the most pressing priority for the new DOJ, eventually Attorney General Sessions announced an about face in his approach to prosecuting federal law as it relates to marijuana. On January 4, 2018, Sessions reinforced the authority of the CSA when he instructed U.S. attorneys “to use previously established prosecutorial principles” regarding federal marijuana enforcement, nullifying the Cole Memorandum.<sup>12</sup>

Some commentators have seen the Sessions announcement as a sudden change in federal policy.<sup>13</sup> Even before this announcement, though, the Cole Memo provided the thinnest of protections for those financial institutions that sought the protec-

tion of state law in providing financial services to marijuana businesses. In practice, the non-binding nature of the promise of non-intervention from federal prosecutors and the unwillingness of federal regulators to commit to a course of action was enough to scare most banks away, the Cole Memo (and its adoption by FinCEN) notwithstanding.<sup>14</sup>

### A MICROCOSM OF THE BANKING PROBLEM

The fragility of the financial regulatory space surrounding marijuana didn’t deter every financial institution. Some hearty entrepreneurs saw the change in state law as an opportunity to bring the federal government kicking and screaming into the era of marijuana legalization. Fourth Corner Credit Union provides the best example of what happens when even motivated financial institutions face the reality of the state-federal mismatch.

Fourth Corner Credit Union was chartered in Colorado with the full support of the state’s governor in late 2014. Colorado established thorough procedures for complying with the Cole Memo, and Fourth Corner in turn followed every rule the state imposed upon it in seeking

its charter.<sup>15</sup> The explicit mission of the credit union was to “service the unique financial needs of the cannabis and hemp industries and their supporters.”<sup>16</sup> In November 2014, Fourth Corner applied for a “master account” from the U.S. Federal Reserve System, as administered by the Federal Reserve Bank of Kansas City (which oversees the payment system in the state of Colorado). A master account allows, among other things, a financial institution to engage in electronic credit and debit transactions with other financial institutions. Without it, a financial institution cannot function.

Fourth Corner spent eight months answering questions from the Kansas City Fed. According to the credit union, master accounts are typically approved within one week. In July 2015, the Kansas City Fed informed Fourth Corner that it had not approved the credit union’s master account—essentially delivering a death sentence to Fourth Corner. As the credit union later stated, this denial turned a full-service financial institution into “nothing more than a vault.”<sup>17</sup>

The Fed based its decision largely on Fourth Corner’s inability to acquire deposit insurance from the National Credit Union Administra-

#### NOTES

Federal Reserve Bank for Denying Account,” *Consumerist*, July 31, 2015.  
<sup>17</sup> The text of Fourth Corner’s complaint is available at <https://consumermediallc.files.wordpress.com/2015/07/fourth-corner.pdf>.  
<sup>18</sup> Nathaniel Popper, “Banking for Pot Industry Hits a Roadblock,” *The New York Times*, July 30, 2015.  
<sup>19</sup> Defendant Federal Reserve Bank of Kansas City’s Motion to Dismiss First Amended Complaint, *Fourth Corner Credit Union v. Federal Reserve Bank of Kansas City*, 2015 WL 13021567 (D.Colo.) (October 21, 2015).

<sup>20</sup> Rules regarding the Fed’s provision of services are available at <https://www.law.cornell.edu/uscode/text/12/248a>.  
<sup>21</sup> Debra Borchart, “Cannabis Credit Union Loses Case Against Fed Reserve Bank,” *Forbes*, January 8, 2016.  
<sup>22</sup> Fourth Corner Credit Union vs. Federal Reserve Bank of Kansas City, 861 F.3d 1052 (10th Cir. 2017).  
<sup>23</sup> Hill, *supra* note 4.  
<sup>24</sup> Dykema Gossett, “Fourth corner Credit Union Obtains Pyrrhic Victory for Marijuana Banking,” *Lexology*, June 30, 2017.  
<sup>25</sup> Gonzalez v. Raich, *supra* note 7.  
<sup>26</sup> The most recent Gallup survey found that 64 percent of

U.S. adults, including a majority of Republicans, support legalization. See Justin McCarthy, “Record-High Support for Legalizing Marijuana in U.S.,” *GALLUP News*, October 25, 2017.  
<sup>27</sup> From the CSA: “The term “controlled substance” means a drug or other substance, or immediate precursor, included in schedule I, II, III, IV, or V of part B of this subchapter. The term does not include distilled spirits, wine, malt beverages, or tobacco, as those terms are defined or used in subtitle E of the Internal Revenue Code of 1986.” Available at <https://www.law.cornell.edu/uscode/text/21/802>.



