

# Proposed U.S. Federal Cannabis Legislation: Updated Briefing on the SAFE Banking Act and STATES Act

## VISUAL MEMORANDUM

April 16, 2019



© 2019 Davis Polk & Wardwell LLP | 450 Lexington Avenue | New York, NY 10017

This communication, which we believe may be of interest to our clients and friends of the firm, is for general information only. It is not a full analysis of the matters presented and should not be relied upon as legal advice. This may be considered attorney advertising in some jurisdictions. Please refer to the firm's [privacy policy](#) for further details.

**Davis Polk**

Davis Polk & Wardwell LLP

# Contents

---

1.	Introduction.....	2
2.	Challenges under the Existing Legal Framework.....	3
3.	The SAFE Banking Act.....	11
4.	The STATES Act.....	20
5.	Comparing the SAFE Banking Act and STATES Act.....	24
6.	Davis Polk Contacts.....	29

---

### Readers' Guide

Those who are familiar with the topic might skip directly to page 24 where there is a chart comparing the SAFE Banking Act and the STATES Act.

---

# Introduction

---

- This memorandum provides a basic briefing on two bills:
  - The [Secure and Fair Enforcement Banking Act](#) (the [SAFE Banking Act](#)); and
  - The [Strengthening the Tenth Amendment Through Entrusting States Act](#) (the [STATES Act](#)).
- Neither bill would federally legalize cannabis or deschedule cannabis from Schedule 1 of the [Controlled Substances Act \(CSA\)](#).
- Instead, the bills would permit depository institutions, in the case of the [SAFE Banking Act](#), or financial institutions, in the case of the [STATES Act](#), to provide financial services to cannabis-related businesses ([CRBs](#)) that comply with state laws regulating legalized cannabis-related activity.
- Both bills would benefit from changes that would take into account a broader range of financial services and the practical difficulties in conducting diligence in the financial sector.
- This memorandum, originally published on February 8, 2019, has been updated following the reintroduction of:
  - the [SAFE Banking Act](#) on March 7, 2019, which was amended and approved by the House Committee on Financial Services ([HFSC](#)) on March 28, 2019; and
  - the [STATES Act](#) on April 4, 2019.
- We will continue to update the memorandum as the bills make their way through Congress.

