

Marijuana -- An Overview of Pertinent Issues Related to Use, Regulation, and Business

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Where Did Marijuana Come From?

- *Cannabis Sativa*, *Cannabis Indica*, *Cannabis Sativa L.*, and *Cannabis Ruderalis* have been used extensively and globally in various ways for thousands of years
 - Burned marijuana seeds have been found in burial mounds in Siberia dating back to 3,000 B.C.
 - Tombs of individuals buried in the Xinjiang region of China in 2,500 B.C. have included “large quantities of mummified psychoactive marijuana”
- Some marijuana plants are thought to have evolved in Central Asia -- specifically in the regions that are now Mongolia and Southern Siberia
- *Cannabis Indica* has origins in Northwest India, Tajikistan, Uzbekistan, and the Western Tian Shan mountain range

History of Marijuana Use

- Marijuana use for medicinal purposes is well-documented throughout the 19th Century
 - Report of the Committee on *Cannabis Indica* of the Ohio State Medical Society, published in 1860, indicated success in treating stomach pain, childbirth psychosis, chronic cough, and gonorrhea through hemp products
 - Widely used to treat pains of inflammatory and “neuralgic nature” and earned a place as a “hypnotic [medicine] next to opium”
 - Sedative, relaxant, anxiolytic, and anticonvulsant functions made marijuana very useful for treatment of opiate and alcohol withdrawal
 - Marijuana gained widespread recognition for its therapeutic uses, low toxicity, and the minimal development of tolerance to marijuana products

History of Marijuana Use (cont'd)

- Recreationally, marijuana has been used extensively throughout history in religious, shamanic, and spiritual contexts
 - Use in Nepal and India dates back to at least 1,500 B.C.
 - Hinduism and Sikhism have historically incorporated use of “weaker preparations” (e.g., *Bhang*) for social and religious purposes at celebrations to induce a relaxed and social mood, and increased appetite
 - Historically, weaker preparations such as *Bhang* and *Ganja* have been deemed socially acceptable, whereas *Charas* (hashish) users were often regarded as “bad characters” -- this is useful in putting today’s nationwide medical and recreational laws and policies into perspective
 - Marijuana regarded as a “fashionable narcotic” at “hashish parlors” across the U.S. -- approximately 500 hashish parlors in New York in 1880s

History of Marijuana Regulation

- Poison Laws (1906)
 - Required labels indicating the harmful effects of the drug or prohibited sale other than by licensed pharmacies and without a prescription -- e.g., “cannabis and its preparations”
- Pure Food and Drug Act (1906)
 - Labeling requirements
- International Opium Convention (1925)
 - U.S. supported a ban on exportation of *Indian Hemp* to countries that had prohibited its use -- importing countries were required to issue certificates approving the importation and stating that the shipment was required “exclusively for medical or scientific purposes”
- Uniform Narcotic State Act (1932)
 - *Marijuana Menace* -- by mid-1930s all states had some regulation of marijuana
- Geneva Drug Trafficking Convention (1936)
 - The U.S. did not sign the Convention because it considered it to be too weak, particularly in relation to extradition, extraterritoriality, and the confiscation of trafficking revenues -- the Convention was a turning point nonetheless because it introduced the concept of drug activities being an “international crime”

History of Marijuana Regulation (cont'd)

- Marijuana Tax Act (1937)
 - Made possession and transfer of marijuana illegal across the U.S. under federal law (excluding medical and industrial uses)
 - *Reefer Madness*, anti-marijuana campaigning, and the hemp industry
- Federal Food, Drug, and Cosmetic Act (FFDCA) (1938)
 - Legislation for U.S. Food and Drug Administration's (FDA) efforts related to marijuana
- Boggs Act (1952) and Narcotic Controls Act (1956)
 - Mandatory sentencing and increased punishment -- first-time possession = minimum of two to ten years with a fine up to \$20,000
- Controlled Substances Act (CSA) (1970) -- current federal law
 - Title II of the Comprehensive Drug Abuse Prevention and Control Act of 1970 -- repealed Marijuana Tax Act
 - Schedule I -- “drugs with **no currently accepted medical use** and a **high potential for abuse**” -- marijuana alongside heroin, lysergic acid diethylamide (LSD), and 3,4-methylenedioxymethamphetamine (ecstasy)
 - Creation of Drug Enforcement Agency (DEA) and “decriminalization” efforts
- Anti-Drug Abuse Act (1986)
 - Mandatory prison sentences and “three-strikes” law under Reagan Administration

