



How to Bank a Marijuana Account

A Compliance Guide for Financial Institutions

Adherence Compliance White Paper | September 2016



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Table of Contents

Banking Marijuana	3
Who Banks Marijuana?	3
Application Processing, Screening & Acceptance	5
Account Setup & Reporting	6
Routine Compliance Monitoring	7
Secure Cash Management & Deposit Verification	8
On-going Due Diligence & Compliance Training	9
Marijuana Banking Software?	10
Hope for the Immediate Future?	11

Banking Marijuana

On August 11, 2016, the Drug Enforcement Administration (DEA) denied two petitions to federally reschedule marijuana¹, leaving it as a schedule I controlled substance. This decision leaves the current landscape for banking marijuana businesses unchanged. According to the Associated Press (AP), more than 300 banks and credit unions (institutions) in the United States now handle marijuana money². This is almost a 500% increase from early 2014. There are now more than 25 states with some form of a legal marijuana market, and more marijuana banking accounts are opening every business day.

There are more than 10,000 operational marijuana business licenses in the United States. As some marijuana businesses have multiple licenses operating under one or more

co-owned companies, it is estimated that there are approximately 4,000 multi-licensed marijuana businesses in operation today. Estimates for legal marijuana sales in the United States are expected to exceed \$6 billion in 2016. The sheer size of this budding industry is immense given consumer demand for the product and its derivatives.



Who Banks Marijuana?

National or multi-state (interstate) banks have shied away from banking marijuana due to current federal guidance and deposit insurance requirements. This massive void is filled by local or private banks and credit unions.

To address “Know Your Customer” (KYC) requirements, an institution should implement a process to verify its marijuana account holders. A customer identification program (CIP) establishes the expectation and monitoring of

customer behavior. A risk management program for marijuana accounts should include enhanced due diligence (EDD) to detect and report on possible money laundering. In order to be effective, the bank’s programs must ensure inventory diversion does not occur and that overall compliance, not just financial compliance, is routinely reviewed and assessed. The process can be very complex without an understanding of the various levels and categories of compliance in the marijuana industry.

¹ D.E.A Headquarters News August 11, 2016, DEA Public Affairs

² Kristena Hansen and Gene Johnson, Banking woes easing for some legal pot businesses, AP The Big Story, April 20, 2016

Marijuana Bank Accounts

For banks or credit unions considering entering this space, the concept can be overwhelming. In evaluating the implementation of a marijuana banking program, an institution needs to evaluate multiple of levels of regulatory and financial compliance.

Four (4) Levels of Regulatory Compliance

An operational marijuana license is the privilege to sell, cultivate or manufacture marijuana or marijuana related products. On top of the financial requirements related to AML, BSA, Cole Memo, FinCEN and more, marijuana businesses must also be compliant with the following regulatory levels:

- Federal
- State
- County
- City

Federal, State & Local Agencies

Even though marijuana businesses are not supported or recognized federally, each one must adhere to all federal requirements and related regulatory agencies, such as the IRS, OSHA, EPA, Agriculture, Labor and others.

Each state, city and county where marijuana sales are legal generate regulatory code and statutes to govern and tax production and sales. Some states have implemented more than 400 pages of regulatory code governing legal marijuana operations.



Looking forward, sales (inventory) may be taxed at all four levels and could impact deposits, receipts, chain-of-custody requirements, transport, business records retention requirements and other compliance areas. The regulatory scrutiny in the marijuana industry is on-par with the health care industry.

Marijuana Compliance

The following five process steps should be considered in setting up a successful marijuana banking program:

1. Application processing, screening & acceptance
2. Account setup & reporting
3. Routine compliance monitoring
4. Secure cash management & deposit verification
5. On-going due diligence & compliance training

Application Processing, Screening & Acceptance

Screening a marijuana business for an operational marijuana bank account can be a daunting task. One bank in Colorado has a checklist requiring more than forty (40) documents prior to processing an application for a business account that sells, processes or cultivates marijuana as its primary business.

