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BANKING AND CANNABIS WEBINAR

The following pages are the introductory comments for Banking & Cannabis: Lending, the Next Frontier from BMD Banking and Cannabis Partner Stephen Lenn.

A. Introduction

1. Welcome attendees to this webinar focused on bank lending to the cannabis industry and a distinguished group of panelists drawn from each constituency: bank and cannabis regulators, bankers, and cannabis industry titans.

2. Later in this introduction I am going to explain some of the other the rationales for choosing this topic, but the response reflects that the choice was timely and a good one. At the same time, we are both pleased and flattered and disappointed that it was necessary to close registration last week when we hit our maximum capacity of 500 registrants. Eyeballing the list, it appears that we have about 350-400 bankers, representing between 200-250 geographically dispersed financial institutions. Registrants include at least a dozen of the 56 largest banks in the U.S., including 2 of the top 10 and a number whose assets are measured in the tens of billions

3. After a few more preliminaries and introducing our Panelists and Sponsors, I will kick off the webinar with some introductory remarks, following which Tanner Daniel, the American Bankers Association VP of Congressional Relations will offer a keynote on the status and prospects for the SAFE Act and other relevant pending federal legislation. We will then turn to our panelists for their views and a lively discussion. If there's time, we will respond to questions from the audience. If not, we will attempt to do so directly afterward.

4. Without going into detail, the cannabis industry is likely the fastest growing in the US. Revenues in 2021 are projected to be increase to about $25 billion, representing a 25% increase over 2020. With states like NY legalizing rec, and additional states coming on stream, continuing dramatic growth seems assured

   As the registration materials reflect, a motivating factor for undertaking this webinar is the huge opportunity bank lending represents for both industries: banks need good loans, and cannabis companies, which are become increasingly bankable, need lower borrowing costs. While rates on some recent non-bank loans have dipped below 10%, most loans outstanding and being made are priced in the mid-teens. According to Viridian Capital Advisors September 3, 2021, Cannabis Deal Tracker report, thus far this year debt transactions have totaled more than $3 billion. On top of this, there are tens of billions of outstanding cannabis industry debt, some of which, likely substantial, could be refinance candidates.

5. Disclaimers and Caveats, and what would a lawyer do without them:

a. First let me underscore that I do not identify as a cannabis lawyer; but rather as a corporate merger and acquisition, corporate finance and banking lawyer who was a top 100 bank general counsel and high-level bank regulatory lawyer with large national and regional firms who happens to have been involved in about $2 billion of cannabis M&A and debt finance transactions. Most of the representations have been large public and private acquirors and institutional or quasi-institutional lenders but have also included borrowers and acquirees. As a result, I speak both banker and weed.

b. Second, as they may also indicate, our panelists are here in their personal capacities and the views expressed here are not necessarily the official positions of their organizations.

c. Third, everything we talk about is predicated on the absence of significant adverse medical, scientific, or social developments, none of which have yet surfaced. By way of comment, I am not aware of a single viable repeal effort

6. Sponsors, critical support staff and Panelists

a. Before introducing our panelists, thanks to Paul Hickman of the Arizona Bankers Association, Jen Waller of the Colorado Bankers Association, Howard Headlee of the Utah Bankers Association, and Mike Adelman, of the Ohio Bankers League, for their co-sponsorship and assistance in recruiting the panel and structuring the program, and the American Bankers Association for making Tanner Daniel, its VP for Congressional Relations, available to give a keynote address updating us on the status and prospects for pending federal legislation.

b. Also, special thanks to Jennifer Shankleton, BMD's marketing director, and Madeline Lange, our marketing specialist, who did all the hard work behind the scenes that made this possible.

c. Panelists

i. Our bank panelists are Ashley Burt, CEO of Colorado's Gunnison Bank and Trust Company, and Frank Smith, VP of Operations of Phoenix based Republic Bank. Ashley has been serving the cannabis industry for many years and as CEO, the buck stops with him when it comes to business development, compliance, and regulatory relationships. Frank has now been involved in the initiation of cannabis business at two banks, in each case working with his board and regulators to develop, implement and oversee policies and procedures and continuing regulatory interface

ii. Representing the perspective of bank regulators, we are fortunate to have Kevin Allard, Ohio Superintendent of Banks, and Shane Foster, Arizona Deputy Superintendent of Banks. Ideally, we would have liked federal regulators to participate on the panel, but we were unable to persuade any to do

so, and it's not for lack of trying. Both Kevin and Shane regulate and examine banks providing services to the cannabis industry, often working with one or more federal bank regulators, so they can address the subject as they see it in real time, if and how the pending federal legislation might affect their approach and, perhaps, help us gain insights with respect to how the feds approach this.

iii. The cannabis industry panelists are two Arizona homegrown industry superstars, each with multistate chops. Steve White is a founder and CEO of Harvest Health & Recreation, one of the largest public cannabis companies, which recently announced a multi-billion merger. Mark Steinmetz has been awarded licenses and overseen profitable operations in multiple states, some of which have been folded into one of the larger private multistate companies.

Both Steve and Mark are past presidents of the AZ Dispensary Owners Association.

iv. Finally, to address the implications for bank lending of cannabis regulation, we have Greg McIlvaine, who was appointed Senior Policy Advisor to the Ohio Department of Commerce to oversee its licensing and regulation of cannabis activities other than retail, caregivers, and patients, including cultivation and processing, and Will Humble, who was Director of the Arizona Department of Health Services as its cannabis policies were being developed.

7. First, let's deal with the elephant in the room. Cannabis is still against federal law, and no one can provide assurance that there are no risks, however theoretical they might be. Anyone considering participating in cannabis related activities must make their own risk assessment. We can say, however, that these risks are mitigated by a number of factors:

a. Federal enforcement policy has been largely hands off at both the DOJ and bank regulatory agencies.

i. While Attorney General Jeff Sessions officially rescinded the Cole Memorandum issued in 2013 by Deputy Attorney James Cole, which provided guidance to US Attorneys establishing a low enforcement priority for state legal activities that didn't involve one of the "deadly sins" identified in the Memorandum, there has been no perceptible change in that policy. Prosecutions and seizures of assets of compliant cannabis businesses are almost non-existent.

ii. Since 2014 there has been a continuing amendment to the federal budget which precludes the DOJ from using any appropriated funds to prosecute state compliant medical marijuana activities.

iii. There is formal federal recognition that financial services can be provided without violating the Bank Secrecy Act or anti money laundering laws which

has been used as a road map by those banks that are doing so and their regulators. In 2014, the Financial Crimes Enforcement Network ("FinCEN"), the division of the US Treasury Department charged with enforcing the anti-money laundering laws, issued guidance which stated its purpose as clarifying *"how financial institutions can provide services to marijuana-related businesses consistent with their BSA obligations…."* It further articulated that the Guidance was intended to *"enhance the availability of services for, and the financial transparency of, marijuana related businesses."* The Guidance and an article summarizing it, *The Inevitable Inexorable Intersection; Banking and Cannabis*, are available through the program materials link.

iv. Substantiation of the federal regulators' hands off approach can be found in a June 2020 speech by FDIC Chair, Jelena McWilliams, in which she stated:

> We know we have banks that are banking marijuana businesses, and you know, we can't bless them and say "go ahead and do it." But to the extent you're doing it because it's legal in your state, follow FinCEN guidance.

v. Some comfort, as well as a competitive incentive for the banks, can be drawn from the Credit Union sector. As many of you know, Credit Unions are active in serving the cannabis business, and their regulators have been both more progressive and aggressive. Notwithstanding whatever internecine rivalry exists, their efforts are complementary, and worth noting. In a speech on September 9, NCUA Board member Rodney Hood, its former Chair, expressed his concern "that the legal and regulatory infrastructure surrounding the cannabis industry is not evolving quickly enough."

While not endorsing any specific piece of legislation, he stated: "let me be clear about where I stand: it is time for federal action to clarify and harmonize the laws and regulations surrounding the state-legal cannabis industry and marijuana-related businesses (MRB), so that this industry can take part in the legitimate financial services industry.

He noted as a basic reality that "as a rule, regulators really don't like to get out too far ahead of the policy process. We always seek to respect the existing statutes, and to defer to Congress as the policy-making arm of the government.

However, there are times when a regulator in the executive branch needs to step forward to provide leadership, or at least nudge things along, when the policy process isn't working as it should. I believe that's the case today with marijuana and the financial services industry.

The bottom line is this: Legalization is going to happen, and the abdication of responsibility to address these issues in Washington is

simply ludicrous. This is precisely the time we need leadership at the federal level to steer this ship in the right direction.

b. The passage of the SAFE Act by the House, which doesn't legalize cannabis, but provides safe harbors for financial institutions, or one of the other pieces of pending federal legislation: The Cannabis Administration and Opportunity Act and the MORE Act each of which, among other things, would remove cannabis from the schedule of illegal drugs, and HR 365, which would move marijuana from Schedule I to Schedule III. The voters in more than 70% of the states have spoken, a percentage which mirrors public opinion, and I suspect even our most recalcitrant congressmen and senators will eventually do the math.

c. The pain points of the current circumstances will also be drivers. Examples include:

   i. the IRS and state and local tax authorities, many of whom are pushing for legislation addressing the banking issue because they are not set up for cash payments

   ii. as noted in a recent CNBC interview, Boris Jordan, CEO of Curaleaf, one of the largest public cannabis companies, focused on the impact of these circumstances on the more than 300,000 (and rapidly growing) cannabis industry employees

   iii. the impact on the banking relationships of the growing number of MRBs

8. The catalyst for the webinar was an article I wrote in February focusing on bank lending to the cannabis industry, a copy of which is available through the link provided to registrants for program materials. That article was the most recent in a series of 50,000-foot articles reporting on and anticipating the evolution of the cannabis industry. All included references to the banking situation and reflect two recurrent themes: "Out of the shadows and into the mainstream," and Woodward and Bernstein's mantra in *All the President's Men*, "Follow the money." I believe both the sponsorships and registration for this webinar are illustrative of the efficacy of those themes. Query- 5 years ago would our sponsors have been receptive to a webinar like this and would we have attracted as many registrants?

9. The catalysts for the article were;

   a. the passage by the House of SAFE Act by substantial, bi-partisan majority, and the introduction of the other bills that would change the landscape

   b. the magnitude of the opportunity presented by convergence of interests between the banking and cannabis industries, which present each with potential financial benefits measured in the tens and perhaps hundreds of billions.

c. the likelihood that processes and protocols re deposit activities were probably largely in place and would not be materially changed by any new legislation, and that progress on access to payment systems was more remote, making lending next on the horizon

d. my view that, while the passage of the SAFE Act, or any of the other pending federal legislation, would greatly accelerate bank lending, it seems anywhere between likely and certain that those activities will continue to increase whether or not any of the proposed legislation passes

10. While the exact number of banks currently serving the cannabis industry is hard to pin down, it is certainly a very, very small percentage of all banks, mostly community banks providing deposit accounts. Reports that the number of insured institutions serving the cannabis industry is approaching 800 are based on Suspicious Activity Report filings and are probably significantly overstated.

    Spoiler alert to banks that have thus far not determined to take the plunge, including the larger banks, this show is coming to a theater near you. I believe Ashley has a perspective on the bigger banks approach. The message to those banks is you can run but you can't hide.

    First, as the cannabis industry continues its rapid growth, an increasing number of good existing or prospective bank customers will become engaged in financial and business relationships with cannabis businesses, almost certainly triggering cannabis banking issues. This trend is described in the Inevitable Intersection article that is available through the program materials link.

    Second, some of the largest companies in the world are itching to find enough wiggle room to acquire cannabis assets. When, not if, but when, they do, are banks going to toss out companies like Altria and Constellation Brands? In this connection, I am intrigued by the language in Section 3 of the SAFE Act as passed by the House. It provides

    "For purposes of … (this act)**, and all other provisions of Federal law,** the proceeds from a transaction involving activities of a cannabis related legitimate business or service provider shall not be considers proceeds from an unlawful activity solely because (it involves certain activities legitimate cannabis related activities specified in the Act) …."

    As an aside, smaller banks shouldn't be scared off by the prospect of larger institutions entering the fray. First, those banks have survived, and indeed thrived, in the face of industry consolidation, and they will likely also do so in serving the cannabis industry. Second, there is an analog to my experience in my practice. I staked out a position relatively early on. When I started in the practice in 2015 there were virtually no larger law firms that would. Now, most major firms have entered the practice, some aggressively (follow the money), and even though I am not

practicing at one of those firms, as a by-product of staking out a position early, and positioning myself to compete as the market evolved, I still have a ticket to the dance and a seat at the table. So can banks that get in early and do it well.