tion (NCUA). For its part, the NCUA did not believe Fourth Corner would be able to manage the risk of working within a single industry that had no track record and that remained illegal nationally.<sup>18</sup> But the Fed also made clear that the concern wasn't specific to Fourth Corner. The Fed had a problem with marijuana. As the Fed made clear in subsequent litigation, Colorado's legalization of marijuana was the same "as if Colorado enacted a scheme to allow trade in endangered species or trade with North Korea."<sup>19</sup> The credit union, according to the Fed, did not have the right to inject state marijuana money into the federal banking system, given the illegality of cannabis at the federal level.

Fourth Corner filed a lawsuit against the Fed, claiming that the Fed's own rules do not give it discretion in deciding which institutions should be disqualified from master account access, nor do they explicitly allow for decisions to be based on those of other agencies, like the NCUA.<sup>20</sup> A federal district court dismissed the lawsuit. Fourth Corner built its case upon the Cole Memo's guidelines, while the Fed, along with many private financial institutions, argued that those guidelines provided no binding protection from prosecu-

tion. The court agreed with the Kansas City Fed, but admitted that "the situation [is] untenable" and required resolution by Congress.<sup>21</sup>

Fourth Corner quickly appealed the decision. In June 2017, the Tenth Circuit Court of Appeals issued its decision in the case of *Fourth Corner Credit Union v. Federal Reserve Bank of Kansas City*.<sup>22</sup> The court's opinion is dizzying, and illustrates well the rank confusion that the state-federal mismatch sows in this area of law. The three-judge panel could not agree on the disposition of the case. One judge would have sided with the Kansas City Fed (and the lower court) because marijuana distribution is illegal, and a bank that services these entities is breaking the law. Another judge would have dismissed the case on procedural grounds, holding that the credit union could have received its master account if it promised not to service marijuana-related businesses. And the third judge would have overruled the lower court and granted the credit union's request for a master account. The consequence of this kind of division was to settle on the least-common denominator: Fourth Corner could amend its complaint and seek again a master account, subject to a commitment to follow the law.

While Fourth Corner could declare a partial victory, this ruling effectively prohibited it from servicing the only clientele for whom it was originally formed.

The experience of Fourth Corner demonstrates a few key points about the fragility of marijuana banking. First, the Federal Reserve's control over access to its payment systems gives it significant regulatory and supervisory control to which courts will defer.<sup>23</sup> Second, the CSA remains dominant in any debate over sovereignty on the marijuana issue, generally. And third, states will not be able to circumvent federal statutes in order to solve the problem of marijuana banking simply by chartering and endorsing special financial institutions.<sup>24</sup> Even though the master account application was historically *pro forma*, a commitment to abiding by federal law—whatever the state law may allow—is still a requirement.

### **POLICY SOLUTIONS: TWO APPROACHES TO REJECT, ONE TO ACCEPT**

The federal government in all three branches—the President, the Congress, and the courts—will have to decide how to manage the increasing

#### **NOTES**

<sup>28</sup> James Higdon, "Did Jeff Sessions Just Increase the Odds Congress Will Make Marijuana Legal?" *Politico*, January 6, 2018.

<sup>29</sup> Available at <https://www.unodc.org/unodc/en/treaties/single-convention.html>.

<sup>30</sup> Panam Post Staff, "Uruguay Stands Up to UN on Marijuana Legalization," *PanamPost*, June 29, 2015.

<sup>31</sup> Press Release from Senator Jeff Merkley, available at <https://www.merkley.senate.gov/news/press-releases/bipartisan-group-of-senators-introduces-legislation-to-provide-access-to-banking-services-for-legal-cannabis-businesses>.

<sup>32</sup> Hill, *supra* note 4.

<sup>33</sup> Jordan Wathen, "Bank of Pot: Why Some Banks Are Diving In to the Marijuana Business," *The Motley Fool*, January 14, 2018.

