

Bank On It

Finance News You Can Count On

December 2019

UPCOMING FIRM EVENTS:

12/12/19

**Business Law Training:
What's Around The Corner?
The Top Ten Things We Are
Watching in Employment
Law for 2020**

12:00 p.m. CST

Register at
www.quarles.com/events

Location: Quarles & Brady
offices and via Webinar

Why Quarles & Brady

With experience handling a diverse array of financings, a deep bench of talent, and offices across the country, Quarles & Brady's commercial finance group covers a lot of territory. After decades as a leader in commercial finance, we have established more than 175 relationships with financial institution clients nationwide. They range from national and regional banks that appreciate our broad geographic coverage and sophistication to local institutions that also value our efficiency and practical solutions.



Banking Cannabis

By James I. Kaplan

Banks face challenges in providing services to the fast-growing cannabis industry due to inconsistency between state and federal law. Cannabis is now legal for retail and/or medical sales for about 70% of the country's population under state law, but federal law continues to contain roadblocks for banks wishing to do

business with the cannabis industry. Federal legislation is in the works that would remove barriers and allow banks to confidently serve the cannabis industry. As is often true in this area, the path is hardly smooth and the resolution is not yet clear. We explain below.

The current state of law regarding the sale to and use by individuals of cannabis and cannabis products for recreational and medical purposes is, to put it mildly, inconsistent. More than 70 percent of the population of the United States live in the 34 states where retail and/or medical distribution, possession and use of cannabis is or shortly will be legal. At the same time, cannabis is a Schedule 1 drug for purposes of the Federal Controlled Substances Act, which means that retail and medical use of cannabis remains illegal for Federal law purposes. A complicating factor is that this Federal-State legal conflict has made most banks reluctant to provide cannabis businesses, and sometimes even their service providers or real estate and equipment lessors, with financial services like deposit account services and lending. Every State and Federally-chartered bank has a Federal regulator, mainly because banks all have federal deposit insurance on all bank deposits up to \$250,000, and the presence and eligibility for membership of state banks in the Federal Reserve System, America's Central Bank.

Legislation now being considered by the U.S. Congress would provide clarity, particularly in regard to banking. The SAFE Banking Act (the "SAFE Act") on September 25, 2019, passed out of the House by a lopsided 321-103 vote (Democrats voting yes by 229-1, with Republicans voting 91 yes 102 no and the



House's sole independent, Justin Amash of Michigan voting yes). The bill, HR1595, has significant support in Congress and outside of it, having been endorsed by the American Bankers Association ("ABA"). The SAFE Act would create an explicit safe harbor for banks, permitting them as a matter of Federal law to provide all banking services to both cannabis businesses as well as their service providers and lessors of real estate and equipment in states where cannabis businesses are legal. That would include more than 30 states where cannabis is permitted for medical purposes and about a dozen where it is currently permitted for recreational purposes. Both categories include California, where more than 12 percent of the US population resides.

The SAFE Act also removes the largest specific roadblock in banking law, the concern that serving cannabis businesses violates the Bank Secrecy Act, and other anti-money laundering statutes and regulations. The basis for this is the universal predicate under all AML statutes and regulations dictating that funds received in an illegal transaction are regarded as "tainted" for AML purposes. Thus, the Federal Controlled Substances Act prohibition on cannabis products makes funds received from their sale as an illegal predicate (at least under Federal law) for AML purposes. The SAFE Act abolishes this prohibition by recharacterizing such funds as legal for Federal law purposes if generated in a transaction that is legal for state law purposes. In addition to providing relief from the Federal prohibition for banks, it also explicitly relieves bank officials from personal liability otherwise imposed by Federal anti-money laundering laws.

The SAFE Act would also provide a safe harbor for the provision of all regular banking services, including deposit account services and lending, as well as treasury and cash management and wire transfers to cannabis businesses as bank clients. The SAFE Act falls short as it relates to the use of credit and debit cards as a routine part of the cannabis business, even in states where retail distribution and sales are legal. This issue arises mainly from the fact that the major card companies do not permit the use of the cards for cannabis-related transactions, owing to the Federal-State law conflict in states that have legalized cannabis. The SAFE Act unfortunately does not directly address this issue, although perhaps an amendment dealing with credit and debit cards and card processors could be added as part of the legislative process prior to passage.