11. Banks that are serving the cannabis industry have developed protocols and practices based on the FinCEN Guidance (which has not amended since issued in 2014). In applying the Guidance, it is important to note

    a. The Guidance articulates its

        i. objective of clarifying *"how financial institutions **can** provide services to marijuana-related businesses consistent with their BSA obligations…."*

        ii. intent to *"enhance the availability of services for, and the financial transparency of, marijuana related businesses."*

    b. Unfortunately, the Guidance did not define the term "marijuana related business ("MRB"), although a footnote suggests that a relationship as remote as being a landlord could result classification as an MRB. The SBA has tried its hand, but its efforts have shed little light. The SBA's attempt is also noted in the Inevitable Intersection article.

    c. The Guidance adopts as underlying precepts the priorities established pursuant to the Cole Memorandum, enumerating what I call the deadly sins:

        - Preventing distribution to minors;
        - Preventing revenue from the sale of marijuana from going to criminal enterprises;
        - Preventing the diversion of marijuana to states in which it is not legal;
        - Preventing state authorized marijuana activities from being used as a cover for other; drug trafficking or illegal activity;
        - Preventing the use of firearms in the cultivation and distribution of marijuana;
        - Preventing drugged driving and other adverse health consequences.

12. In essence, the Guidance calls for know your customer due diligence on steroids but adopts a risk-based approach which has been applied by the banks serving the cannabis industry, and banking regulators, to require more due diligence the closer a customer is to the plant and the greater the potential of facilitating one or more of the deadly sins. While I'll let our bank and bank regulatory panelists go into detail if they wish, virtually all policies segment that risk into tiers, tier one requiring the highest level, and often limit the relationships to non-plant touching customers in lower tiers.

13. A key question for banks and their regulators will be whether lending implicates different bank regulatory considerations beyond the normal financial and credit analyses of any borrower. The protocols and processes established for deposit

relationships may require at least tweaking, perhaps more, of existing protocols – holding a customer's money is one thing, lending that money is another.

14. This brings us to the rationale for adding cannabis regulators to our panel. From the perspective of a corporate finance and banking lawyer, when I first began my work in the cannabis industry in 2015, I was struck by the extent to which cannabis laws and regulations did not reflect a recognition that the industry required lots of capital and that capital has a cost. As a result, documenting capital formation and debt financing frequently requires complicated workarounds, which could be an impediment to conventional bank financing.

15. Cannabis regulation is also quite new in most states, and laws, regulations and regulators have focused primarily on licensing and compliance. As the industry evolves, so to must the regulatory frameworks. Banking regulation has evolved to the point that bank regulators, in addition to their compliance responsibilities, recognize that their regulatory objectives are also served when banks are profitable and financially solid. As the bankers know, after federal exams each bank is given a composite rating called a CAMELS rating—capital, assets, management, earnings, liquidity and sensitivity—which in some sense controls what banks may do. Hopefully, as the cannabis industry and its regulation matures, cannabis regulators will expand their horizons to reflect a recognition that compliance is enhanced by financial stability and success. The cooperation of cannabis regulators to facilitate access to banking services, including lower borrowing costs, will likewise enhance both their ability to oversee the industry and the ability, capacity, and incentives of their regulated businesses to comply.

16. Examples of potential areas cooperation could include both substantive modifications, such as pathways to security interests in licenses, and some which, at least on their face, are more mechanical, such as the issuance directly to lenders, perhaps at the request of license holders, of "good standing certificates" confirming that the underlying licenses were validly issued and are in good standing.

    In our prep session, I asked the bankers what cannabis regulatory changes they'd like to see. Ashley gave a flippant "Nothing." Since I suspect that his motivation was not entirely altruistic, I'm giving him and the bank regulators a heads up; I'm going to restate the question: What cannabis regulatory changes would facilitate bank lending?

17. Lastly, and gratuitously, an aside to the cannabis industry regarding interstate operations that are currently prohibited. The banking industry may provide some insight. When I first entered the banking world in 1975 interstate banking was prohibited. Then, during the 1980s, the industry saw the establishment of interstate compacts that provided reciprocity—you can buy a bank in my state if banks from my state can buy banks in yours. Ultimately, in 1994, interstate banking was approved. Not sayin, just sayin.

Thanks for your attention and now before engaging the other panelists, let’s hear from Tanner on the federal legislation.

BANKING AND CANNABIS: BANK LENDING, THE NEXT FRONTIER

LISTEN. SOLVE. EMPOWER.

By Stephen A. Lenn, Russell T. Rendall and James B. Young of Brennan, Manna & Diamond with Teddy Kirsch of L&S Business Law

A fortuitous combination of developments and circumstances present the banking and cannabis industries a large opportunity to enhance each of their respective bottom lines: conventional bank lending, payment processing, treasury management and other services, and bank administered SBA and revenue bond financing to cannabis businesses.

Loan numbers are difficult to come by, but knowledgeable sources estimate that borrowing for "plant touching" cannabis businesses (e.g., growers, processors, retailers, testing labs and delivery services) was at least in the low to mid hundreds of millions last year, numbers that appear certain to increase dramatically. Whatever the number, it's a significant, growing, untapped line of new business for Banks (all federally insured depository institutions, including credit unions). Even the few Banks that take deposits don't currently lend.

The timing for this surge in demand couldn't be better, as cannabis businesses across the spectrum are achieving operating results that make them increasingly attractive customers for Banks.

Also, the Banks that make the loans will largely own rights of first refusal on the earning power on multiple billions of low/no/negative cost deposits, not to mention tens of millions per year in fees for services ranging from payment processing to the spectrum of treasury management; combined with the likely future prospect of an international component, increasing the attractiveness of cannabis relationships to even the largest Banks. In addition to those compelling bottom-line incentives, the offset rights against deposits would provide important additional loan security, perhaps sufficient to tip the balance as credit judgements are made.

- State legal US cannabis industry revenues in 2020 are estimated at more than $15 billion (some estimates as high as $20 billion) and are expected to continue to grow at 30–40% annually. With concomitant increases in the cannabis industry's needs and appetite for funding, the demand for credit could match this growth rate for the foreseeable future.

- Not only is the future promising, but there is a substantial immediate opportunity. The cannabis industry currently has billions outstanding in high-rate, hard money loans. The refinancing of even a portion of these could offer Banks tens of millions in income at the same time adding tens of millions to cannabis business bottom lines.

- Parallel growth can be expected in ancillary, non-plant touching businesses that may fall under the "marijuana related business" (MRB) definition which triggers enhanced due diligence requirements for Banks.

Despite what appears to be a widespread misperception that it is illegal for Banks to accept cannabis business customers, some banks and credit unions are doing business with the cannabis industry, although there is a lack of clarity about exactly how many. But those that have been doing so for some time, all with the knowledge and under the supervision of their federal and state Bank Regulators, who have wisely and prudently faced the fact that the cannabis industry is here and unlikely to disappear.

To mitigate the risk of running afoul of a myriad of federal financial crimes laws, Banks doing business with the cannabis industry, and their Bank Regulators, draw on guidance issued in 2014 by the Financial Crimes Enforcement Network ("FinCEN"), a bureau of US Department of Treasury.

Despite discomfort with the federal illegality, as Banks tiptoe into the cannabis industry, Bank Regulators are apparently going to school—building on existing guidance and developing policies, procedures, and protocols in connection with cannabis businesses and other MRBs. Although they may have to be adapted to address issues unique to lending, these will be the foundation for regulation whenever new legislation emerges.

Limited federal guidance and oversight to date has been focused on Banks providing deposit services, so although a scaffolding is in place, it will require thoughtful adaptation to address issues unique to lending. Pending federal legislation, the Secure and Fair Enforcement Act (the "SAFE Act") and the Marijuana Opportunity Reinvestment Act (the "MORE Act"), which passed the House last year, appear to have improved prospects in the Senate this year. These would provide expanded safe harbor protections for Banks working with cannabis businesses and re- or de-scheduling marijuana under federal criminal law that could eliminate uncertainties such as the cannabis industry's issues under Section 280E of the Internal Revenue Code and the current lack of access to the US Bankruptcy Courts.

Although there is still important work to be done, for practical purposes, the anticipated federal legislation is largely and effectively in the rearview mirror. The constituents of 70% of states have spoken, and this issue has become demonstrably and increasingly bipartisan.

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Federal legislation will not, however, affect state law limits or outright prohibitions on Banks' ability to secure readily and expeditiously enforceable collateral interests in cannabis licenses. Based on our experience in several hundred million of cannabis debt transactions—representing institutional and high net worth lenders, underwriters, third party beneficiaries and borrowers—collateral security interests have been among the toughest issues largely due to that inhibition.

Possible solutions include pre-approved receivership regimes to enable lenders to quickly get control in the event of a default, thereby mitigating further asset deterioration. Templates may be drawn from the manner in which security interests in liquor and FCC licenses are dealt with.

Unless cannabis licensing becomes federal and preempts state regimes, which is not currently on the active radar, the anticipated federal legislation cannot remediate this challenge. Doing so will require a collaborative effort by the two industries to effect necessary changes at the state level, the fruits of which benefit both.

SIDEBAR; SPOILER ALERT

Please see the following link to a blog discussing the potential that the SAFE and MORE Acts will precipitate a new wave of investment or acquisition activity by non-cannabis companies that previously shunned the cannabis industry due to the unknown implications of owning businesses whose activities are illegal under federal law.

https://www.bmdllc.com/resources/blog/will-federal-legislation-open-cannabis-acquisition-floodgate/

Executive Summary

To put the size, scope, and momentum of the opportunity in perspective, 35 states and DC have legalized marijuana, including recreational or "adult-use" in 15 of those states. That means approximately 225 million, or 70% of Americans, currently have access to state legal medical marijuana, and approximately 111 million, or more than a third, of the US population to recreational. Coincidently, or perhaps not, these percentages closely track public opinion polls. A November 2020 Gallup Poll indicates the most recent approval rate at 68%, an all-time high.

Given the pace of decriminalization and legalization, and organized, well-funded campaigns underway, it seems inevitable that most holdout states will join the list over the next several years. Additionally, almost all states with medical have, or soon will have, active movements to decriminalize or legalize recreational. New York and Florida, and perhaps Ohio, with total populations of almost 53 million, seem poised to do so in the next year or two.

Current state laws either preclude encumbrances against licenses held by marijuana businesses, subject lenders to approvals under transfer of control regulations and processes, or are unhelpfully silent.

Banks, unlike private lenders, are subject to regulation and examination, and are held to an overarching requirement of safety and soundness. In order to assure that Banks and Bank Regulators take license collateral fully into account in evaluating loans to cannabis businesses, Banks need a degree of collateral certainty by way of timely and effective control of underlying assets, so that they can protect against further dissipation in value of the underlying assets and business. This will be difficult to achieve if they must go through some process of uncertain time or success to gain asset control from the defaulting borrower.

Possible solutions

1. Either a blanket carve-out, or an efficient, rational one-time preapproval process, for federally insured Banks lending to cannabis businesses, with some or all of the following characteristics: (i) defined capital or bonding requirements, combined with (ii) limited and reasonable time frames for dispositions upon default to buyers that pass regulatory muster.
2. Using as a template existing processes already designed for comparable licensed businesses, such as liquor and broadcast licenses, which would provide time-tested and predictable protocols.
3. Creating processes for timely and effective execution of security interests in the cannabis industry, which could take several different paths or chart new territory:

(i) a list of preapproved receivers that could be immediately interposed and operate under existing state receivership laws, which is the most prevalent and familiar process currently used by lenders as an alternative to the US Bankruptcy Courts, but perhaps lacking sufficient certainty as to timing and result to meet the likely higher standards of safety and soundness, or

(ii) a regulatory receivership process administered by state cannabis regulators, which would require more state resources and legislative or regulatory action, but perhaps result in a speedier process that is more attuned to the unique aspects of the cannabis industry.

Comments regarding alternatives are welcome and encouraged at cannabislaw@bmdllc.com.

Analysis

Momentum driving the SAFE and MORE Acts (or some variation) toward enactment, will further legitimize and move the cannabis industry another significant step out of the shadows and into the mainstream. This, together with rising revenue, profitability, and cash flow in the cannabis industry, will almost certainly provide a springboard:

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For Banks, this will open an entirely new lending market. A market that is already large and rapidly growing, and increasingly populated by strong, stable and profitable businesses – in other words, highly desirable customers; and, at least for some period of time, lending to this market will offer the Banks pricing at the premium end of their conventional commercial lending rates while still saving borrowers between 3% or 4% at the low end, and significantly more at the high end.

For cannabis businesses, particularly those that become more desirable customers for Banks as they develop a solid financial platform and profitability, this offers a new financing option that can dramatically reduce interest costs, enhance earnings, and offer an attractive borrowing alternative to expensive equity to fund growth.

Although there is still important work to be done, for practical purposes the anticipated federal legislation is largely and effectively in the rearview mirror. Whatever shortcomings our Senators and Representatives may have, most eventually tend to be pretty good at electoral math. The constituents of 70% of the Senators and Representatives have spoken, with the voters having clearly expressed their views.

Moreover, this issue has become demonstrably bipartisan, with any red, blue, purple or puce state divides rapidly disappearing, as traditionally conservative states increasingly get on board with legalization (e.g., Arizona, Oklahoma, Louisiana, Mississippi, Arkansas, North and South Dakota, Montana) with more almost certain to follow.