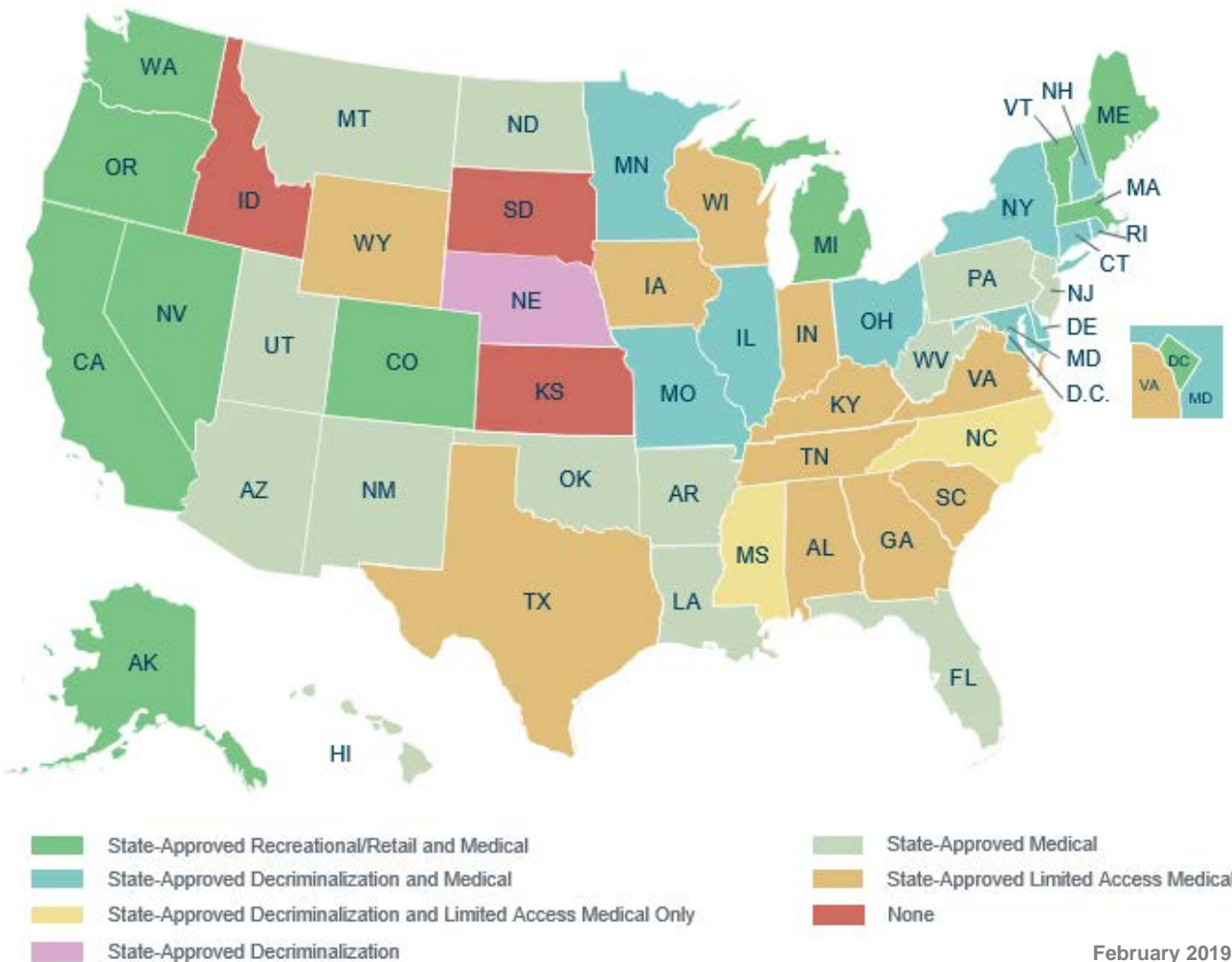
# Overview

---

- **Changing State Laws and Static Federal Laws Related to Cannabis Are Creating an Unworkable Situation.**
  - An increasing number of states are legalizing medical and/or recreational cannabis.
  - Canada legalized recreational cannabis, effective October 17, 2018.
  - Cannabis remains a Schedule 1 drug under U.S. Federal law, and proceeds from related activities remain subject to U.S. anti-money laundering (AML) laws, such as the Money Laundering Control Act (MLCA).
  - Given the uncertain enforcement and heavy penalties, the vast majority of financial institutions consciously avoid knowingly providing financial services to U.S. CRBs.
    - Considerable uncertainty persists for how financial institutions should approach Canadian CRBs.
  - For an overview of the current state of play regarding the conflict between Federal law and state law with respect to the U.S. cannabis sector, and its implications for financial institutions, see Margaret Tahyar & Jeanine McGuinness, *Financial Services and the US Cannabis Sector*, Practical Law (Apr. 2019) [\[Link\]](#).
- **In the Meantime, the Cannabis Sector is Transitioning from a Mom-and-Pop Sector into Big Business, with Major Implications for Investment and Compliance.**
  - For commentary on the implications of the current versions of the SAFE Banking Act and the STATES Act for the cannabis sector's transformation, see pages 26–27.

# CHALLENGES UNDER THE EXISTING LEGAL FRAMEWORK

## The Map



Source: Committee Memorandum for the HFSC Hearing (citing a Congressional Research Service presentation of data from the National Conference of State Legislatures)

This map comes from the committee memorandum submitted for the February 13, 2019 hearing entitled “Challenges and Solutions: Access to Banking Services for Cannabis-Related Businesses,” convened by an HFSC subcommittee ([HFSC Hearing](#)).

The committee memorandum uses:

- “**limited-access medical**” to mean low-tetrahydrocannabinol (THC) cannabis or cannabidiol (CBD) oil
- “**state-approved**” to mean (i) legalization of recreational and/or medical cannabis and/or (ii) decriminalization of cannabis possession in small amounts
- “**decriminalization**” to mean withdrawal of criminal penalties for cannabis possession in small amounts.

According to this taxonomy:

- **47 states** have legalized or decriminalized some form of cannabis
- **33 states** have legalized medical cannabis (not including limited access)
- **10 states** have legalized recreational cannabis
- **Washington, D.C.** has legalized medical and recreational cannabis

## Constraints on Federal Agencies

---

- **Federal Agencies Cannot Fix the Problem.**

- Federal banking agencies must operate within the bounds of Federal law and are unlikely to believe they have authority to lift barriers for financial institutions to provide financial services to CRBs.

“ I don't believe this is a failure of the regulators. I want to defend the regulators on this issue. . . . This is something where there is a conflict between federal and state law that we and the regulators have no way of dealing with. ”

–*Secretary Treasury Steven Mnuchin, before the House Appropriations Committee (Apr. 2019)*

- Relying on existing Federal guidance remains perilous.
  - Federal agency guidance, such as the guidance issued by the Financial Crimes Enforcement Network (FinCEN) in 2014 (FinCEN Guidance), is nonbinding and revocable, as seen with then-Attorney General Jeff Session's rescission of the Cole Memoranda issued in 2013 and 2014.
  - Even before rescission, the Cole Memoranda merely articulated a set of advisory priorities. Neither Cole Memorandum purported to alter Federal law or the Department of Justice's (DOJ) prosecutorial authority.