Current Legal Status of Marijuana

- Marijuana is illegal under federal law -- classified as a Schedule I drug under CSA
- Medical marijuana is legal in 28 states and Washington, D.C., including New York, Florida, and Ohio
- Recreational marijuana legalization measures in eight states and Washington, D.C. -- currently, recreational marijuana is legal in California, Oregon, Washington, Alaska, Colorado, and Washington, D.C.
 - Massachusetts -- **December 15, 2016**
 - Nevada -- **January 1, 2017**
 - Maine (“wild card”) -- recount -- **30 days after Governor certifies election results**
- Numerous states have decriminalization measures in place for marijuana

Current Public Opinion on Marijuana

- Approximately 200 million users or more across the globe
- Fifty-seven percent of U.S. adults believe marijuana use should be legal, whereas 37 percent believe it should be illegal -- a decade ago, 32 percent of U.S. adults favored legalization, and 60 percent opposed legalization
- “Millennials” -- those of ages 18 to 35 in 2016 -- are more than twice as likely to support legalization of marijuana as they were in 2006 (71 percent vs. 34 percent), and are significantly more likely to support legalization than other generations
- Fifty-seven percent of “Generation X” (ages 36 to 51) supports legalization of marijuana
- Fifty-six percent of “Baby Boomers” (ages 52 to 70) support legalization of marijuana
- Sixty-six percent of Democrats support marijuana legalization
- Forty-one percent of Republicans favor marijuana legalization
- Hispanics are generally less supportive of marijuana legalization than those of other ethnicities

*Source: Pew Research Center

Federal-level Legal Issues

- Commerce Clause -- *Gonzales v. Raich* (2005)
 - Question: Does CSA exceed Congress' power under the Commerce Clause as applied to intrastate cultivation and possession of marijuana for medical use?
 - Answer: No -- the Court held that the Commerce Clause gives Congress authority to prohibit the local cultivation and use of marijuana despite state law to the contrary
 - Local use affects supply and demand in the national marijuana market, making regulation of intrastate marijuana use essential to regulating the national marijuana market

- Supremacy Clause -- *Crosby v. National Foreign Trade Council* (2000)
 - State laws that conflict with federal law are generally preempted and therefore void
 - *Crosby v. National Foreign Trade Council* -- state law presents a sufficient obstacle to the accomplishment of federal objectives where “the purpose of the [federal act cannot be accomplished]”
 - A lack of finding of a “positive conflict” and use of the Supremacy Clause to preempt state laws is arguably an indication of a degree of acceptance of state-level marijuana legalization measures

- Anti-Commandeering Principle -- *Printz v. United States* (1997)
 - Prohibits federal government from imposing targeted, affirmative, coercive duties upon state legislators or executive officials -- federal government cannot force states to criminalize conduct

Ogden Memo (October 19, 2009)