The Current Banking Environment

Despite what appears to be a widespread misperception that it is illegal for Banks to accept cannabis business customers, there are hundreds of banking institutions that are and have been doing so for some time, all with the knowledge and under the supervision of their federal and state Bank Regulators.

In a Marijuana Banking Update as of June 30, 2020, FinCEN, the mission of which is to safeguard the financial system from illicit use and combat money laundering and promote national security, reported that 510 banks and 185 credit unions were doing business with the cannabis industry. Cannabis businesses seeking depository relationships will find that number hard to believe based on the difficulty they have in finding willing Banks. Most states have only a relative handful (e.g., Arizona only has four and Ohio only has only a few). That disconnect appears to exist because FinCEN's numbers are derived based on institutions filing Suspicious Activity Reports (SARs) related to marijuana, and not all institutions that file marijuana related SARs take deposit accounts for marijuana businesses.

To mitigate the risk of running afoul of a myriad of federal financial crimes laws, Banks doing business with the cannabis industry, and their Bank Regulators, draw on guidance issued by FinCEN in 2014 (the "FinCEN Guidance"). In fact, reflecting the acceptance of the FinCEN Guidance as the current lodestar, the SAFE Act would call for FinCEN to issue new guidance for the submission of SARs for transactions with state legal cannabis-related businesses in order to avoid significantly inhibiting the provision of financial services to such businesses.

Despite discomfort with the federal illegality, Bank Regulators have wisely and prudently faced the fact that the cannabis industry is here and unlikely to disappear.

FDIC Chairwoman Jelena McWilliams neatly explained why things are still so complicated[1]:

> It has been one of the perhaps—I would say—more challenging issues that I have encountered at the FDIC. And here's why: At a federal level it is still an illegal substance. And at many state levels, it's now legal, and it's legal to frankly bank it at a state level. And so banks find themselves caught between the federal regulatory regime and the state...so what I've been telling banks: There's so much uncertainty in this space that as a federal regulator, I still have to say, it's illegal to bank marijuana.
>
> But to the extent that you're doing it because it's legal in your state, please follow FinCEN guidance.
>
> We know we have banks that are banking marijuana businesses, and you know, we can't bless them and say "go ahead and do it." But to the extent you're doing it because it's legal in your state, follow FinCEN guidance.

Credit Unions and their regulators have taken a somewhat more progressive approach, demonstrated when Rodney Hood, Chairman of the National Credit Union Administration stated

> that credit unions will not be sanctioned for conducting business with marijuana-related firms. He said that it is a business decision for credit unions and that the NCUA would not micromanage financial institutions the agency supervises. He said that credit unions still have to follow Financial Crimes Enforcement Network rules, which requires credit unions and other financial institutions to file Suspicious Activity Reports.

The FinCEN Guidance sought to clarify "how financial institutions can provide services to marijuana-related businesses consistent with their BSA obligations" with the goal of enhancing "the availability of services for, and the financial transparency of, marijuana related businesses."

1 Crains Detroit Business, June 3, 2020
2 The Credit Union Times, August 5, 2019

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The FinCEN Guidance specifically incorporated content from a memorandum issued by the U.S. Department of Justice in 2013 by Deputy Attorney General James Cole (the "Cole Memo"), that essentially deprioritized prosecution of marijuana-related federal offenses so long as the actors were complying with state law. Among other things, the Cole Memo identified continuing priorities such as preventing distribution to minors, money flowing to criminal enterprises, and diversion of marijuana to states where it was still illegal.

Drawing on the Cole Memo, FinCEN's Guidance provides a laundry list of red flags and dictates that financial institutions must tailor their relationships with MRBs to reflect its priorities. Unfortunately, the FinCEN Guidance does not define MRB, other than indicating that it includes more than just plant touching enterprises, for example covering landlords with MRB tenants. This expansive reading is supported by a non-binding Small Business Administration Policy Notice from April 2018, which offered the following definitions:

> "Direct Marijuana Business" – a business that grows, produces, processes, distributes, or sells marijuana or marijuana products, edibles, or derivatives, regardless of the amount of such activity.

> "Indirect Marijuana Business" – a business that derived any of its gross revenue for the previous year (or, if a start-up, projects to derive any of its gross revenue for the next year) from sales to Direct Marijuana Businesses of products or services that could reasonably be determined to support the use, growth, enhancement or other development of marijuana. Examples include businesses that provide testing services, or sell grow lights or hydroponic equipment, to one or more Direct Marijuana Businesses."

The SAFE and MORE Acts; The Past as a Prologue for the Future

The SAFE Act has been rattling around Congress for a couple of years, passed the House in 2019, and now has meaningful support in the Senate. Briefly, it aims to provide a "safe harbor" for depository institutions that want to do business with state-licensed cannabis companies and their service providers. Banks need a safe harbor because marijuana is currently a Schedule I drug under the Controlled Substances Act, banned for all purposes and illegal under federal law even in states that have legalized. Although the SAFE Act doesn't address the legality or scheduling of marijuana, it would provide a huge step towards resolving uncertainty, reducing risk, and providing a framework for expanded Bank participation in the industry, removing many of the concerns that prevent most Banks from doing so.

It would prevent federal Banking Regulators from punishing banks just because they provide services to cannabis businesses and free up federally insured Banks to both take deposits and lend. Among other things, it would clarify that, for purposes of federal anti-money laundering statutes, the proceeds of transactions involving activities of state legal cannabis businesses would not be considered proceeds of an unlawful activity. It would also provide that Banks that have a legal interest in the collateral for a loan or other financial service to state-legal cannabis businesses, or to an owner or operator of real estate or equipment leased or sold to such a business, would not be subject to criminal, civil, or administrative forfeiture of that legal interest pursuant to any federal law for providing that loan or service.

The MORE Act would significantly advance the progress represented by the SAFE Act. The MORE Act also passed the House (in December 2020) and several prominent Democratic senators have indicated that they intend to bring the MORE Act or something substantially similar to the Senate in 2021. The MORE Act would entirely remove marijuana—more specifically, THC, the psychoactive element in the plant—from the schedules of controlled substances under federal law, essentially legalizing the drug at the federal level. This would remove the many complications caused by current federal law for the cannabis industry and banks, including access to bankruptcy courts, tax deduction issues for cannabis businesses related to Section 280E of the tax code, impediments to obtaining insurance, etc.

Given this fraught environment, even Banks that already provide deposit accounts and a limited range of other services to MRBs don't make loans. Consequently, although some larger and more financially successful public companies have fared better, most cannabis companies needing debt finance have had to accept hard money terms from private lenders-much higher rates (ranging into the high teens and likely averaging 12–15%) and often highly dilutive equity conversion rights.

Impressive Financial Improvements; The Lure of Attractive Customers

If the mythological analogy of the cannabis industry from the second half of 2019 until mid-2020 is Icarus plummeting to earth after flying too close to the sun, it now is much more aptly the Phoenix rising from the ashes. Across the spectrum—small, single license operators, larger single state operators, small to large private multi-state operators ("MSOs"), and public companies—have achieved improvements in their financial condition and performance ranging from steady and solid to very, very impressive.

As a result, as the cannabis industry's already substantial appetite for credit continues to grow, at the same time, by gosh, cannabis businesses are becoming increasingly attractive customers for the Banks.

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Even as they do, it is likely, at least for some time, that Banks extending credit to the industry, even its best performers, will be able to price loan products at the premium end of the range for conventional commercial loans; providing highly attractive net interest margins.

Since even those premium rates will be far, far less than the rates the industry has been paying, the entry of Banks into the cannabis lending market will not only have meaningful, direct, and force multiplier effect, improving bottom lines, but should also accelerate the growth of the cannabis industry by providing an attractive incremental alternative to high priced debt or dilutive equity.

The Rocky Road to Encumbrances; Transfers of Control

Particularly in light of the inability to access the U.S. Bankruptcy Courts, creditors of cannabis businesses must look to current state laws and regulations. These provide a patchwork of uncertainty regarding security interests in licenses that will almost certainly inhibit Bank lending to cannabis companies even if the SAFE and MORE Acts are enacted. Existing state laws either preclude encumbrances against licenses and/or would subject lenders to post-default approvals under often complex, time consuming and inherently uncertain transfer of control regulations and processes. This is a major hurdle for lenders seeking to enforce their rights to take control before the value of an asset or business can be dissipated by a defaulting borrower that, presumably, wouldn't be in default unless the business was already in trouble.

Receiverships as an Alternative to Bankruptcy

Lessons may be drawn from two of the most mature cannabis states—Washington and Oregon.

Washington regulations allow a receiver for purposes of foreclosure and liquidation within the recreational cannabis industry. The Washington State Liquor and Cannabis Board maintains a list of preapproved receivers and allows for appointment of a receiver who is not preapproved upon receipt of the standard receiver application. Similarly, Oregon regulations allow for appointment of an authority to temporarily operate a cannabis licensed business as a trustee, receiver, or secured party.

Evaluating the Silence

When a state's laws, regulations, and cannabis regulators are silent on whether a license may be encumbered, the next logical step is to evaluate a state's position on transfers of ownership or control generally. Whether a license or control of a licensed business may be transferred, the steps involved in transferring a license or ownership, and whether there are carveouts for a license's transferability in connection with the exercise of a collateral interest, are all factors in the evaluation of whether a lender has a path to an enforceable security interest adequate to satisfy a Bank's and Bank Regulators' safety and soundness criteria.

As a general proposition, states typically impose onerous and time-consuming transfer requirements, and there are no guarantees that an approval will ultimately be granted, circumstances which must be addressed at the state level as part of an overall resolution to enable and facilitate Bank lending to cannabis businesses.

For questions, please contact Business and Corporate Law Member and Managing Partner of BMD's Phoenix/Scottsdale location Stephen Lenn at salenn@bmdllc.com, or 480.687.9747.

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Credit Union Regulator Urges Action On Pot Banking Reform

By **Sarah Jarvis**

Law360 (September 9, 2021, 8:09 PM EDT) -- National Credit Union Administration board member and former chairman Rodney Hood said at a payment industry conference that it's high time for banking regulators and Congress to take action to integrate the state-legal cannabis industry into the banking system.

Hood said in prepared remarks Thursday at the PBC Conference 2021 that in light of the rapid changes in the cannabis industry in recent years, the legal and regulatory infrastructure surrounding the cannabis industry is not evolving quickly enough.

"Let me be clear about where I stand: It is time for federal action to clarify and harmonize the laws and regulations surrounding the state-legal cannabis industry and marijuana-related businesses so that this industry can take part in the legitimate financial services industry," Hood said.

Hood was appointed to the National Credit Union Administration in 2005 and served a four-year term before he was sworn in for his second term in 2019, and he served as the agency's chairman until January.

He said that while the NCUA regulates more than 5,000 federally insured credit unions, just 169 of those are providing services to "one of the fastest-growing industries in the nation," which he called a serious market failure. Although many of the financial institutions would like to provide services to the cannabis industry, he said, they don't know how to proceed given limited guidance from the Financial Crimes Enforcement Network.

"The guidance from FinCEN, along with the Justice Department's guidance in the 2013 Cole memo, which was rescinded, was at least a start," Hood said. "But those were published in 2014 and 2013, respectively — almost a decade ago — and are too vague in any event to give financial institutions the clarity and confidence they need to move forward with cannabis banking beyond providing basic bank account services."

Hood highlighted his experience working to normalize banking services for hemp-related businesses after the 2018 Farm Bill delisted hemp from the federal list of controlled substances. He said there was a lack of clarity about the industry's regulatory status while awaiting new rules from the U.S. Department of Agriculture, noting the farm bill only addressed hemp cultivation and not the production and processing of hemp-derived products like CBD.

He said that in the NCUA's initial interim guidance, the agency wanted to give credit unions flexibility to experiment with the best way to work with lawful hemp businesses. He said after feedback from that initial guidance, the agency followed up with additional guidance in June 2020.

"Our approach was not overly prescriptive or heavy-handed," Hood said. "We wanted to provide credit unions the room to experiment and to decide for themselves how best to serve this burgeoning industry while we awaited the definitive regulatory guidance from the USDA, which finally took effect this year."

He said that while there are still challenges in the hemp space, including a lack of clear regulatory direction from the U.S. Food and Drug Administration, the agency helped set standards and clarify "a forward direction" for credit unions.

Looking ahead, he called for the creation of a formal working group through the Federal Financial Institutions Examination Council to start developing an approach to cannabis banking, calling the interagency body "a natural place for this working group to reside." He said the group could share a potential preliminary regulatory framework with other regulators and members of Congress.

Hood also urged Congress to take action to address cannabis banking but stopped short of endorsing any specific legislation, such as the Secure and Fair Enforcement, or SAFE, Banking Act, which was **passed** by the U.S. House of Representatives in April. The bill is on the back burner for Senate Majority Leader Chuck Schumer, D-N.Y., who has said he and his colleagues would prioritize the **marijuana decriminalization bill** he co-authored and released in July.