<sup>34</sup> Aaron Gregg, "How a Maryland bank is quietly solving the marijuana industry's cash problem," *The Washington Post*, January 2, 2018. ("Each day, dispensaries must email the bank detailed daily financial and inventory logs from Metric, the software system that regulators use to track marijuana from seed to sale.")



conflict between federal enforcement and state sovereignty. The Sessions announcement, unfortunately, increases the tension between the federal and state governments. The United States cannot long remain in the present stalemate because, crucially, the marijuana industry continues to thrive. And an industry like this will demand access to financial services. An entire industry conducting all of its business in cash cannot be fairly taxed or regulated and, historically, has been associated with lawlessness—everything from security concerns, transportation and currency problems, money laundering, and cash hoarding. If the federal government—Congress in particular—ignores this issue, it will soon face a public policy crisis. What, then, to do to resolve this tension? I explore below the spectrum of alternatives.

First, Congress can do nothing. The status quo, in that event, will see a one-way ratchet in a growing demand for marijuana in the states that legalize it, pushing its use further and further into black and gray markets. Although there is ample legal authority for the federal government to insist on its supremacy in this space,<sup>25</sup> this tension will likely foment a political reaction and lead to policy upheaval.

There is much to be said for this strategy. We are not yet at a fevered pitch of instability. Perhaps forcing the federal government to react, or the states to retrench, will be the correct move. A political solution is more likely to follow a crisis made by politicians. And it is not a stretch to characterize any resulting crisis around the legitimacy of state-sanctioned marijuana use as largely a creation of politicians.

At the other extreme, Congress can follow the lead of Colorado and legalize marijuana completely. There is certainly political enthusiasm for that kind of legislation in some corners. Federal legalization would preempt states that choose to criminalize marijuana's use, imposing a single policy on the entire country.

The problem with that opposite extreme is that it removes authority from the states to chart their own course. Colorado currently takes a different view on marijuana use from its neighbor, Utah. Perhaps Utahans are wrong, Coloradans are right. But perhaps we simply don't know enough about the strange new world of legalized marijuana. Better than imposing a single, national solution on a complex policy domain, Congress should allow the states to take different views on this question. Doing so will provide more information for citizens to understand what marijuana use means for the health and welfare of their citizens. We know very little about the consequences of long-term, legal marijuana use in the United States. Enthusiasm for marijuana use may be on the rise in light of that lack of knowledge.<sup>26</sup> Certainly, tobacco use has become increasingly disfavored, even as marijuana has grown in popularity. Thus, allowing states to experiment in their approaches to this delicate issue will ultimately provide the kind of information that should inform the citizenry. Cutting it off with national homogenization is a move too far.

The best approach, then, is a more tailored one that allows states to pursue their own interests in this sensitive area without requiring a national crisis

to spur change. The following proposals reflect that preference for a middle road and present a suite of options for Congress to pursue.

### 1. MARIJUANA LEGALIZATION, FULL STOP

Congress could respect the wishes of the states and treat marijuana as it does other, arguably more harmful drugs like alcohol and tobacco.<sup>27</sup> A move like this would give states the license to control the use of the drug within their own borders as they see fit without fear of a superseding authority. One example of legislation that advocates for this type of approach is the Ending Federal Marijuana Prohibition Act, sponsored by Rep. Thomas Garrett (R-VA). It would remove marijuana from Schedule 1 and eliminate federal penalties for anyone engaged in state-legal marijuana activity.<sup>28</sup> There are fewer hurdles to this approach than there is with re-scheduling marijuana.

Full-press legalization, though, is complicated by the United States' international commitments and raises questions for those states (like Utah) that may prefer a different course. International treaties, such as the UN's Single Convention on Narcotic Drugs (1961),<sup>29</sup> requires the U.S. to enforce international sanctions on marijuana. Some countries appear to have had success recently in walking away from these sanctions—including Uruguay after its national legalization of marijuana—so there is precedent for the U.S. to attempt the same maneuver.<sup>30</sup> And there are easy carve-outs that could be included for those states who wish to cut a different path. Ending prohibitions





in this incremental way could be the viable path for simplifying the state-national tensions that currently plague the system.

## 2. RECLASSIFICATION

Congress has historically left drug scheduling up to the DEA, but it could change a drug’s schedule itself by legislation. By reclassifying marijuana as a Schedule II drug, rather than its current status as a Schedule I drug, Congress would permit broader use and experimentation under the supervision of doctors and pharmacists. Simply re-scheduling marijuana would likely be insufficient and inapplicable, giving the country the worst of all worlds. A rescheduled marijuana would be difficult if not impossible for states to forbid. And to even qualify, researchers would have to prove in a clinical setting that the drug has “medical benefits” that outweigh the costs. Furthermore, Schedule II drugs are still mostly restricted (in that they require a prescription), so it would be far from full legalization. Reclassification, then, could help resolve banks that fund marijuana-related businesses, but only insofar as those business models are aimed at a Schedule-II-type understanding of marijuana, a framework inapplicable to states like Colorado, California, or Washington.