- Memorandum from David W. Ogden, Deputy Attorney General, to U.S. Attorneys “intended solely as a guide to the exercise of investigative and prosecutorial discretion”
- “Original hands-off policy”
 - Did not change the U.S. Department of Justice’s (DOJ) authority to enforce federal law, including laws prohibiting manufacture, possession, or use of marijuana
 - “The prosecution of significant traffickers of illegal drugs, including marijuana, and the disruption of illegal drug manufacturing and trafficking networks continues to be a core priority ... investigative and prosecutorial resources should be directed towards these objectives. **As a general matter, pursuit of these priorities should not focus federal resources [on] individuals whose actions are in clear and unambiguous compliance with existing state laws providing for the medical use of marijuana**”
 - *E.g.*, prosecution of individuals with cancer or other serious illnesses who use marijuana as part of a recommended treatment regimen consistent with state law, or those caregivers in clear and unambiguous compliance with existing state law who provide such individuals with marijuana, is unlikely to be an efficient use of limited federal resources
 - Prosecution of commercial enterprises that unlawfully market and sell marijuana for profit continues to be an enforcement priority
 - Typically, the following characteristics, among others, may indicate illegal drug trafficking of potential federal interest: (1) unlawful possession or unlawful use of firearms; (2) violence; (3) sales to minors; (4) excessive amounts of cash; and (5) illegal possession or sale of other controlled substances

Cole Memo 1.0 (June 29, 2011)

- Memorandum from James M. Cole, who replaced Ogden as Deputy Attorney General, to U.S. Attorneys
 - “Caregiver” = “individuals providing care to individuals with cancer or other serious illnesses, not commercial operations cultivating, selling or distributing marijuana”
 - “[DOJ’s] view of the efficient use of limited federal resources as articulated in the [Ogden Memo] has not changed. There has, however, been an increase in the scope of commercial cultivation, sale, distribution and use of marijuana for purported medical purposes. For example, within the past 12 months, several jurisdictions have considered or enacted legislation to authorize multiple large-scale, privately-operated industrial marijuana cultivation centers. Some of these planned facilities have revenue projections of millions of dollars based on the planned cultivation of tens of thousands of cannabis plants”
 - Ogden Memo was never intended to shield cultivation of marijuana in states where medical marijuana is legal from federal enforcement action and prosecution -- “persons who are in the business of cultivating, selling or distributing marijuana, and those who knowingly facilitate such activities, are in violation of [CSA]”
 - Cultivators, sellers, and distributors of marijuana are subject to federal enforcement action
 - Those engaged in transactions involving the proceeds of marijuana cultivation, sale, or distribution may also be in violation of federal money laundering statutes and other federal financial laws
- Cole Memo 1.0 and the *DEA Position on Marijuana* resulted in numerous raids against the marijuana industry

Cole Memo 2.0 (August 29, 2013)

- Memorandum from James M. Cole, Deputy Attorney General, to U.S. Attorneys
 - DOJ's enforcement priorities: (1) preventing distribution of marijuana to minors; (2) preventing revenue from the sale of marijuana from going to criminal enterprises, gangs, and cartels; (3) preventing the diversion of marijuana from states where it is legal under state law in some form to other states; (4) preventing state-authorized marijuana activity from being used as a cover or pretext for trafficking of other illegal drugs or other illegal activity; (5) preventing violence and the use of firearms in the cultivation and distribution of marijuana; (6) preventing drugged driving and the exacerbation of other adverse public health consequences associated with marijuana use; (7) preventing the growing of marijuana on public lands; and (8) preventing marijuana possession or use on federal property
 - Cole Memo 2.0 serves as guidance to DOJ attorneys and law enforcement to focus enforcement resources and efforts, including prosecution, on persons/organizations whose conduct interferes with these priorities, irrespective of state law
 - Federal government has traditionally relied upon states and local law enforcement agencies to address marijuana activity through enforcement of their own narcotics laws -- "[t]he enactment of state laws that endeavor to authorize marijuana production, distribution, and possession by establishing a regulatory scheme for these purposes affects this traditional joint federal-state approach to narcotics enforcement. [DOJ's] guidance in this memorandum rests on the expectation that states and local governments that have enacted laws authorizing marijuana-related conduct will implement strong and effective regulatory and enforcement systems"

Cole Memo 2.0 (August 29, 2013) (cont'd)

- In jurisdictions that have enacted laws legalizing marijuana in some form and that have implemented strong and effective regulatory and enforcement systems to control cultivation, distribution, sale, and possession of marijuana, conduct in compliance with those laws is less likely to threaten the aforementioned priorities
 - Enforcement of state law by state and local law enforcement and regulatory bodies should be the primary means of addressing marijuana-related activity
 - Message = inefficient use of federal resources to prosecute state-level legal marijuana businesses