"The bottom line is this: Legalization in some form is going to happen, and the abdication of responsibility to address these issues in Washington is simply ludicrous," Hood said. "This is precisely the time we need leadership at the federal level to steer this ship in the right direction."

--Additional reporting by Sam Reisman. Editing by Daniel King.

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Rodney E. Hood
National Credit Union Administration
PBC Conference 2021:
Payments, Banking, Compliance in the Cannabis Industry
September 9, 2021

Thank you very much, and it's a pleasure to join you today.

I was sworn in as the chairman of the NCUA board in 2019, but this is actually my second term of service on the board. I was appointed to the NCUA in 2005 under President Bush; I served a four-year term that ended in 2009. I can tell you that serving two appointments at the same agency, separated by a decade, is one way to gain a unique vantage point on how rapidly things can change.

For example, when I first served on the NCUA board, I don't know that I would have attended this type of conference. Of course, that's assuming I would have been invited in the first place…

At that time, several states had already allowed qualified patients to access and use marijuana for medicinal purposes, but as a regulator I would not have considered the banking challenges of the cannabis industry to be at the top of my list of concerns. Of course, during that time we were also facing the housing crisis, the financial industry meltdown, and the subsequent recession and recovery – so we were focused on some particularly compelling priorities.

Well, here we are today, which is a testament to how fast things can evolve in a relatively short time. I take that idea of change and evolution as my theme today, because as a regulator, I'm concerned that the legal and regulatory infrastructure surrounding the cannabis industry is not evolving quickly enough.

And so as not to leave you in suspense, let me be clear about where I stand: it is time for federal action to clarify and harmonize the laws and regulations surrounding the state-legal cannabis industry and marijuana-related businesses (MRB), so that this industry can take part in the legitimate financial services industry.

Growth of an industry, and new challenges

For our purposes here today, I don't need to recount all of the statistics about the number of states that have legalized cannabis in one form or another, or the explosive growth of the state-legal cannabis industry over the last decade. If you weren't already familiar with those facts and statistics, you wouldn't be here. It's simply a remarkable social and cultural change that has taken place right before our eyes, and it's only going to continue to develop over the coming years.

Yet while this revolution has unfolded, federal law surrounding marijuana and cannabis-derived products has barely changed. There have been some welcome changes at the federal level, like delisting hemp from the list of controlled substances in the 2018 Farm Bill, but even those changes have been slow to arrive and relatively marginal. And there's been no meaningful legal change on the federal level when it comes to marijuana, despite all the rhetoric around marijuana legalization federally.

As a result, we've seen only limited development of the basic commercial banking infrastructure needed to provide financial services to this rapidly growing industry. Looking at the data from the Treasury Department's Financial Crimes Enforcement Network, or FinCen, as of the end of last year there were only 515 U.S. banks and 169 credit unions providing banking services to MRBs in accordance with the 2014 FinCEN guidelines, which as you all know is currently the only legitimate way for cannabis businesses to secure depository accounts with financial institutions.

Let's think about those numbers. My agency, the NCUA, regulates the system of federally insured credit unions, which includes more than 5,000 institutions. Yet only 169 of those are providing services to one of the fastest growing industries in the nation? That can only be described as a serious market failure.

The problem is not with the financial institutions themselves; many of them would be happy to provide services to the industry, but they're unsure of how to proceed given the limited FinCEN guidance. The guidance from FinCen, along with the Justice Department's guidance in the 2013 Cole memo, which that Cole memo was rescinded anyway, was at least a start. But those were published in 2014 and 2013, respectively—almost a decade ago!—and are too vague in any event to give financial institutions the clarity and confidence they need to move forward with cannabis banking beyond providing basic bank account services.

Which means we have this promising industry that's developing and growing rapidly – yet no way for the people who work in this industry to conduct the most fundamental business operations through legitimate financial channels. That is, frankly, an untenable situation. In stating these facts, I'm not telling you anything you don't know – again, it's why we're here today. The more critical question centers around what needs to happen next.

Here's a basic reality: as a rule, regulators really don't like to get out too far ahead of the policy process. We always seek to respect the existing statutes, and to defer to Congress as the policy-making arm of the government. However, there are times when a regulator in the executive branch needs to step forward to provide leadership, or at least nudge things along, when the policy process isn't working as it should. I believe that's the case today with marijuana and the financial services industry.

The hemp precedent

I have some relevant experience here based on the work we did at NCUA two years ago to normalize banking services for hemp-related businesses. One of the first regulatory reforms I undertook after being sworn in as chairman in 2019 was to push for interim regulatory guidance on providing financial services to hemp-related businesses. Many credit union industry leaders were focused on this issue, and we knew we needed to take action.

After Congress legalized hemp as an agricultural commodity, removing it from the list of controlled substances and allowing its cultivation in accordance with applicable State Plans, there remained a lack of clarity about the industry's regulatory status while we awaited new rules from the U.S. Department of Agriculture. Keep in mind that the 2018 Farm Bill only addresses the cultivation of hemp -- it is silent regarding the production and processing of hemp-derived products like CBD, which represents a huge slice of the hemp market in the United States.

And so a lot of hemp entrepreneurs found themselves stuck in a regulatory limbo – and as a result, financial services providers were unsure of how to work with them, especially since FinCEN guidelines only addressed state-licensed marijuana businesses and bank accounts. This new industry needed access to financial services to get off the ground – these entrepreneurs needed access to capital to invest in facilities and equipment; they needed to be able to meet payroll; they needed access to bank accounts so they didn't have to rely on cash transactions; and so forth. Does that sound familiar?

So I wanted the NCUA to take a leadership role in providing some clarity while we worked through that transition. In our initial interim guidance, we sought to keep it fairly simple, and to give credit unions the flexibility they needed to work with lawfully operating hemp-related businesses. As long as they did their due diligence and managed their risks accordingly, we wanted credit unions to be able to experiment with the best way to work with these businesses. Based upon feedback to our initial guidance, we followed that up with additional advisory guidance in June 2020, to address unforeseen issues and to provide additional clarity.

Our approach was not overly prescriptive or heavy-handed. We wanted to provide credit unions the room to experiment and to decide for themselves how best to serve this burgeoning industry while we awaited the definitive regulatory guidance from the USDA, which finally took effect this year.

Now, there are still some significant challenges in the hemp space, and things haven't progressed as quickly there as we might like, in part because they still don't have a clear regulatory direction from the Food and Drug Administration. But I'm proud that, at least when it came to credit unions, we were able to take a leading role in setting standards and clarifying a forward direction.

Next steps

I'd like to see something similar happen for cannabis and marijuana-related businesses, which is why I'd like to outline three steps that I would like to take now, as a regulator, to move this issue forward:

- **First, we already have a working group at the NCUA devoted to cannabis banking, and I've been in communication with them and will be working with them to determine what we might do next to better address the challenges to cannabis banking on our side. At this point, we may be somewhat limited in what we can achieve, but I'm urging the agency to think hard about taking those next steps.**

- **Second, and this might be the most significant action item we can achieve right now, I am calling for the establishment of a formal working group on the part of financial regulators to take the lead on this issue and to start developing a principles-based approach to cannabis banking. The good news is that we already have a vehicle through which this could be accomplished: the Federal Financial Institutions Examination Council, or FFFIEC. Most of you have never heard of FFFIEC, which is fine, but it's an interagency body that develops uniform principles, standards, and report forms for the federal examination of financial institutions. The NCUA is a member, and I've done a lot of work with the council over the years, so I know it's a natural place for this working group to reside and to deliver a preliminary regulatory framework that we can share with other regulators and members of Congress who share our concern about addressing these problems.**

- **Third, I will urge Congress to take action to address cannabis banking as the 2014 FinCEN guidelines are simply not enough to support what hemp and cannabis businesses need to grow and sustain. You're probably aware there are various legislative proposals dealing with these challenges. I'm told the SAFE Banking Act, for example, includes a number of promising proposals that would go a long way toward providing the clarity we need, but for now I don't plan to endorse any particular piece of legislation. I would prefer for Congress to make that determination, and will be happy to provide any advice or guidance from the regulators' perspective that will be of help. In fact, just next week I'll be talking to one of the credit union trade associations on their annual visit to meet with members of Congress, and I'll be encouraging them to help us make the case to their representatives and senators. I certainly appreciate the members of Congress who are taking part in this conference today, and I look forward to working with them to make progress on this issue.**

A caveat here: I'm a financial services industry regulator, and I can only speak to issues related to that area. I recognize there are a host of other regulatory issues that will need to be considered to address consumer protection issues, environmental issues, and other concerns.

The good news is that the banking issues should be relatively straightforward, compared to some of those challenges. We're talking here primarily about taking deposits; opening up lending at reasonable rates of interest; and opening increased access to payment systems so you don't have to handle massive piles of cash. If we can address those needs in a straightforward manner, we create an on-ramp to legitimize the cannabis industry while ensuring the safety and soundness of the financial system. Really, these should not be such difficult issues to address, should they? The 2014 FinCEN guidelines laid the groundwork for depository accounts, but it's time now to build on those guidelines to accommodate the rapid growth of the industry.

Conclusion

I've spent a good deal of time and energy on this issue over the last couple of years, talking to experts on the legal side, on the industry side, in the financial services industry. I've heard a variety of perspectives, but there's one common refrain: they all agree that legalization is a matter of when, not if – and they urge federal action to get it done.

The bottom line is this: Legalization is going to happen, and the abdication of responsibility to address these issues in Washington is simply ludicrous. This is precisely the time we need leadership at the federal level to steer this ship in the right direction. In one of my discussions with an attorney who works on these issues, he noted that this is a unique opportunity to create a completely new industry – but that will require rethinking an outdated approach to marijuana that centers around the prohibition mindset.

As the great management thinker Peter Drucker noted, "The greatest danger in times of turbulence is not the turbulence – it is to act with yesterday's logic." Or perhaps in this case, to *fail to act* based on yesterday's logic. It's time to get past yesterday's logic and focus on the future.

Moreover, as I look at this promising, growing industry, I can't help but notice that it sits comfortably at the intersection of several of my top priorities: regulatory reform; support for entrepreneurialism and innovation; and financial inclusion. That's a tremendous opportunity that brings tremendous challenges – but it requires leadership to get it done. And continued inaction, just allowing a patchwork of ad hoc state solutions to take effect, is not my idea of leadership.

The fact that we haven't had adequate federal leadership on cannabis banking to date doesn't mean that we can't have leadership now, so I'm happy to take what actions I can to create forward momentum. For those of you in the industry, I can't promise you that you'll get everything you want—but certainly if we can address key needs like commercial lending and opening access to electronic payments for this industry, we'll have made a significant step forward. And my pledge to you is that I'll be working with you to get it done. Thank you.

American Bankers Association
Building Success. Together.

Rob Nichols
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April 19, 2021

The Honorable Nancy Pelosi
Speaker of the House
U.S. House of Representatives
Washington, D.C. 20515

The Honorable Kevin McCarthy
Minority Leader
U.S. House of Representatives
Washington, D.C. 20515

Dear Speaker Pelosi and Minority Leader McCarthy:

On behalf of the American Bankers Association (ABA), I am writing to express our strong support for H.R. 1996, the Secure and Fair Enforcement Banking Act (SAFE Banking Act) of 2021 introduced by Representatives Ed Perlmutter (D-CO), Steve Stivers(R-OH), Warren Davidson (R-OH), Nydia Velazquez (D-NY) and over 150 bipartisan cosponsors.

This legislation, scheduled for consideration on this week's suspension calendar, addresses the conflict between federal and state law and whether banks can serve cannabis and cannabis related businesses. This issue has become a challenge for so many of our nation's communities and the banks that serve them. We were pleased to see this legislation passed the House of Representatives last Congress with over 300 bipartisan votes. With more states legalizing some form of cannabis use, we are hopeful that H.R. 1996 will once again receive a favorable and strong bipartisan vote.

Since 1996, voters across the country have determined that it is appropriate to allow their citizens to use cannabis for medical purposes and, since 2012, for adult use. Currently, 36 states have legalized cannabis for medical or adult use and that number continues to grow. Nevertheless, current federal law prevents banks from safely banking cannabis businesses, as well as the ancillary businesses that provide them with goods and services.

As a result, a majority of states are struggling to address the significant challenges to public safety, as well as regulatory and tax compliance that go hand-in-hand with businesses forced to operate in an all-cash environment. Providing a mechanism for the cannabis industry to access the banking system would help those communities reduce cash-motivated crimes, increase the efficiency of tax collections, and improve the financial transparency of the cannabis industry. Since bank accounts are monitored in accordance with existing anti-money laundering and Bank Secrecy Act requirements, bringing cannabis-related legitimate businesses into the mainstream banking sector would also help law enforcement to identify suspicious transactions – an opportunity that is not available in an all-cash environment.

ABA does not take a position on the legalization of cannabis. Nevertheless, our member banks find themselves in a difficult situation due to the conflict between state and federal law, with local communities encouraging them to bank cannabis businesses and federal law prohibiting it. Congress must act to resolve this conflict between state and federal law.

