

Investing in Green
Funding the Marijuana Industry (Part 1)
A talk with David N. Feldman

- The cannabis and cannabis related industry is one of the fastest growing in the U.S. With more states in the U.S. legalizing or decriminalizing marijuana, there is no doubt that investments in the space will continue to grow. Marijuana remains a Schedule I controlled substance under federal law, which poses significant challenges in banking, financing, securities, and tax to cannabis-related businesses. David Feldman, seasoned securities attorney, explains the issues most commonly faced by cannabis related businesses and their service providers as a result of this fed and state laws dichotomy and what he expects on the legislative horizon.
- Federal and state laws dichotomy
 - Though many states have decriminalized cannabis, its cultivation, sale, and use remain a federal crime.
 - Fed law
 - Controlled Substances Act (CSA)¹: marijuana remains a Schedule I drug under the Controlled Substances Act (CSA). In the same class as cocaine, heroin, and LSD.
 - States
 - 33 states have legalized medical marijuana, and 11 have legalized recreational use
 - Most states have passed referendums.
 - Illinois was first state legislature to legalize.²
- Federal enforcement and a slow move toward legalization?
 - Cole Memo³
 - In 2013, then-acting US Deputy Attorney General James Cole issued an enforcement memo (commonly called the “Cole Memo”) to address the tension between the Controlled Substances Act and certain states’ laws.
 - The memo outlined the DOJ’s main enforcement priorities in preventing:
 - Distribution to minors;
 - Revenue from marijuana sales going to gangs and cartels;

¹ DEA website Information on The Controlled Substances Act, including alphabetical listing of Controlled Substances: <https://www.dea.gov/controlled-substances-act>

² Cannabis Regulation and Tax Act, 410 ILCS 705:
<http://www.ilga.gov/legislation/ilcs/ilcs3.asp?ActID=3992&ChapterID=35>

³ DOJ Memorandum: Guidance Regarding Marijuana Enforcement, August 29, 2013.
<https://www.justice.gov/iso/opa/resources/3052013829132756857467.pdf>

- Diversion of marijuana from legal states to other states;
- State-authorized marijuana activity from being used as a cover for other criminal activity;
- Driving under the influence and other adverse public health consequences;
- Growing or possession on federal property.
- It noted that the fed government had generally left up to the states to prosecute individuals for possession of small amounts and that it would continue to look to the states to do so.
- In states that have legalized marijuana in some form, they should implement robust regulatory and enforcement systems to ensure that the federal priorities outlined would not be threatened.
- FinCEN guidance: 2014 DOJ Memo Guidance Regarding Marijuana Related Financial Crimes⁴
 - After the Cole Memo, the DOJ issued guidance on enforcement of financial crimes related to marijuana. It reiterated the 8 enforcement priorities outlined in the 2013 Cole Memo and that marijuana-related financial crimes would be treated as low enforcement priorities so long as those institutions were operating within a robust state regulatory system and were following adequate anti-AML procedures.
- Jeff Sessions rescinds Cole Memo in 2018
 - Then-AG Jeff Sessions rescinded the Cole Memo and its 2014 follow-up, directing prosecutors to “follow the well-established principles that govern all federal prosecutions.”⁵
 - After the rescission, Treasury stated that the principles of the Cole memo still apply as it relates to the FinCen guidance.
- Joyce Amendment
 - Also called the Rohrabacher-Farr and the Rohrabacher-Blumenauer Amendments. First adopted as part of a spending bill in 2014, the amendment was renewed subsequently multiple times. Current iteration is effective through September 2020.⁶⁷

⁴ U.S. Department of Justice, Memorandum on Guidance Regarding Marijuana Related Financial Crimes, February 14, 2014: <https://dfi.wa.gov/documents/banks/dept-of-justice-memo.pdf>

⁵ U.S. Department of Justice, Memorandum on Marijuana Enforcement, January 4, 2018: <https://www.justice.gov/opa/press-release/file/1022196/download>

⁶ H.Amndment : <https://www.congress.gov/amendment/114th-congress/house-amendment/332>

⁷ Kyle Jaeger, “Congress Attaches Marijuana, Hemp And CBD Provisions To Federal Spending Bills.” *Marijuana Moment* December 20, 2019: <https://www.marijuanamoment.net/congress-attaches-marijuana-hemp-and-cbd-provisions-to-federal-spending-bills/>

- Prohibits DOJ from enforcement spending against licensed medical cannabis businesses in states where it's legal.
 - Agricultural Improvement Act (Farm Bill) enacted in 2019
 - Removes hemp and CBD from the definition of marijuana in the CSA. 21 U.S.C. § 802 (16).
 - Allows states to submit a plan to the USDA about hemp and CBD production and distribution in the state.
- Issues arising from fed-state law tension (see more in Part 2)
 - Fundraising
 - Cannabis related businesses have lacked access to traditional sources of capital. Institutional investors were (and still are, to an extent) reluctant to be involved in businesses that touch the plant. Typically, many businesses relied on friends and family and some PE funding.
 - Banking
 - Because cannabis is still a Schedule 1 drug, the financial services industry has generally been averse to taking risks in the space.
 - Under the Bank Secrecy Act (BSA), financial institutions must file suspicious activity reports (SAR) with the FinCEN whenever there are suspected cases of fraud or money laundering.
 - For cannabis businesses, financial institutions must file the SARs at least on a quarterly basis. Cannabis businesses must disclose certain details on their operations not required of other businesses. These requirements increase costs for banks that take on cannabis businesses. Because these costs are usually passed to the customers, cannabis businesses often pay a premium for bank accounts.
 - Cannabis legalization in Canada
 - Canada legalized cannabis in 2018. In the past decade, US cannabis companies went public in Canada, primarily through reverse mergers, trading on its lower exchanges.
 - Some in the industry see cannabis legalization in the U.S as a foregone conclusion. As a result, in recent years, there has been a shift in capital markets to the U.S. Capital markets continued in Part 2.