Along with standard legal agreements, account information and required financial information, banks and credit unions can also require:

- **Ownership and Owner Details** — resumes, operating and licensing agreements, investor lists and associated contract agreements
- **Operational Details** — vendor and payee lists (GL), employee lists, leases, licensing agreements, cash management systems and insurance policies
- **State Documentation** — corporate statements, licenses, state application, articles of organization, certificates or transmittals of good standing and facilities diagrams
- **City and/or County Documentation** — required permits, local regulatory requirements from public safety, fire, licensing and various ordinances
- **Regulatory Compliance Documentation** — standard operating procedures (federal, state and local requirements), training protocols, enforcement and discipline violations and/or citations, proof of compliance or evidence of regulatory inspections or audits
- **Validation or Deposit Documentation** — state-mandated inventory tracking system reports or verification, tax filings, EOM point-of-sale sales summaries along with transactional data

With the amount of detail required, this type of scrutiny during application screening is unprecedented for most businesses and subject to many pitfalls. The marijuana industry continues to be one of the most highly regulated industries in the world.



Account Setup & Reporting

Once a marijuana business has been accepted by the institution and approved for an operational account, banks must file a suspicious activity report (SAR) at account opening. The initiation SAR, termed a “Marijuana Limited” SAR identifies the account and potential risk. Most banks would need to alter current policies related to managing anti-money laundering programs and SARs to address exceptions in their programs.

Another consideration for institutions banking marijuana is currency transaction reports, or CTRs. FinCEN, the Financial Crimes Enforcement Network requires a CTR to be filed for each deposit, withdrawal or other payment or transfer of more than \$10,000. To address this consideration, most banks would need to ensure marijuana businesses are ineligible for currency transaction report exemptions. This would make it a required filing any time a marijuana business exceeds the mandated threshold. Often banks or credit unions will ‘exempt’ a standard business account from this requirement³.

The Cole Memo stipulates that marijuana is still considered a dangerous drug. On the federal level, distribution and sale of marijuana is a serious crime⁴. Top priorities include:

- Preventing the distribution of marijuana to minors;
- Preventing the diversion of marijuana from states where it is legal under state law in some form to other states;

Suspicious Activity Report (SAR)

Who must file?

- BSA requires every US national bank to file a Suspicious Activity Report (SAR) when they detect certain known or suspected violations of federal law or suspicious transactions related to a money laundering activity or a violation of the BSA.

When is a SAR required?

- SAR filing is required for any potential crimes:
 - involving insider abuse regardless of the dollar amount;
 - where there is an identifiable suspect and the transaction involves \$5,000 or more; and
 - where there is no identifiable suspect and the transaction involves \$25,000 or more

When to file?

- SAR should be filed no later than 30 calendar days from the date of the initial detection of facts that may constitute a basis for filing a SAR.
- In cases where no suspect can be identified, the time period for filing a SAR is extended to 60 days

BSA Expectations Regarding Marijuana-Related Businesses — FinCEN-2014-G001

- Preventing state-authorized marijuana activity from being used as a cover or pretext for the trafficking of other illegal drugs or other illegal activity;
- Preventing drugged driving and the exacerbation of other adverse public health consequences associated with marijuana use;

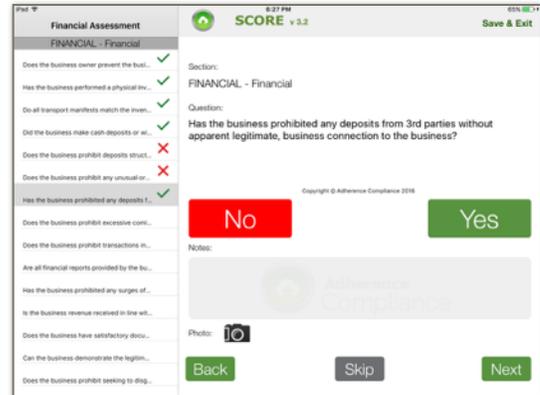
To facilitate reporting requirements, design a marijuana account compliance risk management framework and develop written compliance program documents consistent with the institution’s objectives and regulatory requirements. Focus on scalable, effective, low-cost processes to support readiness reviews, risk and control assessments, remediation and transaction testing. Effective on-boarding and account setup is imperative for institutions to support monitoring and reporting requirements. Preparing for continual regulatory inspections should be a component of any successful program.

³ Kohr, Lauren; ACAMS; Weeding Through The Challenges of Banking the Marijuana Industry, August 2015

⁴James M. Cole, Deputy Attorney General, U.S. Department of Justice, Memorandum for All United States Attorneys: Guidance Regarding Marijuana Enforcement, August 29, 2013

Routine Compliance Monitoring

Routine compliance monitoring involves assessing and evaluating a standard or common set of rules and requirements by operational license location in an automated, repeated fashion. Effective compliance monitoring includes establishing a baseline or scoring mechanism to track and report on overall progress. The leading marijuana compliance software in the market (*Adherence's SCORE App*) lists more than 330 operational requirements (federal, state, city and county) in its compliance assessment for a retail (21+) infused producer license located in Denver Colorado.