The Controlled Substances Act (21 U.S.C. §801 et seq.) classifies cannabis as an illegal drug and prohibits its use for any purpose. For banks, that means that all proceeds generated by a cannabis-related business, even when it is operating in compliance with state law, are unlawful proceeds under federal law, and so any attempt to conduct a financial transaction with that money (including simply accepting a deposit) can be considered money-laundering. All banks, whether state or federally

chartered, are subject to federal anti-money laundering laws. And, all banks must have access to the federal payment system to operate, which is under the purview of federal authority. Thus, banking entities related to the cannabis business can pose significant regulatory sanction risk, loss of access to the payments system, and the potential loss of the bank charter itself. This places banks in an untenable position in dealing with these state-authorized businesses.

Currently, the only direction available to financial institutions in connection with cannabis-related accounts comes from guidance issued by the Financial Crimes Enforcement Network (FinCEN) in 2014. That guidance, which references a now rescinded memorandum from the U.S. Department of Justice (the "Cole Memo"), describes how financial institutions can report cannabis-related business activity consistent with their Bank Secrecy Act obligations. It does not create a safe harbor or otherwise modify federal law to protect banks from criminal and civil liability for money laundering. It merely creates a system for reporting activity that is illegal under federal law but otherwise legal under state law.

Although some financial institutions have weighed the prevailing climate of non-enforcement and have decided to shoulder the risk in order to serve the needs of their communities, the majority of financial institutions will not take the legal, regulatory, or reputational risk associated with banking cannabis-related businesses without congressional action. As a result, state-legal businesses are being excluded from the mainstream financial system.

The problems, though, are not limited to those businesses that have direct contact with the marijuana plant, such as growers and dispensaries. The impact of the divide between state and federal law extends to any person or business that derives revenue from a cannabis firm – including real estate owners, security firms, utilities, vendors and employees of cannabis businesses, as well as investors. As the legal state-cannabis industry continues to grow, the indirect connections to cannabis revenues will also continue to expand. Without greater clarity, that entire portion of economic activity in legal cannabis states will continue to be marginalized from the banking system.

The bipartisan SAFE Banking Act would be an important step toward enabling financial services for cannabis-related businesses. The bill specifies that proceeds from a legitimate cannabis business would not be considered unlawful under federal money laundering statutes or any other federal law, which is necessary to allow the provision of financial services to cannabis-related legitimate businesses as well as any ancillary businesses that derive some portion of their income from those businesses. The bill would also direct FinCEN, and the federal banking regulators through the Federal Financial Institutions Examination Council, to issue guidance and exam procedures for banks doing business with cannabis-related legitimate businesses. Explicit, consistent direction from federal financial regulators will provide needed clarity for banks and help them better evaluate the risks and supervisory expectations for cannabis-related customers. The SAFE Banking Act is not a cure all for the cannabis banking challenge, but it is a measure that helps clarify many issues for the banking industry and regulators.

ABA is pleased to support the SAFE Banking Act and urges members of the House of Representatives to vote in favor of this legislation when it is brought up on this week's suspension calendar.

Sincerely,

Rob Nichols

cc: Members of the United States House of Representatives

U.S. Department of Justice

Office of the Deputy Attorney General

The Deputy Attorney General

Washington, D.C. 20530

February 14, 2014

MEMORANDUM FOR ALL UNITED STATES ATTORNEYS

FROM: James M. Cole
Deputy Attorney General

SUBJECT: Guidance Regarding Marijuana Related Financial Crimes

On August 29, 2013, the Department issued guidance (August 29 guidance) to federal prosecutors concerning marijuana enforcement under the Controlled Substances Act (CSA). The August 29 guidance reiterated the Department's commitment to enforcing the CSA consistent with Congress' determination that marijuana is a dangerous drug that serves as a significant source of revenue to large-scale criminal enterprises, gangs, and cartels. In furtherance of that commitment, the August 29 guidance instructed Department attorneys and law enforcement to focus on the following eight priorities in enforcing the CSA against marijuana-related conduct:

- Preventing the distribution of marijuana to minors;
- Preventing revenue from the sale of marijuana from going to criminal enterprises, gangs, and cartels;
- Preventing the diversion of marijuana from states where it is legal under state law in some form to other states;
- 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 violence and the use of firearms in the cultivation and distribution of marijuana;
- Preventing drugged driving and the exacerbation of other adverse public health consequences associated with marijuana use;
- Preventing the growing of marijuana on public lands and the attendant public safety and environmental dangers posed by marijuana production on public lands; and
- Preventing marijuana possession or use on federal property.

Under the August 29 guidance, whether marijuana-related conduct implicates one or more of these enforcement priorities should be the primary question in considering prosecution

under the CSA. Although the August 29 guidance was issued in response to recent marijuana legalization initiatives in certain states, it applies to all Department marijuana enforcement nationwide. The guidance, however, did not specifically address what, if any, impact it would have on certain financial crimes for which marijuana-related conduct is a predicate.

The provisions of the money laundering statutes, the unlicensed money remitter statute, and the Bank Secrecy Act (BSA) remain in effect with respect to marijuana-related conduct. Financial transactions involving proceeds generated by marijuana-related conduct can form the basis for prosecution under the money laundering statutes (18 U.S.C. §§ 1956 and 1957), the unlicensed money transmitter statute (18 U.S.C. § 1960), and the BSA. Sections 1956 and 1957 of Title 18 make it a criminal offense to engage in certain financial and monetary transactions with the proceeds of a "specified unlawful activity," including proceeds from marijuana-related violations of the CSA. Transactions by or through a money transmitting business involving funds "derived from" marijuana-related conduct can also serve as a predicate for prosecution under 18 U.S.C. § 1960. Additionally, financial institutions that conduct transactions with money generated by marijuana-related conduct could face criminal liability under the BSA for, among other things, failing to identify or report financial transactions that involved the proceeds of marijuana-related violations of the CSA. *See, e.g.,* 31 U.S.C. § 5318(g). Notably for these purposes, prosecution under these offenses based on transactions involving marijuana proceeds does not require an underlying marijuana-related conviction under federal or state law.

As noted in the August 29 guidance, the Department is committed to using its limited investigative and prosecutorial resources to address the most significant marijuana-related cases in an effective and consistent way. Investigations and prosecutions of the offenses enumerated above based upon marijuana-related activity should be subject to the same consideration and prioritization. Therefore, in determining whether to charge individuals or institutions with any of these offenses based on marijuana-related violations of the CSA, prosecutors should apply the eight enforcement priorities described in the August 29 guidance and reiterated above. [1] For example, if a financial institution or individual provides banking services to a marijuana-related business knowing that the business is diverting marijuana from a state where marijuana sales are regulated to ones where such sales are illegal under state law, or is being used by a criminal organization to conduct financial transactions for its criminal goals, such as the concealment of funds derived from other illegal activity or the use of marijuana proceeds to support other illegal activity, prosecution for violations of 18 U.S.C. §§ 1956, 1957, 1960 or the BSA might be appropriate. Similarly, if the financial institution or individual is willfully blind to such activity by, for example, failing to conduct appropriate due diligence of the customers' activities, such prosecution might be appropriate. Conversely, if a financial institution or individual offers

[1] The Department of the Treasury's Financial Crimes Enforcement Network (FinCEN) is issuing concurrent guidance to clarify BSA expectations for financial institutions seeking to provide services to marijuana-related businesses. The FinCEN guidance addresses the filing of Suspicious Activity Reports (SAR) with respect to marijuana-related businesses, and in particular the importance of considering the eight federal enforcement priorities mentioned above, as well as state law. As discussed in FinCEN's guidance, a financial institution providing financial services to a marijuana-related business that it reasonably believes, based on its customer due diligence, does not implicate one of the federal enforcement priorities or violate state law, would file a "Marijuana Limited" SAR, which would include streamlined information. Conversely, a financial institution filing a SAR on a marijuana-related business it reasonably believes, based on its customer due diligence, implicates one of the federal priorities or violates state law, would be label the SAR "Marijuana Priority," and the content of the SAR would include comprehensive details in accordance with existing regulations and guidance.

services to a marijuana-related business whose activities do not implicate any of the eight priority factors, prosecution for these offenses may not be appropriate.

The August 29 guidance rested on the expectation that states that have enacted laws authorizing marijuana-related conduct will implement clear, strong and effective regulatory and enforcement systems in order to minimize the threat posed to federal enforcement priorities. Consequently, financial institutions and individuals choosing to service marijuana-related businesses that are not compliant with such state regulatory and enforcement systems, or that operate in states lacking a clear and robust regulatory scheme, are more likely to risk entanglement with conduct that implicates the eight federal enforcement priorities. [2] In addition, because financial institutions are in a position to facilitate transactions by marijuana-related businesses that could implicate one or more of the priority factors, financial institutions must continue to apply appropriate risk-based anti-money laundering policies, procedures, and controls sufficient to address the risks posed by these customers, including by conducting customer due diligence designed to identify conduct that relates to any of the eight priority factors. Moreover, as the Department's and FinCEN's guidance are designed to complement each other, it is essential that financial institutions adhere to FinCEN's guidance.[3] Prosecutors should continue to review marijuana-related prosecutions on a case-by-case basis and weigh all available information and evidence in determining whether particular conduct falls within the identified priorities.

As with the Department's previous statements on this subject, this memorandum is intended solely as a guide to the exercise of investigative and prosecutorial discretion. This memorandum does not alter in any way the Department's authority to enforce federal law, including federal laws relating to marijuana, regardless of state law. Neither the guidance herein nor any state or local law provides a legal defense to a violation of federal law, including any civil or criminal violation of the CSA, the money laundering and unlicensed money transmitter statutes, or the BSA, including the obligation of financial institutions to conduct customer due diligence. Even in jurisdictions with strong and effective regulatory systems, evidence that particular conduct of a person or entity threatens federal priorities will subject that person or entity to federal enforcement action, based on the circumstances. This memorandum is not intended, does not, and may not be relied upon to create any rights, substantive or procedural, enforceable at law by any party in any matter civil or criminal. It applies prospectively to the exercise of prosecutorial discretion in future cases and does not provide defendants or subjects of enforcement action with a basis for reconsideration of any pending civil action or criminal prosecution. Finally, nothing herein precludes investigation or prosecution, even in the absence of any one of the factors listed above, in particular circumstances where investigation and prosecution otherwise serves an important federal interest.

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[2] For example, financial institutions should recognize that a marijuana-related business operating in a state that has not legalized marijuana would likely result in the proceeds going to a criminal organization.

[3] Under FinCEN's guidance, for instance, a marijuana-related business that is not appropriately licensed or is operating in violation of state law presents red flags that would justify the filing of a Marijuana Priority SAR.

Department of the Treasury
Financial Crimes Enforcement Network

Guidance

FIN-2014-G001
Issued: February 14, 2014
Subject: BSA Expectations Regarding Marijuana-Related Businesses

The Financial Crimes Enforcement Network ("FinCEN") is issuing guidance to clarify Bank Secrecy Act ("BSA") expectations for financial institutions seeking to provide services to marijuana-related businesses. FinCEN is issuing this guidance in light of recent state initiatives to legalize certain marijuana-related activity and related guidance by the U.S. Department of Justice ("DOJ") concerning marijuana-related enforcement priorities. This FinCEN guidance clarifies how financial institutions can provide services to marijuana-related businesses consistent with their BSA obligations, and aligns the information provided by financial institutions in BSA reports with federal and state law enforcement priorities. This FinCEN guidance should enhance the availability of financial services for, and the financial transparency of, marijuana-related businesses.

Marijuana Laws and Law Enforcement Priorities

The Controlled Substances Act ("CSA") makes it illegal under federal law to manufacture, distribute, or dispense marijuana.[1] Many states impose and enforce similar prohibitions. Notwithstanding the federal ban, as of the date of this guidance, 20 states and the District of Columbia have legalized certain marijuana-related activity. In light of these developments, U.S. Department of Justice Deputy Attorney General James M. Cole issued a memorandum (the "Cole Memo") to all United States Attorneys providing updated guidance to federal prosecutors concerning marijuana enforcement under the CSA.[2] The Cole Memo guidance applies to all of DOJ's federal enforcement activity, including civil enforcement and criminal investigations and prosecutions, concerning marijuana in all states.

The Cole Memo reiterates Congress's determination that marijuana is a dangerous drug and that the illegal distribution and sale of marijuana is a serious crime that provides a significant source of revenue to large-scale criminal enterprises, gangs, and cartels. The Cole Memo notes that DOJ is committed to enforcement of the CSA consistent with those determinations. It also notes that DOJ is committed to using its investigative and prosecutorial resources to address the most

[1] Controlled Substances Act, 21 U.S.C. § 801, *et seq.*
[2] James M. Cole, Deputy Attorney General, U.S. Department of Justice, *Memorandum for All United States Attorneys: Guidance Regarding Marijuana Enforcement* (August 29, 2013), *available at* http://www.justice.gov/iso/opa/resources/3052013829132756857467.pdf.

significant threats in the most effective, consistent, and rational way. In furtherance of those objectives, the Cole Memo provides guidance to DOJ attorneys and law enforcement to focus their enforcement resources on persons or organizations whose conduct interferes with any one or more of the following important priorities (the "Cole Memo priorities"):[3]

- Preventing the distribution of marijuana to minors;
- Preventing revenue from the sale of marijuana from going to criminal enterprises, gangs, and cartels;
- Preventing the diversion of marijuana from states where it is legal under state law in some form to other states;
- 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 violence and the use of firearms in the cultivation and distribution of marijuana;
- Preventing drugged driving and the exacerbation of other adverse public health consequences associated with marijuana use;
- Preventing the growing of marijuana on public lands and the attendant public safety and environmental dangers posed by marijuana production on public lands; and
- Preventing marijuana possession or use on federal property.