- Although previous memoranda arguably authorized targeting of “large scale, for-profit commercial enterprises,” Cole Memo 2.0 stated that existence of a strong state-level regulatory system and an operation’s compliance with the system “may allay the threat that an operation’s size poses to federal enforcement interests”
 - Prosecutors should not consider the size or commercial nature of a marijuana operation alone as a proxy for assessing whether marijuana trafficking implicates enforcement priorities
 - Prosecutors should review marijuana cases on a case-by-case basis and weigh all available information and evidence, including whether the operation is “demonstrably in compliance with a strong and effective state regulatory system”

Cole Memo 2.0 (August 29, 2013) (cont'd)

- Interesting policy deviation -- revised and more meaningful “hands-off approach”
 - Tacit message from Obama Administration that permitted marijuana businesses to grow
 - Unless enforcement priorities are implicated, CSA not enforced for marijuana in states where legalization measures are in place
- December 2014 \$1.1 trillion spending bill prohibits DOJ from using funds to target state-level medical marijuana programs -- distribution, possession, and cultivation included
 - Implied that DEA will not enforce federal-level marijuana law in states where legalization measures are in place
 - Sam Farr (D-CA): “The federal government will finally respect the decisions made by the majority of states that passed medical marijuana laws. This is a great day for common sense because now our federal dollars will be spent more wisely on prosecuting criminals and not sick patients”

Marijuana Law Reform Efforts

- Ending Federal Marijuana Prohibition Act of 2013 (H.R. 499)
- Respect State Marijuana Laws Act of 2013 (H.R. 1523)
- States' Medical Marijuana Patient Protection Act of 2013 (H.R. 689)
- Truth in Trials Act of 2013 (H.R. 710)
- National Commission on Federal Marijuana Policy Act of 2013 (H.R. 1635)
- No Welfare for Weed Act of 2014 (H.R. 4142)
- Unmuzzle the Drug Czar Act of 2014 (H.R. 4046)
- Charlotte's Web Medical Hemp Act of 2014 (H.R. 5226)
- Clean Slate for Marijuana Offenses Act of 2015 (H.R. 3124)

Marijuana Law Reform Efforts (cont'd)

- Regulate Marijuana Like Alcohol Act of 2015 (H.R. 1013)
- Marijuana Tax Revenue Act of 2015 (H.R. 1014)
- States' Medical Marijuana Property Rights Protection Act of 2015 (H.R. 262)
- Veterans Equal Access Act of 2015 (H.R. 667)
- Industrial Hemp Farming Act of 2015 (S. 134)
- Small Business Tax Equity Act of 2015 (S. 987)
- Legitimate Use of Medicinal Marijuana Act (LUMMA) of 2015 (H.R. 2373)
- Respect States' and Citizens' Rights Act of 2015 (H.R. 3629)
- Marijuana Businesses Access to Banking Act of 2015 (H.R. 2076)
- Compassionate Access, Research Expansion, and Respect States (CARERS) Act of 2015 (H.R. 1538/S. 683)

Marijuana and Banking

- *The Fourth Corner Credit Union v. Federal Reserve Bank of Kansas City (2016)* -- “courts cannot use equitable powers to issue an order that would facilitate criminal activity ... A federal court cannot look the other way”
- Bank Secrecy Act (BSA), enforced by the U.S. Department of the Treasury’s Financial Crimes Enforcement Network (FinCEN), requires banks to monitor customer accounts for activities associated with crime and terrorism -- marijuana is under CSA Schedule I
 - BSA requires banks to investigate their customers thoroughly and neither negligently nor knowingly conduct business with those acting illegally
 - FinCEN released Guidance on February 14, 2014, providing pathways for banks that want to work with the legal marijuana industry while maintaining compliance with BSA
 - Banks’ due diligence in assessing risk in providing financial services to marijuana-related businesses should include: (1) verifying with appropriate state authorities that the business is duly licensed and registered; (2) reviewing the marijuana license application of the business; (3) requesting from state licensing and enforcement authorities available information about the business and related parties; (4) developing an understanding of the normal and expected activity of the business, including the types of products to be sold and the types of customers; (5) ongoing monitoring of publicly available sources for adverse information about the business and related parties; (6) ongoing monitoring for suspicious activity; and (7) refreshing information obtained as part of customer due diligence on a periodic basis and commensurate with risk
 - Banks must consider if Cole Memo 2.0 priorities are implicated by marijuana businesses