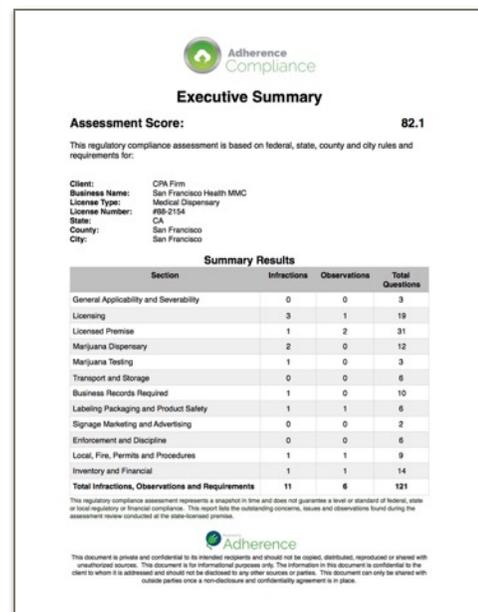


[*Adherence SCORE App*](#)

An infused producer is a licensed manufacturer of ingestible or topical marijuana products. The average compliance score for the retail marijuana infused producer license type in Colorado is 78.4% in 2016, based on more than 10 assessments conducted. On average these licenses fail more than 16 federal, state and/or local compliance requirements. According to Adherence's proprietary marijuana compliance scoring algorithm, an assessment score in the 70s is classified as medium-to-high closure risk:

Adherence Risk Score Classification

- 91-100% Strong Compliance
- 81-90% Low-to-Medium Closure Risk
- 71-80% Medium-to-High Closure Risk
- 61-70% Immediate Closure Risk



Detailed Compliance Report

Monitoring overall regulatory compliance categories at the license premise or location is just as imperative as monitoring financial and transactional aspects of the business.

Secure Cash Management & Deposit Verification

Currently, the top credit card vendors in the U.S. will not allow PIN-debit or credit card transactions by a merchant that is identified as a legal marijuana business. For institutions considering setting up a program, account holders must process cash for all marijuana product sales. The handling of currency creates the need for a secure cash management supply chain, including money processing, transport and verification reporting. Identification and correction of cash management issues should be a top priority for all stakeholders involved. Effective cash management starts with a well-documented plans (e.g. Standard Operating Procedures covering federal, state, city and county requirements) and aligning with a secure, insured vendor for processing solutions, deposits and cash vaulting needs.

Common areas of secure cash management consideration are:

- Cash collection, receipt & deposit policies
- Depositing, verification and reporting
- Cash A/P and A/R processing
- Segregation of duties for cash control

The cost of cash for marijuana businesses can be expected to exceed 5-8% due to related compliance, processing services and fees associated with an all-cash business.



If we postulate a 6% cost of cash for compliant businesses, assuming most operations are in fact compliant, the cost of cash in the marijuana industry could exceed \$300 million based on a lower estimate of \$5 billion in total projected sales for 2016.

Until credit card processors legally support marijuana businesses, reducing the risks associated with cash handling should be a key objective of any marijuana banking program.

On-going Due Diligence & Compliance Training

As banks are unable to absolve their operational risk with marijuana businesses, staying ahead of the compliance curve will be instrumental in managing an effective marijuana banking program. Enhanced due diligence will be of utmost importance.

On-Going Due Diligence

A marijuana banking program can be expected to be routinely reviewed by and commented on by regulatory authorities. On-going due diligence requires continual program evaluation internally to ensure teams are ready for regulators. Once regulators arrive, institutions should plan to educate stakeholders in advance of program review to ensure a common understanding of the industry and requirements is achieved.

Continuing Education

Given the four (4) levels of regulatory oversight (federal, state, city and county), continuing education and compliance training is critical to program success. As this is an emerging and growing market, compliance will continue to be a core competency for successful marijuana businesses and banking programs. With new and ever changing regulations, continual review of regulatory rules and requirements will be necessary to ensure account holders are compliant across multiple categories.