Concurrently with this FinCEN guidance, Deputy Attorney General Cole is issuing supplemental guidance directing that prosecutors also consider these enforcement priorities with respect to federal money laundering, unlicensed money transmitter, and BSA offenses predicated on marijuana-related violations of the CSA.[4]

Providing Financial Services to Marijuana-Related Businesses

This FinCEN guidance clarifies how financial institutions can provide services to marijuana-related businesses consistent with their BSA obligations. In general, the decision to open, close, or refuse any particular account or relationship should be made by each financial institution based on a number of factors specific to that institution. These factors may include its particular business objectives, an evaluation of the risks associated with offering a particular product or service, and its capacity to manage those risks effectively. Thorough customer due diligence is a critical aspect of making this assessment.

In assessing the risk of providing services to a marijuana-related business, a financial institution should conduct customer due diligence that includes: (i) verifying with the appropriate state authorities whether the business is duly licensed and registered; (ii) reviewing the license application (and related documentation) submitted by the business for obtaining a state license to operate its marijuana-related business; (iii) requesting from state licensing and enforcement authorities available information about the business and related parties; (iv) developing an understanding of the normal and expected activity for the business, including the types of

[3] The Cole Memo notes that these enforcement priorities are listed in general terms; each encompasses a variety of conduct that may merit civil or criminal enforcement of the CSA.

[4] James M. Cole, Deputy Attorney General, U.S. Department of Justice, *Memorandum for All United States Attorneys: Guidance Regarding Marijuana Related Financial Crimes* (February 14, 2014).

products to be sold and the type of customers to be served (e.g., medical versus recreational customers); (v) ongoing monitoring of publicly available sources for adverse information about the business and related parties; (vi) ongoing monitoring for suspicious activity, including for any of the red flags described in this guidance; and (vii) refreshing information obtained as part of customer due diligence on a periodic basis and commensurate with the risk. With respect to information regarding state licensure obtained in connection with such customer due diligence, a financial institution may reasonably rely on the accuracy of information provided by state licensing authorities, where states make such information available.

As part of its customer due diligence, a financial institution should consider whether a marijuana-related business implicates one of the Cole Memo priorities or violates state law. This is a particularly important factor for a financial institution to consider when assessing the risk of providing financial services to a marijuana-related business. Considering this factor also enables the financial institution to provide information in BSA reports pertinent to law enforcement's priorities. A financial institution that decides to provide financial services to a marijuana-related business would be required to file suspicious activity reports ("SARs") as described below.

Filing Suspicious Activity Reports on Marijuana-Related Businesses

The obligation to file a SAR is unaffected by any state law that legalizes marijuana-related activity. A financial institution is required to file a SAR if, consistent with FinCEN regulations, the financial institution knows, suspects, or has reason to suspect that a transaction conducted or attempted by, at, or through the financial institution: (i) involves funds derived from illegal activity or is an attempt to disguise funds derived from illegal activity; (ii) is designed to evade regulations promulgated under the BSA, or (iii) lacks a business or apparent lawful purpose.[5] Because federal law prohibits the distribution and sale of marijuana, financial transactions involving a marijuana-related business would generally involve funds derived from illegal activity. Therefore, a financial institution is required to file a SAR on activity involving a marijuana-related business (including those duly licensed under state law), in accordance with this guidance and FinCEN's suspicious activity reporting requirements and related thresholds.

One of the BSA's purposes is to require financial institutions to file reports that are highly useful in criminal investigations and proceedings. The guidance below furthers this objective by assisting financial institutions in determining how to file a SAR that facilitates law enforcement's access to information pertinent to a priority.

"Marijuana Limited" SAR Filings

A financial institution providing financial services to a marijuana-related business that it reasonably believes, based on its customer due diligence, does not implicate one of the Cole Memo priorities or violate state law should file a "Marijuana Limited" SAR. The content of this

[5] *See, e.g.*, 31 CFR § 1020.320. Financial institutions shall file with FinCEN, to the extent and in the manner required, a report of any suspicious transaction relevant to a possible violation of law or regulation. A financial institution may also file with FinCEN a SAR with respect to any suspicious transaction that it believes is relevant to the possible violation of any law or regulation but whose reporting is not required by FinCEN regulations.

SAR should be limited to the following information: (i) identifying information of the subject and related parties; (ii) addresses of the subject and related parties; (iii) the fact that the filing institution is filing the SAR solely because the subject is engaged in a marijuana-related business; and (iv) the fact that no additional suspicious activity has been identified. Financial institutions should use the term "MARIJUANA LIMITED" in the narrative section.

A financial institution should follow FinCEN's existing guidance on the timing of filing continuing activity reports for the same activity initially reported on a "Marijuana Limited" SAR.[6] The continuing activity report may contain the same limited content as the initial SAR, plus details about the amount of deposits, withdrawals, and transfers in the account since the last SAR. However, if, in the course of conducting customer due diligence (including ongoing monitoring for red flags), the financial institution detects changes in activity that potentially implicate one of the Cole Memo priorities or violate state law, the financial institution should file a "Marijuana Priority" SAR.

"Marijuana Priority" SAR Filings

A financial institution filing a SAR on a marijuana-related business that it reasonably believes, based on its customer due diligence, implicates one of the Cole Memo priorities or violates state law should file a "Marijuana Priority" SAR. The content of this SAR should include comprehensive detail in accordance with existing regulations and guidance. Details particularly relevant to law enforcement in this context include: (i) identifying information of the subject and related parties; (ii) addresses of the subject and related parties; (iii) details regarding the enforcement priorities the financial institution believes have been implicated; and (iv) dates, amounts, and other relevant details of financial transactions involved in the suspicious activity. Financial institutions should use the term "MARIJUANA PRIORITY" in the narrative section to help law enforcement distinguish these SARs.[7]

"Marijuana Termination" SAR Filings

If a financial institution deems it necessary to terminate a relationship with a marijuana-related business in order to maintain an effective anti-money laundering compliance program, it should

[6] Frequently Asked Questions Regarding the FinCEN Suspicious Activity Report (Question #16), *available at:* http://fincen.gov/whatsnew/html/sar_faqs.html (providing guidance on the filing timeframe for submitting a continuing activity report).

[7] FinCEN recognizes that a financial institution filing a SAR on a marijuana-related business may not always be well-positioned to determine whether the business implicates one of the Cole Memo priorities or violates state law, and thus which terms would be most appropriate to include (i.e., "Marijuana Limited" or "Marijuana Priority"). For example, a financial institution could be providing services to another domestic financial institution that, in turn, provides financial services to a marijuana-related business. Similarly, a financial institution could be providing services to a non-financial customer that provides goods or services to a marijuana-related business (e.g., a commercial landlord that leases property to a marijuana-related business). In such circumstances where services are being provided indirectly, the financial institution may file SARs based on existing regulations and guidance without distinguishing between "Marijuana Limited" and "Marijuana Priority." Whether the financial institution decides to provide indirect services to a marijuana-related business is a risk-based decision that depends on a number of factors specific to that institution and the relevant circumstances. In making this decision, the institution should consider the Cole Memo priorities, to the extent applicable.

file a SAR and note in the narrative the basis for the termination. Financial institutions should use the term "MARIJUANA TERMINATION" in the narrative section. To the extent the financial institution becomes aware that the marijuana-related business seeks to move to a second financial institution, FinCEN urges the first institution to use Section 314(b) voluntary information sharing (if it qualifies) to alert the second financial institution of potential illegal activity. See *Section 314(b) Fact Sheet* for more information.[8]

Red Flags to Distinguish Priority SARs

The following red flags indicate that a marijuana-related business may be engaged in activity that implicates one of the Cole Memo priorities or violates state law. These red flags indicate only possible signs of such activity, and also do not constitute an exhaustive list. It is thus important to view any red flag(s) in the context of other indicators and facts, such as the financial institution's knowledge about the underlying parties obtained through its customer due diligence. Further, the presence of any of these red flags in a given transaction or business arrangement may indicate a need for additional due diligence, which could include seeking information from other involved financial institutions under Section 314(b). These red flags are based primarily upon schemes and typologies described in SARs or identified by our law enforcement and regulatory partners, and may be updated in future guidance.

- A customer appears to be using a state-licensed marijuana-related business as a front or pretext to launder money derived from other criminal activity (i.e., not related to marijuana) or derived from marijuana-related activity not permitted under state law. Relevant indicia could include:
    - The business receives substantially more revenue than may reasonably be expected given the relevant limitations imposed by the state in which it operates.
    - The business receives substantially more revenue than its local competitors or than might be expected given the population demographics.
    - The business is depositing more cash than is commensurate with the amount of marijuana-related revenue it is reporting for federal and state tax purposes.
    - The business is unable to demonstrate that its revenue is derived exclusively from the sale of marijuana in compliance with state law, as opposed to revenue derived from (i) the sale of other illicit drugs, (ii) the sale of marijuana not in compliance with state law, or (iii) other illegal activity.
    - The business makes cash deposits or withdrawals over a short period of time that are excessive relative to local competitors or the expected activity of the business.

[8] Information Sharing Between Financial Institutions: Section 314(b) Fact Sheet, *available at: http://fincen.gov/statutes_regs/patriot/pdf/314bfactsheet.pdf.*

- Deposits apparently structured to avoid Currency Transaction Report ("CTR") requirements.

- Rapid movement of funds, such as cash deposits followed by immediate cash withdrawals.

- Deposits by third parties with no apparent connection to the accountholder.

- Excessive commingling of funds with the personal account of the business's owner(s) or manager(s), or with accounts of seemingly unrelated businesses.

- Individuals conducting transactions for the business appear to be acting on behalf of other, undisclosed parties of interest.

- Financial statements provided by the business to the financial institution are inconsistent with actual account activity.

- A surge in activity by third parties offering goods or services to marijuana-related businesses, such as equipment suppliers or shipping servicers.

- The business is unable to produce satisfactory documentation or evidence to demonstrate that it is duly licensed and operating consistently with state law.

- The business is unable to demonstrate the legitimate source of significant outside investments.

- A customer seeks to conceal or disguise involvement in marijuana-related business activity. For example, the customer may be using a business with a non-descript name (e.g., a "consulting," "holding," or "management" company) that purports to engage in commercial activity unrelated to marijuana, but is depositing cash that smells like marijuana.

- Review of publicly available sources and databases about the business, its owner(s), manager(s), or other related parties, reveal negative information, such as a criminal record, involvement in the illegal purchase or sale of drugs, violence, or other potential connections to illicit activity.

- The business, its owner(s), manager(s), or other related parties are, or have been, subject to an enforcement action by the state or local authorities responsible for administering or enforcing marijuana-related laws or regulations.

- A marijuana-related business engages in international or interstate activity, including by receiving cash deposits from locations outside the state in which the business operates, making or receiving frequent or large interstate transfers, or otherwise transacting with persons or entities located in different states or countries.

- The owner(s) or manager(s) of a marijuana-related business reside outside the state in which the business is located.

- A marijuana-related business is located on federal property or the marijuana sold by the business was grown on federal property.

- A marijuana-related business's proximity to a school is not compliant with state law.

- A marijuana-related business purporting to be a "non-profit" is engaged in commercial activity inconsistent with that classification, or is making excessive payments to its manager(s) or employee(s).

Currency Transaction Reports and Form 8300's

Financial institutions and other persons subject to FinCEN's regulations must report currency transactions in connection with marijuana-related businesses the same as they would in any other context, consistent with existing regulations and with the same thresholds that apply. For example, banks and money services businesses would need to file CTRs on the receipt or withdrawal by any person of more than $10,000 in cash per day. Similarly, any person or entity engaged in a non-financial trade or business would need to report transactions in which they receive more than $10,000 in cash and other monetary instruments for the purchase of goods or services on FinCEN Form 8300 (Report of Cash Payments Over $10,000 Received in a Trade or Business). A business engaged in marijuana-related activity may not be treated as a non-listed business under 31 C.F.R. § 1020.315(e)(8), and therefore, is not eligible for consideration for an exemption with respect to a bank's CTR obligations under 31 C.F.R. § 1020.315(b)(6).

* * * * *

FinCEN's enforcement priorities in connection with this guidance will focus on matters of systemic or significant failures, and not isolated lapses in technical compliance. Financial institutions with questions about this guidance are encouraged to contact FinCEN's Resource Center at (800) 767-2825, where industry questions can be addressed and monitored for the purpose of providing any necessary additional guidance.

