



THE LEGALIZATION OF MARIJUANA AND FINANCIAL ACCOUNTABILITY FOR AMERICA'S NEXT REGULATED CONSUMER PRODUCT

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Twenty-two states and the District of Columbia have legalized the use of medical marijuana to date. Earlier this year, the State of Washington and Colorado legalized the recreational use of cannabis for adults within their jurisdictions.

Polls suggest that a sizeable percentage of our population believes this is, and should be, just the beginning of a nationwide wave of marijuana legalization. However, deeper research into the issue of marijuana legalization indicates that the vast majority of opinion-holders are unaware of the complexities associated with making this newly legalized industry financially accountable -- to the regulators who are responsible for its oversight, as well as to the public at large.

Electronic Funds Transfer (EFT) is a key tool for achieving financial accountability. Regulators vested with the responsibility to oversee the new marijuana industry would do well to require EFT between all the tiers, *i.e.*, growers and processors, distributors, and retail dispensaries, so that regulators can receive reports from the EFT providers and better audit the legitimacy and compliance of industry members. It works well for the heavily-regulated alcohol industry, and has the potential to deliver the same positive benefits for the growing cannabis market.

WHY FINANCIAL ACCOUNTABILITY IS IMPORTANT

Financial accountability is key to any regulated industry. Regulators, and the public they seek to protect, require accurate information about all relevant transactions involving highly-regulated products.

Those transactions range from the producer, through the processor, down the distribution chain, and all the over to the retailer's ultimate sale of the product to an end-use consumer. Honest, reliable and verifiable transaction data help assure legitimacy, safeguard product and industry member integrity, and afford an accurate basis in real-time from which to collect taxes and monitor industry behavior.

A big challenge for holding America's expanding medical and recreational marijuana industries accountable is that most of their transactions remain on a cash-only basis. Because cannabis remains illegal in the eyes of the federal government, many banks and financial institutions refuse to do business with marijuana-related ventures. The federal government is primarily responsible for regulating banks and financial institutions in this country, and bankers are

understandably concerned about the risk of federal prosecution or compliance actions based on alleged participation in illegal drug activities.

STEPS FORWARD TOWARD ACCOUNTABILITY

On February 14, 2014, the U.S. Treasury Department's Financial Crimes Enforcement Network (FinCEN), working with the U.S. Department of Justice, issued guidance for financial institutions seeking to provide services to cannabis-related businesses. FinCEN writes the rules and regulations that U.S. financial institutions, like banks, credit unions, and money services businesses, must follow to help protect the U.S. financial system from money laundering and terrorist finance. FinCEN also has the civil power to enforce these rules and penalize offenders.

The stated goal of the new federal guidelines is to promote "greater financial transparency in the marijuana industry and mitigate the dangers associated with conducting an all-cash business." According to its February 14th press release, FinCEN expects financial institutions to perform thorough customer due diligence on marijuana businesses and file reports that highlight information that is particularly valuable to law enforcement. How this translates at the street level is far from clear.

Trying to create an infrastructure to bridge that federal-state gap, Colorado Governor John Hickenlooper signed into law this summer state legislation that allows legal marijuana businesses in Colorado to create marijuana financial services cooperatives, referred to in the statute as "cannabis credit co-ops." The law is intended to bring financial accountability to Colorado's expanding cannabis commerce.

These steps represent incremental progress towards financial accountability. The ultimate goal should be an industry environment where all relevant players can utilize EFT to document, as well as implement, their business transactions.

ESCALATING ECONOMICS

Why take these steps? According to the latest data from the Colorado Department of Revenue, the state's legal recreational marijuana industry generated more than \$6.5 million in taxes, license funds and fees just in July of 2014. A study by the Marijuana Policy Group¹ that was commissioned by the Colorado Department of Revenue and issued in June of 2014 estimates that the total demand by the legal citizens of Colorado for marijuana in the year 2014 will exceed 121 metric tons. Projections for sales of over \$1 billion annually are becoming the norm.

Though lagging behind Colorado in implementing its legal marijuana retail system, the State of Washington is two months into its recreational cannabis experiment, and so far the commercialization of marijuana appears to be an economic success. After initiating sales at the

¹ The Marijuana Policy Group (MPG) was formed in 2014 as a collaborative effort between the University of Colorado Boulder Business Research Division (www.leeds.colorado.edu/brd) and BBC Research & Consulting (www.bbcresearch.com) in Denver. Both entities have offered custom economic, market, financial and policy research and consulting services for over 40 years.

beginning of July, Washington State's marijuana market has seen \$3.8 million in sales in the first month, and raised right around \$1 million in new tax revenue for the state. Those figures represent the initial sales of only 18 stores across the state; while approximately forty stores have been licensed by Washington State for marijuana sales, some were still organizing by the end of July, while others were ready for business but had to remain closed due to cannabis shortages.

The legal pot business in the United States, including both the newly legalized retail operations in Washington and Colorado and the medical-marijuana use now allowed in California and 22 other states, is expected to grow this year to \$2.6 billion from \$1.5 billion in 2013, according to the ArcView Group, a San Francisco-based marijuana research and investment firm. In five years, that number could swell to more than \$10 billion.

CONCLUSION

A new survey from online polling data company CivicScience shows that a majority of American adults continue to support marijuana legalization in the United States, and that support appears to be growing. The CivicScience survey, released in late August of 2014, asked more than 450,000 U.S. adults over the last two years this question: *"Would you support or oppose a law in your state that would legalize, tax, and regulate marijuana like alcohol?"*

Fifty-eight percent (58%) of respondents said they support marijuana legalization -- with 39 percent (39%) saying they "strongly support" and 19 percent (19%) saying they "somewhat support" reformed marijuana laws in their states. Thirty-five percent (35%) oppose legalization of marijuana -- with 29 percent (29%) "strongly" opposing and 6 percent (6%) "somewhat" opposing laws that would regulate marijuana like alcohol. Seven percent (7%) of respondents had no opinion on the issue.

CivicScience then analyzed the data from just the last three months of responses -- from May to August of 2014 -- and identified an increase in support, and decrease in opposition, to the regulation of marijuana like alcohol. Of those who responded most recently, 61 percent (61%) said they strongly or somewhat support marijuana legalization, while only 30 percent (30%) were opposed.

If these data suggest that legalization is inescapable, then the need for financial accountability becomes all the more relevant, and imperative. Creating an environment where cannabis industry members have the ability to use EFT for all their transactions ultimately will serve regulators, businesses and the public.