Marijuana and Banking (cont'd)

- FinCEN requires that financial institutions file Suspicious Activity Reports (SAR) with the federal government when they know or suspect an account holder is engaging in unlawful activity -- all marijuana activity is unlawful
 - Does not implicate Cole Memo 2.0 priorities = “Marijuana Limited” SAR Filings
 - Reasonably believes, based on due diligence, that the marijuana-related business implicates Cole Memo 2.0 priorities = “Marijuana Priority” SAR Filings
 - Deems it necessary to terminate a relationship with a marijuana-related business to maintain an effective anti-money laundering compliance program = “Marijuana Termination” SAR Filings
- Guidance identifies “red flags” to distinguish Priority SARs (e.g., substantially more revenue than may be expected, depositing more cash than is commensurate with revenue reported for tax purposes)
- Cole Memo 3.0 (February 14, 2014) complements FinCEN Guidance -- if banks offer services to marijuana businesses that do not implicate a Cole Memo 2.0 priority, prosecuting them “may not be appropriate”
- Little or no assurance from the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation (FDIC), and the Federal Reserve that financial institutions can work with legal marijuana trade safely
- Ambiguities, a lack of comprehensive guidance, the current misalignment between state and federal marijuana law, and onerous reporting requirements have meant numerous banks across the U.S. have denied access to the legal marijuana industry, creating numerous process and security issues (e.g., large amounts of cash)
- “De-scheduling” of marijuana under CSA and Marijuana Businesses Access to Banking Act of 2015 can change current situation in a meaningful way whereby banks will feel safer in providing services to the legal marijuana trade

Marijuana and Taxes

- *James v. United States (1961)* -- illegal income is taxable
- Internal Revenue Code Section 280E
 - “No deduction or credit shall be allowed for any amount paid or incurred during the taxable year in carrying on any trade or business if such trade or business (or the activities which comprise such trade or business) consists of trafficking in controlled substances (within the meaning of schedule I and II of [CSA]) which is prohibited by Federal law or the law of any State in which such trade or business is conducted”
 - Internal Revenue Service (IRS) must enforce Section 280E due to the federal-level status of marijuana
 - No important deductions for marijuana trade (e.g., rent, employee salaries, utility bills)
 - Large taxable income -- some marijuana businesses have paid effective tax rates of 50-70 percent
 - Accountant stated “you find all these weird little strategies that people use to parse definitions”
 - Generally, industry wants to be legitimized and pay taxes similar to other businesses
- IRS Guidance ILM 201504011 attempts to assist marijuana businesses in determining the cost of goods sold
- De-scheduling under CSA represents a feasible alternative to marijuana businesses paying high tax rates

Conclusion

- Marijuana legalization trend is strong, and it is anticipated that more states will continue to legalize, decriminalize, and actively regulate marijuana trade -- federal-level reform is more challenging
- Appropriate marijuana regulation is critically important due to:
 - Widespread use and consumer safety (e.g., typical risks associated with black market)
 - Social costs (e.g., millions of Americans have never been arrested of any criminal offense except marijuana possession)
 - Business implications (e.g., banking and taxes)
 - Government resources (e.g., nationwide legalization could save government billions annually in expenditure on enforcement of prohibition)
- The future of marijuana in the U.S. will depend upon:
 - Success of ongoing reform efforts
 - Public opinion
 - Politics, including the approach adopted by the Trump Administration

Thank You

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