Hon. Charles E. Schumer
Majority Leader
322 Hart Senate Office Building
Washington, DC 20510

Hon. Mitch McConnell
Minority Leader
317 Russell Senate Office Building
Washington, DC 20510

Hon. Nancy Pelosi
Speaker of the House
1236 Longworth House Office Building
Washington, DC 20515

Hon. Kevin McCarthy
Minority Leader
2468 Rayburn House Office Building
Washington, DC 20515

Hon. Sherrod Brown
Chair
Senate Committee on Banking,
Housing and Urban Affairs
503 Hart Senate Office Building
Washington, DC 20510

Hon. Pat Toomey
Ranking Member
Senate Committee on Banking,
Housing and Urban Affairs
455 Dirksen Senate Office Building
Washington, DC 20510

Hon. Maxine Waters
Chair
House Committee on Financial
Services
2221 Rayburn House Office Building
Washington, DC 20515

Hon. Patrick McHenry
Ranking Member
House Committee on Financial
Services
2004 Rayburn House Office Building
Washington, DC 20515

April 19, 2021

Dear Congressional Leaders:

As our States' chief executives, we urge Congress to pass legislation allowing states with legalized medical or adult-use cannabis to operate safely under the national banking system. We strongly support the passage of the Secure and Fair Enforcement (SAFE) Banking Act of 2021 (H.R. 1996/S. 910) or similar legislation that would remove the legal uncertainty and allow banks and credit unions to provide services to state-licensed cannabis-related businesses.

We were pleased that the House passed similar legislation in the 116th Congress (H.R. 1595). The SAFE Banking Act of 2021 already has more than 165 bipartisan House cosponsors and more than 30 bipartisan Senate cosponsors. The legislation has also received support from more than 30 associations.

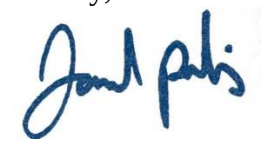
Currently, 36 U.S. states, four U.S. territories, and the District of Columbia have legalized the medical use of cannabis. Additionally, 18 states, two territories, and the District of Columbia have legalized recreational use by adults over 21 years of age. Despite legalization of cannabis at the state-level, our financial institutions face enormous legal risks and criminal and civil liability under the Controlled Substances Act. These barriers disincentive financial institutions from providing banking services to state-licensed and regulated cannabis businesses.

Because few banks and credit unions provide these services, state-licensed cannabis businesses predominantly operate on a cash basis. Without banking services, state-licensed cannabis businesses are unable to write checks, make and receive electronic payments, utilize a payroll provider, or accept credit and debit cards. Cash only businesses pose a significant public safety risk to customers and employees. The cash-only environment also burdens state and local government agencies that must collect tax and fee payments in person and in cash, which creates additional public expenses and employee safety risks.

State and federal governments have a shared interest in upholding the rule of law, protecting public safety, and transitioning markets out of the shadows and into our transparent and regulated banking system. Many of our states have implemented laws and regulations to reduce these risks while ensuring financial accountability of the cannabis industry. These public safety risks can be further mitigated on the federal level by passing the SAFE Banking Act to provide state-licensed cannabis businesses with access to banking service providers.

We urge you to pass the SAFE Banking Act of 2021 or similar legislation that would provide a safe harbor for depository institutions that provide a financial product or service to a state-licensed cannabis business in states that have legalized cannabis. We look forward to working with you as legislation progresses to address this urgent public policy and safety concern.

Sincerely,



Governor Jared Polis
State of Colorado

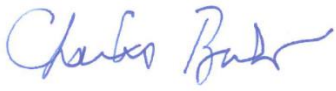
Governor Gavin Newsom
State of California

Governor Ned Lamont
State of Connecticut

Governor JB Pritzker
State of Illinois

Governor John Bel Edwards
State of Louisiana

Governor Janet Mills
State of Maine



Governor Charlie Baker
State of Massachusetts

Governor Gretchen Whitmer
State of Michigan

Governor Steve Sisolak
State of Nevada

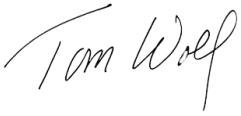
Governor Phil Murphy
State of New Jersey

Governor Michelle Lujan Grisham
State of New Mexico

Governor Andrew Cuomo
State of New York

Governor Doug Burgum
State of North Dakota

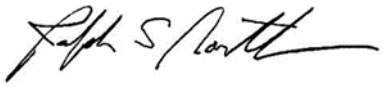
Governor Kate Brown
State of Oregon



Governor Tom Wolf
State of Pennsylvania

Governor Spencer Cox
State of Utah

Governor Albert Bryan
Territory of U.S. Virgin Islands



Governor Ralph Northam
State of Virginia

Governor Jay Inslee
State of Washington

Governor Jim Justice
State of West Virginia

Governor Tony Evers
State of Wisconsin

April 19, 2021

The Honorable Nancy Pelosi
Speaker of the House
U.S. House of Representatives
Washington, D.C. 20515

The Honorable Kevin McCarthy
Minority Leader
U.S. House of Representatives
Washington, D.C. 20515

Dear Speaker Pelosi and Minority Leader McCarthy:

On behalf of the undersigned state bankers associations, representing banks of all sizes, we write to express our support for H.R. 1996, the Secure and Fair Enforcement Banking Act (SAFE Banking Act) of 2021. This strongly bipartisan legislation scheduled for consideration on this week's suspension calendar would be an important step to address the conflict between federal and state laws and how banks safely work with legal cannabis and cannabis related businesses.

Although we do not take a position on the legalization of marijuana, our members are committed to serving the financial needs of their communities – including those that have voted to legalize cannabis. Currently, 36 states covering 70 percent of the nation's population have legalized cannabis for medical or adult-use. Despite this ever-growing voter preference, current federal law continues to prevent banks from safely banking these businesses without fear of federal sanctions. As a result, this segment of our local economies is forced to operate on an all-cash basis, which creates serious public safety, revenue administration, and legal compliance concerns in the communities we serve.

The impact on our local economies could also prove significant, as revenue paid to unrelated industries that provide products and services to state-authorized cannabis businesses such as law firms, accountants and contractors is technically money derived from illegal activities, and thus could be considered money laundering. This raises the significant question of whether financial institutions can bank these ancillary businesses, as such actions could likewise be considered violations of the money laundering laws. Without a change to federal law, that entire portion of economic activity in legal cannabis states may be marginalized from the banking system.

The SAFE Banking Act is a banking-specific bipartisan solution that would address the reality of the current marketplace and allow banks to serve cannabis-related businesses in states where the activity is legal.

We urge members of the House of Representatives to support H.R. 1996, the SAFE Banking Act, when this bill comes before the House on this week's suspension calendar.

Sincerely,

Alabama Bankers Association
Alaska Bankers Association
Arizona Bankers Association
Arkansas Bankers Association
California Bankers Association
Colorado Bankers Association
Connecticut Bankers Association
Delaware Bankers Association

Florida Bankers Association
Georgia Bankers Association
Hawaii Bankers Association
Idaho Bankers Association
Illinois Bankers Association
Indiana Bankers Association
Iowa Bankers Association
Kansas Bankers Association
Kentucky Bankers Association
Louisiana Bankers Association
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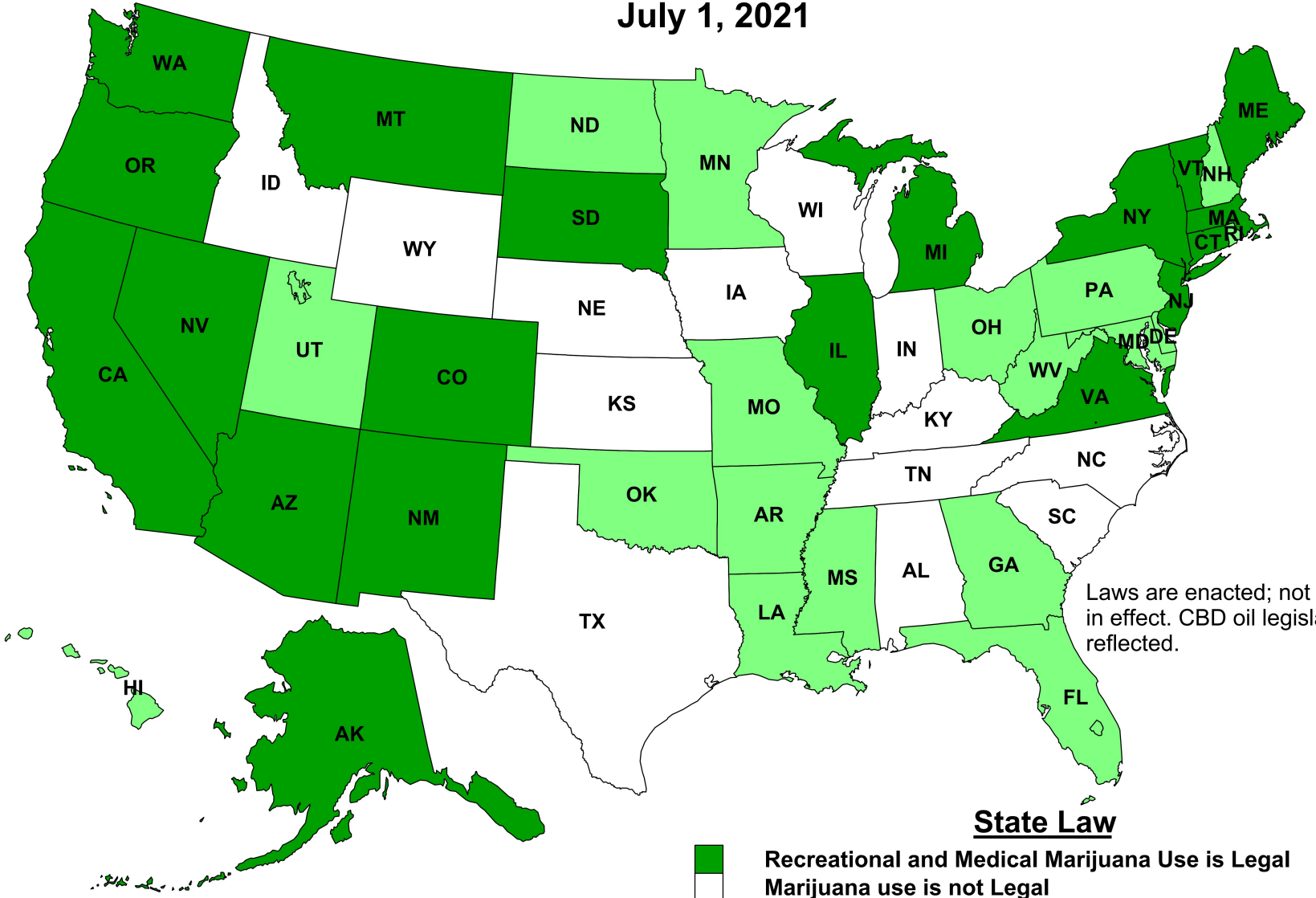
Nevada Bankers Association
New Hampshire Bankers Association
New Jersey Bankers Association
New Mexico Bankers Association
New York Bankers Association
North Carolina Bankers Association
North Dakota Bankers Association
Ohio Bankers League
Oklahoma Bankers Association
Oregon Bankers Association
Pennsylvania Bankers Association
Puerto Rico Bankers Association
Rhode Island Bankers Association
South Carolina Bankers Association
South Dakota Bankers Association
Tennessee Bankers Association
Texas Bankers Association
Utah Bankers Association
Vermont Bankers Association
Virginia Bankers Association
Washington Bankers Association
West Virginia Bankers Association
Wisconsin Bankers Association
Wyoming Bankers Association

cc: Members of the United States House of Representatives

States with Legalized Marijuana

American Nonsmokers' Rights Foundation

July 1, 2021



Laws are enacted; not yet necessarily in effect. CBD oil legislation is not reflected.

State Law

Recreational and Medical Marijuana Use is Legal
Marijuana use is not Legal
Medical Marijuana Use, but not Recreational, is Legal

Note: In total, medical marijuana use is legal in 37 states.

To see a map of state and local laws prohibiting smoking and vaping marijuana,visit https://no-smoke.org/wp-content/uploads/pdf/marijuana-smokefree-laws-map.pdf

Note: American Indian and Alaska Native sovereign Tribal laws are not reflected on this map.

[LS-49]

The Inevitable Inexorable Intersection: Cannabis And Banking

by **Benzinga Cannabis Contributors** 10 min read
4 days ago

By Teddy Kirsch and Steve Lenn of L&S Business Law.

As the cannabis industry continues to expand, so too will the universe of existing and potential banking customers that will necessarily have financial or business relationships with licensed cannabis companies ("Licensees"). While the SAFE Banking Act languishes in Congress, under the limited existing federal guideline available, even banks that do not do business directly with Licensees are finding it necessary to address the possible requirements for enhanced due diligence, documentation and monitoring that may be required when considering doing business with customers that have interests and relationships that may be considered "marijuana related businesses" ("MRBs") even when the proposed banking relation is totally separate from, and unrelated to, the customer's

cannabis interests. In fulfilling their know your customer ("KYC") responsibilities at intake and on an ongoing basis, banks need to be alert to these potential requirements. They must also understand that the banking regulators are both sensitized to the possibilities and appear to be working cooperatively to address them, so transparency with regulators is, at the same time, a must.