"Cannabis is now legal for retail and/or medical sales for about 70% of the country's population under state law, but federal law continues to contain roadblocks for banks wishing to do business with the cannabis industry."

The SAFE Act is the vehicle most likely to pass both Houses of Congress this session, prior to the 2020 election. A separate piece of legislation, co-sponsored by Reps. Earl Blumenauer (D-OR) and David Joyce (R-OH) in the House and Sens. Elizabeth Warren (D-MA) and Corey Gardner (R-CO) in the Senate would go further toward full legalization. The bill called the STATES Act by its sponsors, would make state legalization of cannabis legal as a matter of Federal law, thus eliminating the force of the Federal prohibition entirely in any state that chose this path. The STATES Act would also include the banking safe harbor provisions of the SAFE Act.

The current politics of cannabis banking legislation is somewhat murky. As noted above, almost half of House Republicans voted to approve the bill, along with nearly all Democrats, which advanced it to the US Senate. If the rough party breakdown in the House (Dems for it, GOP basically split) were to hold in the Senate, the bill would become law, because proponents need only a handful of GOP votes in the Senate - four - to pass legislation, absent a filibuster. The GOP position on the issue of cannabis banking is not clear. The Trump Administration has not announced a position on HR1595, but the Justice Department under its first (now departed) Attorney General, Jeff Sessions,



withdrew the Obama Administration's so-called Cole Memorandum, which declined to bring federal legal actions against ordinary cannabis distribution and possession in states that had legalized it. Nonetheless, the DOJ, under Sessions and his successor, William Barr, has not moved to prosecute cannabis under Federal law in states where it is legal, and it is generally felt that cannabis legalization is popular among voters, a key factor since Congress is already entering into election mode for November 2020. A key question for HR 1595 is, assuming it passes the Democratic House, whether Senator McConnell, the Senate Majority Leader, will even call the bill for action. Thus far, few bills passed through the Democratic House have been brought up for Senate action, and McConnell could perhaps avoid political damage by simply ignoring the bills, rather than bringing them to the floor and having to address the issue. Nonetheless, the GOP must defend 3 GOP-held Senate seats in 2020 that are in States that either voted for Hillary Clinton in 2016, or else have legalized retail or medical cannabis, and the GOP losing just those seats (Colorado, Maine, Arizona) alone would give the Democrats a 50-50 tie in the chamber, and would flip the majority if a Democrat was elected President in 2020. Allowing GOP senators in those states to cast a vote in favor of cannabis banking legislation, even if not full legalization, could help their reelection efforts. The ABA reported on September 26, 2019, just after the House vote, that "[Senate] Banking Committee Chairman Mike Crapo (R-Idaho) has signaled a willingness in recent days to advance a cannabis banking bill." This willingness may reflect the GOP Senate leadership's strategy.

In any case, the issue will only force itself further onto the national agenda in coming years, as additional states (like Illinois, which fully legalized cannabis recently) seem likely to legalize retail cannabis in the near future. At some point, it seems quite likely that Federal banking law, one way or another, will accommodate retail cannabis, and if the Congress embraces Federal-State harmonization in the cannabis banking sector, it could lead to further advances in other areas.



James I. Kaplan
Partner
312.715.5028
james.kaplan@quarles.com

You are receiving this communication from us because you are listed in our database as an existing client or professional colleague/friend of our Firm. This communication is not intended as a solicitation or advertisement to the general public. To unsubscribe, click [here](#). We respect your right to privacy. View our [policy](#).

© 2019 Quarles & Brady LLP

This document provides information of a general nature. None of the information contained herein is intended as legal advice or opinion relative to specific matters, facts, situations or issues. Additional facts and information or future developments may affect the subjects addressed in this document. You should consult with a lawyer about your particular circumstances before acting on any of this information because it may not be applicable to you or your situation.

CONFIDENTIALITY NOTICE: This electronic mail transmission and any attachments are confidential and may be privileged. They should be read or retained only by the intended recipient. If you have received this transmission in error, please notify the sender immediately and delete the transmission from your system.

This email was sent by: Quarles & Brady LLP, 411 East Wisconsin Avenue, Suite 2400, Milwaukee, WI 53202-4426 USA (414.277.5000). To see a listing of our offices, [click here](#).



The SAFE Act would also provide a safe harbor for the provision of all regular banking services, including deposit account services and lending, as well as treasury and cash management and wire transfers to cannabis businesses as bank clients.