Marijuana Compliance Categories

With any marijuana business, the following areas of compliance must be considered:

Licensing; Licensed Premise;
Enforcement & Discipline; Marijuana
Testing; Labeling, Packaging & Product
Safety; Marketing & Advertising;
Required Business Records;
Transportation & Storage; Inventory &
Financial; Federal Agencies; Local
Agencies & Permitting; Waste and Water;
Applications and Renewals

To reduce the systemic risk of banking marijuana businesses and establishing scalable programs, on-going due diligence and continuing education needs to take place not only within the institution but with the operational account holders as well.

Marijuana Banking Software?

Do banks need to buy expensive marijuana monitoring software that requires costly implementation and management licensing fees? It may be better to spend that time and effort on ensuring the up-front vetting or a proper account verification process is in place, as well as understanding of how the business processes and accounts for inventory. Many marijuana businesses are faced with reconciling multiple, disparate inventory systems. e.g.:

- Physical or on-hand inventory
- Point-of-Sale inventory
- State-mandated inventory tracking system
- Accounting system (e.g. Quickbooks)

Does “*out-of-the-box*” marijuana banking software ensure that up to four (4) disparate systems are accurately reconciled? Does the software ensure that Starting Inventory is compliant, that no diversion or theft has previously occurred and that state-based inventory tracking system reconciliation is occurring on a daily basis? A physical inventory inspection along with comparative analysis of inventory system reconciliation should occur first. Has this particular marijuana business always been compliant with inventory? If inventory has been incorrect in the past, all revenue and taxes reported and filed will be incorrect as well.

Garbage In, Garbage Out

Does the marijuana business employ a revenue and tax accountant? How does it monitor and

manage marijuana product vendor accounts? Is the business properly coding expenses as per IRS 280e requirements and is it appropriately processing tax payments? Without a solid foundation, the overall liability of previous inventory tracking (and omissions) may be too great of a risk for a financial institution absorb.



Some banks are betting “*out-of-the-box*” marijuana banking software can help, however many are learning expensive lessons in managing and maintaining yet another monitoring system. Most banks already have suitable AML/BSA systems in place for monitoring and alarming on various limits or thresholds on active account holders. For marijuana banking accounts, a similar ‘in-house’ method should to be implemented or in place for the constraints related to FinCEN and Cole Memo requirements (e.g. comparative analysis of deposits and variances between similar sized businesses).

The process, not costly software, should be the focus for establishing a successful marijuana banking compliance program.

Hope for the Immediate Future?

With California's upcoming conversion of medical marijuana to a "for-profit" model, as well as the pending retail marijuana (AMUA) vote in November, it's only a matter of time until State Assemblies start proactively addressing the banking and all-cash situation with marijuana. Insiders in the marijuana industry are hoping the election in the fall of 2016 will change the federal course and lead to rescheduling marijuana. Until the federal government acts, hopes for continued marijuana banking will remain at the local or state level.

Adherence to compliance requirements will be key. Standardization or a common framework of marijuana rules and requirements at any level remains highly unlikely. Institutions will need to consider the evolving market when reviewing and implementing a marijuana banking program.

Authors' Note: For more information on cannabis compliance assessments, training or statistics and data related to marijuana compliance, please contact Adherence Compliance at 720-616-3900 or visit www.adherence-corp.com/contact-us/.

About the Author

[Steve Owens](#), MBA, is the CEO and Founder of Adherence Compliance and is considered a thought leader in regulatory and financial marijuana compliance. He has written extensively in the areas of operational compliance and has more than four (4) years of marijuana regulatory and financial compliance expertise.



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About Adherence Compliance

Adherence was the first company to develop a cloud-based, automated, legally-reviewed marijuana compliance software and quantitative risk score for the marijuana industry by operational license type.

Adherence offers cannabis compliance training, standard operating procedures and initiation of compliance monitoring programs for banks, insurance providers, regulatory agencies and other cannabis or marijuana stakeholders.

The [Adherence SCORE App](#) has conducted more than 400 marijuana compliance assessments in the United States and collected more than 190,000 data points. Adherence has the following marijuana or marijuana compliance assessment types available:

- Medical Marijuana Dispensary
- Medical Marijuana Cultivation Facility
- Medical Marijuana Infused Producer
- Retail Marijuana Store
- Retail Marijuana Cultivation Facility
- Retail Marijuana Infused Producer
- Banking Risk Assessment
- Insurance Underwriting Inspection
- Financial Risk Assessment
- Lessor/Landlord Inspection