While securing services from financial institutions has been a challenge for MRBs, there are several dozen federally insured banks and credit unions that openly offer such services. To mitigate the risk of running afoul of a myriad of federal financial crimes laws by doing so, banks (and banking regulators) draw upon guidance in a release dated February 14, 2014 issued by the Financial Crimes Enforcement Network ("FinCen"), "BSA Expectations Regarding Marijuana-Related Businesses" (the "Guidance").

FinCen is a bureau of the U.S. Department of the Treasury, the mission of which is to safeguard the financial system from illicit use and combat money laundering and promote national security. The text of the Guidance articulates as its purpose as clarifying *"how financial institutions can provide services to marijuana-related businesses consistent with their BSA obligations…."* It further articulated that the Guidance was intended to *"enhance the availability of services for, and the financial transparency of, marijuana related businesses."*

The Guidance cites as underlying precepts the priorities established pursuant to a memorandum issued by U.S. Department of Justice Deputy Attorney General James M. Cole dated August 29, 2013 (the "Cole Memorandum"). Although the Cole Memorandum was supplemented by advisories from other Assistant U.S. Attorneys, the priorities have essentially been left in place. It is also important to keep in mind that the Cole Memorandum (as supplemented) provides guidance only. Early in his tenure, Attorney General Sessions issued a "recission" of the guidance, but there has been no perceptible change at the enforcement level.

The Cole Memorandum priorities include:

- Preventing distribution to minors;
- Preventing revenue from the sale of marijuana from going to criminal enterprises;
- Preventing the diversion of marijuana to states in which it is not legal;
- Preventing state authorized marijuana activities from being used as a cover for other; drug trafficking or illegal activity;
- Preventing the use of firearms in the cultivation and distribution of marijuana;
- Preventing drugged driving and other adverse health consequences.

The Guidance also provides a laundry list of red flags[1], and dictates that financial institutions seeking to act in compliance with the Guidance must tailor their relationships with MRBs to address and mitigate the risk of interfering with the accomplishment of the priorities shown above.

Unfortunately, the Guidance does not define "marijuana related business," and FinCEN has not issued any further guidance regarding this definition. However, the Guidance makes clear that the classification includes more than just plant touching enterprises, choosing to directly extend the classification as far as to landlords of MRB's[2]. While not dispositive nor binding as it relates to the Guidance, an expansive reading is supported by a Small Business Administration Policy Notice effective April 3, 2018, which offered the following definitions:

(a) "Direct Marijuana Business" -- a business that grows, produces, processes, distributes, or sells marijuana or marijuana products, edibles, or derivatives, regardless of the amount of such activity. This applies to personal use and medical use even if the business is legal under local or state law where the applicant business is or will be located. (b) "Indirect Marijuana Business" -- a business that derived any of its gross revenue for the previous year (or, if a start-up, projects to derive any of its gross revenue for the next year) from sales to Direct Marijuana Businesses of products or services that could reasonably be determined to support the use, growth, enhancement or other development of marijuana. Examples include businesses that provide testing services, or sell grow lights or hydroponic equipment, to one or more Direct Marijuana Businesses.

Under the circumstances, and particularly in view of the sensitivity of bank regulators to these issues, it seems prudent for banks to consider the definition expansively, at least for purposes of a threshold determination regarding whether and what level of enhanced attention is necessary. Banks must be alert to even what seem to be fairly attenuated financial and business relationships in considering, underwriting, structuring and monitoring any transaction involving a customer that could be deemed an MRB.

In connection with any customer that could be so classified, banks should consider and address the extent to which any of the Cole Memorandum priorities could be implicated and, therefore, which red flags to be alert to. **Simply put, the greater the risk a priority is implicated, the more a bank will need to do in these regards. Conversely, as the Guidance recognizes, to the extent certain priorities are not implicated, a bank's approach may reflect the lower level of risk and remain in compliance with the Guidance.** Documenting reasonable consideration of these factors is critical, not just for purposes of compliance with the Guidance, but also to mitigate the risks of federal asset seizure of any assets material to the customer relationship, an area of regulatory concern.

Analysis And Conclusions

1. Banks in states with large and expanding legal cannabis markets should put in place procedures specifically designed to alert them to potential MRB issues. They may also wish to consider at least general policies so they have a framework in place and can react in a businesslike process and competitive time frame when an attractive opportunity arises.

2. A bank's regulators should be kept in the loop and consulted as bank's policies and procedures are developed and evolve. Doing so in consultation with regulatory authorities

not only assures transparency, but also enables a bank to benefit from the experience and expertise being developed by regulatory authorities that are increasingly being called upon as both the marijuana industry and its intersections with the banking industry expand.

3. There are a number of sections of the Guidance that reflect FinCEN's recognition of the relevance of "reasonableness" and practical considerations relating, among other things, to the unavailability of information or materials regarding the actual Licensee. While it calls upon financial institutions to consider, "*to the extent applicable*," the Cole Memorandum priorities referred to in the Guidance, it also explicitly recognizes distinctions based on the extent to which any particular marijuana-related business could implicate Cole Memorandum considerations and that deciding to "indirectly" provide services to a marijuana-related business is "a risk-based decision that depends on a number of factors specific to that institution and the relevant circumstances."

The Guidance specially recognizes that some of the information suggested in it may be confidential and unavailable to a bank not doing business directly with a Licensee. The Guidance notes, "With respect to information regarding state licensure obtained in connection with such customer due diligence, a financial institution may reasonably rely on the accuracy of information provided by state licensing authorities, ***where states make such information available***". In such circumstances, it may be prudent to ask the customer what can be provided or make available to assist the bank in taking the actions contemplated by the Guidance regarding (i) tracking cash transactions, (ii) verification of the license and that the MRB is being operated in conformity with the Cole Memorandum. A bank may also wish to assure ongoing monitoring of publicly available sources for adverse information about the business and related parties and for suspicious activity, including for any of the red flags described in the Guidance, and refreshing information obtained as part of customer due diligence on a periodic basis and commensurate with the risk.

Finally, issues related to the potential risk of federal seizure of assets are complicated and, as with much of the law related to the cannabis business, less than clear and appear to be evolving as the industry matures.

Generally speaking, to support a seizure, particularly one in which an asset is subject to a perfected security interest, the government must prove, among other things, that the asset represented the fruits of an illegal enterprise. With that in mind, based on circumstances described below, the risk of an asset collateralizing a credit transaction being lost due to federal seizure can be substantially mitigated, if not entirely eliminated if a bank (i) adheres to the Guidance, (ii) exercises and documents due diligence, underwriting and monitoring procedures appropriate to the particular circumstances, (iii) takes care in documentation, and (iv) even though the burden of proof may be on the government, if the bank can demonstrate it was not acquired with proceeds of illegal activities.

Absent other factors, such as the failure to file Suspicious Activity Reports ("SAR") or activity that otherwise impairs the Cole Memorandum priorities, there appears limited appetite for asset seizure enforcement at the federal level with respect to medical

marijuana activities legal at the state level. To a certain extent this reflects increasing public acceptance of decriminalization, recently at more than two-thirds. In addition, more likely than not, also a reflection or byproduct of the shift in public opinion, since 2014 annual bi-partisan budget appropriations have included a prohibition against the Department of Justice use of appropriated funds to prosecute in circumstances where there has been full compliance with state medical marijuana laws. In 2016, this limitation was applied in the U.S. 9th Circuit Court of Appeals case, United States v. McIntosh[3]. The Court held that 11 USC § 542[4] prohibits the DOJ from spending funds from relevant appropriations acts for the prosecution of individuals who engaged in conduct permitted by state medical marijuana laws and who fully complied with such laws. However, the 9th Circuit also held that it would not be improper to sue under 11 USC § 542 and ultimately have the DOJ use appropriations act funds to seize the assets of individuals who do not strictly comply with all state-law conditions regarding the use, distribution, possession, and cultivation of medical marijuana.

With the foregoing in mind, the following additional comments and suggestions are offered:

1. In underwriting any credit transaction, a bank should be prepared to demonstrate that it will not look to the value or revenues of the MRB as sources of repayment.

2. The initial and ongoing underwriting protocols, due diligence, monitoring and documentation should:

a. Restrict cash transactions, perhaps and, if possible, by requiring any funds received by a customer from or in connection with an MRB shall have been paid by check drawn on a federally insured depositary institution;

b. Assure that non-MRB assets and revenues remain sufficient;

c. Require prompt notice of any change in the status of the Licensee triggering the MRB definition or in any banking relationship of such MRB.

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[1] See Pgs. 5-7, https://www.fincen.gov/sites/default/files/guidance/FIN-2014-G001.pdf.

[2] See Pg 4 Footnote 7. https://www.fincen.gov/sites/default/files/guidance/FIN-2014-G001.pdf

[3] https://cdn.ca9.uscourts.gov/datastore/opinions/2016/08/16/15-10117.pdf

[4] https://www.law.cornell.edu/uscode/text/11/542

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Dear Congressional Leaders:

We are a bipartisan group of state and territorial attorneys general committed to public safety, financial transparency, and the rule of law. On May 8, 2019, 38 state and territorial attorneys general urged passage of the SAFE Banking Act, or similar legislation, that would provide a safe harbor for depository institutions that service a marijuana-related business in a state with robust regulatory controls that ensure accountability in the marijuana industry. *See Enclosed*. The undersigned attorneys general renew that support here and urge Congress advance these same goals as part of any future COVID-19 relief package.

The COVID-19 pandemic has sharply focused the need for legislative relief in three key respects. First, threats to public safety caused by a cash-intensive business model, often the target of criminal activity, have intensified in the months since the pandemic began. Next, the presence of large cash transactions places law enforcement, tax regulators, consumers, and patients at heightened risk of exposure to the virus. Finally, the ability to efficiently collect tax revenue from the marijuana industry, estimated to have generated $15 billion in sales in 2019, will provide critical relief for state and local governments predicting budget shortfalls due to the pandemic.

The current predicament of a rapidly expanding national marketplace without access to the national banking systems has resulted in an untenable situation. We stress that current legislative models are available to fix this situation. In advancing these legislative goals, Congress is not necessarily endorsing any state or territory's legalization of marijuana-related transactions; similarly, the enactment of the SAFE Banking Act is not a call for the legalization of medical or retail marijuana in those jurisdictions that choose not to pursue such an approach. Rather, it reflects a recognition of the realities on the ground and an embrace of our federalist system of government that is flexible enough to accommodate divergent state approaches

We look forward to working with you and to providing any further expertise as Congress continues this important legislative endeavor.

Sincerely,

Phil Weiser
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Wayne Stenehjem
North Dakota Attorney General

Kevin G. Clarkson
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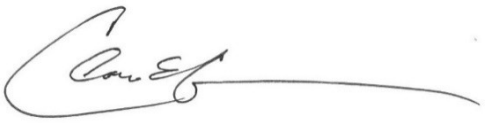

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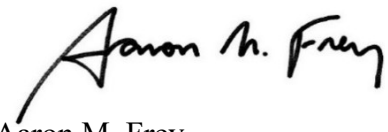

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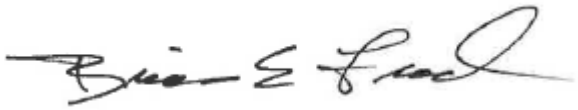

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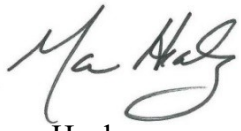

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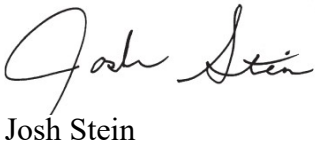

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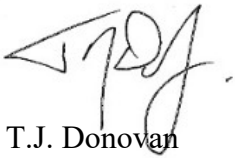

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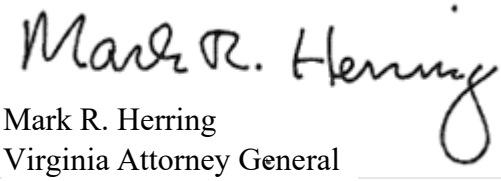

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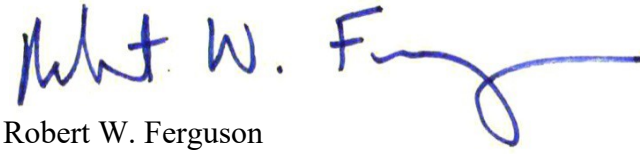

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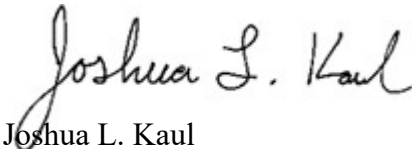

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Boris Jordan’s MSN interview link

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