## 3. LEGISLATION THAT SINGLES OUT BANKING

Another approach would leave in place existing federal laws governing marijuana but target banking as a means for allowing marijuana-related businesses to participate

in the financial system. This is an approach favored by Senator Jeff Merkeley (D-OR) and Representative Ed Perlmutter (D-CO) in their Secure and Fair Enforcement (SAFE) Banking Act of 2017. This legislation would favor incumbent banks by ignoring the master account issue discussed above in the Fourth Corner case, but would provide clarity and some incentives for existing financial institutions to service marijuana-related businesses.<sup>31</sup>

There is much that is laudable about this effort, but its exclusion of protections for new entrants, with no capital, would mean that an already concentrated industry would remain entrenched, leaving little space for outside innovation. Ultimately, the picking of winners and losers is best left to the marijuana industry itself. The SAFE Banking Act should therefore be changed to allow for that kind of entrance.

Still, giving a legislative green light to well-established banks might seem like a welcome change from the status quo for marijuana businesses. We have not seen sufficient clarity around banking the marijuana industry to know how existing financial institutions would approach this situation. The compliance costs may overshadow any profits from an industry still in its infancy, should federal financial regulators set too high a bar for anti-money laundering and safety and soundness due diligence requirements.<sup>32</sup> Even so, this kind of approach may well give banks and marijuana-related businesses the space needed to continue, incrementally, the great cannabis experiment already well underway.

## 4. THE REGULATORY APPROACH

Whether Congress proceeds in this incremental fashion or not, states where marijuana is legalized to some extent or another will still need the support of federal financial regulators. Specifically, it remains unclear at the time this Issue Brief goes to press how and whether the financial regulators will react to the Sessions announcement. The financial regulators—the National Credit Union Administration, the Federal Reserve, the Federal Deposit Insurance Corporation, and the Comptroller of the Currency— would have to be willing, as an official policy, to grant access to share or deposit insurance to banking institutions that work with marijuana-related businesses. And the Federal Reserve would have to treat all state-chartered institutions alike, granting master accounts and opening up their payment systems to entities like Fourth Corner, regardless of clientele. Again, as long as the CSA remains intact, this is unlikely to happen, as the precedent set in the Fourth Corner case demonstrates.

## THE LIMITS OF A DIVIDED HOUSE

According to a July 2017 report from FinCEN, as many as 390 banks and credit unions are accepting deposits from marijuana businesses.<sup>33</sup> *The Washington Post* recently profiled the Maryland-based Severn Savings Bank, a community bank offering business accounts to several marijuana dispensaries and growers in the state. In exchange for a large monthly fee and rigorous daily self-



compliance, Severn's accounts allow them to "pay employees through an automatic debit system, buy supplies with a debit card and purchase marijuana through wire transfers."<sup>34</sup> However, they cannot write checks from (or accept them into) their account, nor can they accept credit cards, as those activities require access to federally regulated payment systems. They also cannot apply for small-business loans, which are necessary not only for the further growth of individual companies, but for the marijuana industry as well.

Severn Savings Bank is also exposing itself to some kinds of risk in the face of the changing political

landscape. If I were advising Severn today, I would strongly urge a reexamination of this approach in light of the Sessions announcement that the Cole Memo is no longer in force.

That uncertain world is where we remain. The United States is a house divided on marijuana policy—a reality unlikely to change in the short term. Only Congress can definitively resolve this morass of conflicts. Members of Congress should do so with a steady eye and an incrementalist approach. Cutting off access to finance and banking will push a legally ambiguous set of activities even further into the shadows. And, in the process, it will continue

to deprive cities and states, not to mention the federal government, from more fully reaping the benefit of assessing and collecting tax revenue from economic activity in what has become a booming industry. Offering a halfway guarantee that federal enforcement priorities will be focused elsewhere is inadequate, as the Sessions reversal shows. Either the federal government should undertake the political project necessary to convince the states that they should reverse their legalization efforts, or it should learn to live peaceably with those states by facilitating the legality, safety, and transparency of the full financial system.



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