

When State and Federal Laws Differ

by [Steve Brown](#)

States around the country are discussing the legalization of marijuana and the inevitable quandary that follows. Colorado and Washington are the first states in the US to legalize pot in small amounts for personal recreational use and there are already 20 states, plus the District of Columbia, that already allow the use of medical marijuana. Whether controlled by the state Liquor Control Board, the Department of Revenue or other agency, states see this as a way to raise much needed revenue. Even the Feds through the US Justice Department said on Aug. 29 that they will not try to stop states from legalizing recreational use, so long as there are strong enforcement systems in place.

Thus, an agricultural and ancillary services mini-boom began in these states, but it also added a burden to the financial system. The problem for growers and bankers occurs because marijuana remains illegal under federal law. Since federally insured financial institutions that take deposits, process credit cards or do any other kind of business with the pot trade could face federal drug racketeering charges, they avoid these customers like the plague. In fact, in 2011, American Express said it would no longer process financial transactions for medical marijuana due to fear of prosecution. Shortly after that, the DOJ gave banks an explicit directive regarding medical marijuana, indicating that any institution that engaged in transactions of such activities would be in violation of federal money laundering statutes and other federal financing laws.

This has left growers and sellers in a position of having to operate on a cash-only basis or push these activities to other digital cash channels perhaps. As business has expanded in CO and WA, there is, of course, a need for financial services to assist the licensed legal enterprises taking part in the trade. Even Congress has gotten involved and a bill has been proposed that would allow federally regulated financial institutions to service their states' sanctioned growers. Getting a bill of any variety through Congress is likely to be a challenge and this one could be particularly sticky since state and federal laws don't mesh very well together, so the states are asking federal banking regulators to issue a moratorium. We don't see that happening as it runs counter to Federal laws, but it is interesting to watch nonetheless.

Now enter the next oddity in this customer seeking banking services saga. The very same DOJ deputy attorney general who cautioned institutions in regard to the American Express actions of 2011 has now stated that the Justice Department and federal banking regulators will help clear the way for financial institutions to transact business with the legitimate marijuana industry without fear of prosecution. We imagine banks would like to see that in writing before proceeding.

For the states, anticipated tax revenues from the marijuana business are significant. Some estimates are as high as \$2B over 5Ys just for CO and WA. The quandary for those states though is while it is easy to pass new laws that clash with federal ones, bankers have to operate in both worlds so must support only the most conservative approach. We wonder how that states plan to collect taxes in a cash-only business outside the banking system if things stay the way they are now and are sure those numbers will likely be much lower as a result.

No matter your position on the legalization of marijuana, it is interesting to see how things unfold particularly as it relates to the banking business. We hope you enjoyed the discussion.

BANK NEWS

M&A

One PacificCoast Bank (\$280mm, CA) has received Fed approval to acquire Albina Community Bank (\$121mm, OR) for an undisclosed sum.

Huge Competition

PayPal announced it has purchased Braintree for \$800mm, as it launches more aggressively into mobile payments. Braintree processed \$12B in payments this year and has 40mm customers and does business with merchants in 40 countries.

Less Debt

The ABA reports consumers continue to pay down credit card debt, driving it down 22% since 2008.

Infusion Needed

The FHA reportedly has asked for a \$1B infusion from the Treasury Department by the end of this month to shore up the agency due to losses in its troubled reverse mortgage program.

Penalty

Citibank agreed to pay FHLMC \$395mm as part of a settlement related to 3.7mm defective mortgages it sold between 2002 and 2012.

Real Time Payments

Cleveland Fed President Pinalto said the Fed should move to a "near real time" payments system to meet demand from businesses and consumers.

New Bill

The new \$100 bill features color changing ink, a 3-D security ribbon and more texture on Ben Franklin's collar. The bills enter circulation on Oct. 8 and the Fed expects to issue 2.5B of them this year.

Mobile Strength

An SAP survey finds 52% of consumers in 17 countries surveyed have made a bank transfer on a mobile device, more than 50% have used mobile to pay a bill and 48% have set up new accounts this way.

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