

**Investing in Green**  
**Funding the Marijuana Industry (Part 2)**  
**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.
- 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.
- Cannabis related businesses challenges:
  - Who is affected?
    - Growers and retailers (touch the plant)
    - Vendors, suppliers, landlords, and other service providers (don't touch the plant) are still affected by the state/fed dichotomy.
  - Banking
    - The financial services industry is reluctant to take on cannabis businesses because of its classification as a Schedule 1 drug. Other statutory barriers include the Bank Secrecy Act (BSA), USA Patriot Act, RICO, and others.
    - Under the BSA, financial institutions must file with the FinCEN suspicious activity reports (SAR) whenever there are suspected cases of fraud or money laundering.
    - There are heightened due diligence requirements for banks servicing cannabis related businesses. These requirements increase risks and costs for banks; that cost is usually passed on to the customers. As a result, cannabis businesses pay a premium for these services.
    - When cannabis businesses cannot or find it too cost-prohibitive to secure banking services, they cannot obtain a line of credit or mortgage or process debit/credit transactions. They must conduct all their transactions in cash, from paying employees, vendors, and landlords, to paying taxes.
  - Fed Tax

- Cash payments
    - The IRS levies a 10% penalty for cash payments.
    - The IRS revised its policy in 2015 to provide relief for certain cannabis businesses. No penalty is assessed if the taxpayer can show it made reasonable efforts to obtain a bank account.<sup>1</sup> Each request is assessed on a case-by-case basis.
  - Section 280E
    - §280E of the Internal Revenue Code prohibits “drug trafficking” businesses from deducting ordinary business expenses. The result is that cannabis businesses operating in legal states may pay well over half their net income in federal taxes.
    - The IRS released Memo 201504011 clarifying the costs that may be allocated to Costs of Goods Sold (COGS).<sup>2</sup>
    - Some cannabis businesses create separate entities for different arms of their business that don’t touch the plant as a workaround. Nevertheless, cannabis businesses still pay higher percentage taxes than businesses in other industries.
- Proposed legislation
  - Secure and Fair Enforcement (SAFE) Banking Act: House Bill to provide a safe harbor for financial institutions servicing cannabis-related businesses in legalized states.<sup>3</sup>
  - Strengthening the Tenth Amendment Through Entrusting States (STATES) Act: Senate Bill to amend the CSA to restrict federal enforcement against individuals and businesses operating in legal states.<sup>4</sup>
- Capital markets
  - Many believe that legalization in the U.S. is a foregone conclusion. Businesses that went public in Canada are now looking at U.S. exchanges. Until fed legalization, however, exchanges must still contend with fed laws.
  - Large exchanges like NASDAQ and NYSE have begun listing U.S. based cannabis related businesses (that don’t touch the plant), like CBD companies, a real estate investment trust, and a vape company.

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<sup>1</sup> IRS Memorandum, “Interim Guidance on the Failure to Deposit Penalty under Section 6656 for Taxpayers Unable to get a Bank Account” (June 9, 2015):

[https://www.irs.gov/pub/foia/ig/spder/SBSE-04-0615-0045\[1\].pdf](https://www.irs.gov/pub/foia/ig/spder/SBSE-04-0615-0045[1].pdf)

<sup>2</sup> IRS Memo 201504011, Release Date 1/23/2015: <https://www.irs.gov/pub/irs-wd/201504011.pdf>

<sup>3</sup> H.R. 1595: Secure and Fair Enforcement Banking Act of 2019: <https://www.govtrack.us/congress/bills/116/hr1595>

<sup>4</sup> S.3032 - STATES Act: <https://www.congress.gov/bill/115th-congress/senate-bill/3032/text>

- Greenlane Holdings, a vape distributor, went public on the NASDAQ in 2019. It was the first U.S. based cannabis company to be listed on the exchange.
- Social justice policies
  - Some jurisdictions are responding to the historical racial discrepancies in drug laws enforcement though policies intended to create more racially inclusive legal regimes.
  - For example, in Oakland, equity applicants for licenses are eligible for workshops and consultations to help them in starting a cannabis business. It also has a quota system, requiring at least half of the 8 max permits issued per year must be issued to an equity applicant.<sup>5</sup>
  - Massachusetts prioritizes license applicants of individuals from historically marginalized groups and also offers various programs to counter the effects of disproportionate drug enforcement.<sup>6</sup> It also does not bar individuals with prior convictions for possession from owning cannabis businesses. Individuals who have been convicted of a felony or distribution of a controlled substance may not own cannabis businesses.

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<sup>5</sup> For more on who qualifies as “equity applicant,” follow link to the City of Oakland, Become an Equity Applicant or Incubator About page: <https://www.oaklandca.gov/topics/become-an-equity-applicant-or-incuabtor>

<sup>6</sup> For more information on Massachusetts cannabis social equity programs, follow link to Massachusetts Cannabis Control Commission Equity Programs page: <https://mass-cannabis-control.com/equityprograms-2/>