## CHALLENGES UNDER THE EXISTING LEGAL FRAMEWORK

# Cash-related Concerns

---

- **Challenges Arise from Large Volumes of Cash.**

- The vast majority of financial institutions are unwilling to directly assist CRBs given the threat of federal prosecutorial or regulatory penalties, exacerbating the cannabis sector’s dependence on cash.

““ It is ironic that we are forcing one sector of the economy to be cash-based at the same time that the digital transformation is leading in the opposite direction. ””

–Margaret Tahyar, in *Bloomberg Law* (Feb. 2019)

- The cash-intensive nature of the cannabis sector creates risks to **public safety** and obstacles to **tax collection**.

““ Lack of access to banking services that are taken for granted by other legal businesses—opening accounts, writing checks, accepting credit cards, transferring money—forces cannabis businesses to deal in large amounts of cash, which makes them targets for assaults and puts the general public in danger. ””

–John Chiang, in a report by the California State Treasurer’s Cannabis Banking Working Group (Nov. 2017)

““ I assure you that we don’t want bags of cash. We want to make sure we can collect our necessary taxes and other things in other than cash. ””

–Secretary Treasury Steven Mnuchin, before the HFSC (Feb. 2018)

## Regulation of Hemp

---

- **Open Questions Exist Regarding the New Regulatory Structure for Hemp.**

- The new regulatory structure for hemp under the 2018 Farm Bill has yet to be implemented.
- Enacted in December 2018, the 2018 Farm Bill legalized the production of industrial hemp for purposes beyond research by excluding hemp from the CSA’s definition of “marihuana.”
- Although the 2018 Farm Bill generally protects hemp-related activities, hemp is also derived from the cannabis plant, which raises questions on how to produce hemp consistent with the CSA’s restrictions on cannabis.
  - The Department of Agriculture, the Federal agency responsible for implementing the 2018 Farm Bill, has yet to publish implementing regulations, including the requirements that state plans for producing hemp must meet.
- Approval from the Food and Drug Administration may also be required for certain hemp-based or cannabinoid-based products.



# Ancillary Businesses

- **Avoiding Indirect Dealings with CRBs Is Becoming More Challenging for Financial Institutions.**

- How should financial institutions make decisions around indirect business—conducting business with parties that serve the U.S. cannabis sector? What, if any, diligence must they conduct in these circumstances?
  - See Loren Picard, *You already bank the pot industry. You just don't know it*, American Banker (June 2017).
- Testimony on behalf of community banking and credit unions at the HFSC Hearing, emphasized this issue:

“ “ What is less well appreciated are the risks and burdens of serving, or merely monitoring in the course of our due diligence, the numerous [indirect cannabis-related businesses](#). . . . Consider the plumbers, electricians, internet service providers, and accountants, . . . whose customer base includes cannabis-related businesses. These businesses are also drawn into the net, as is any business that, [knowingly or unknowingly](#), derives any revenues from a cannabis business. As a senior official from the Washington State Department of Financial Institutions recently told me, [‘banks may not know’](#) that they are serving cannabis-related businesses. ” ”

–Gregory S. Deckard, on behalf of the Independent Community Bankers of America (Feb. 13, 2019)

“ “ [Indirect connections to marijuana revenues](#) are hard, if not impossible, for financial institutions to both identify and avoid. [L]ike almost every other business, the [cannabis] industry is dependent upon any number of vendors and suppliers to function. These are [everyday businesses](#) like the printing company[,] the office supply company[,] the housekeeping crew or landlord[,] and even the utility company. . . . Under the existing status quo, a credit union that does business with any one of these [indirectly affiliated entities](#) could [unknowingly](#) risk violating the federal Controlled Substance Act, . . . Bank Secrecy Act, . . . among other federal statutes. ” ”

–Rachel Pross, on behalf of the Credit Union National Association (Feb. 13, 2019)

# Calls for Congressional Reform at the Federal Level

---

- Calls for federal legislative clarity for the financial sector on cannabis-related banking have been made by members of Congress and government officials in both political parties, including:
  - [Representative Maxine Waters](#), the Chairwoman of the HFSC, said, “[I]t’s inevitable we are going to have to talk about” this issue (Nov. 2018).
  - [Ten senators](#), including [Kirsten Gillibrand](#), [Elizabeth Warren](#), [Bernard Sanders](#), and [Cory Booker](#), stated in a letter to FinCEN: “Locking [direct and indirect businesses such as] lawyers, landlords, plumbers, electricians, security companies, and the like out of the nation’s banking and finance systems serves no one’s interest” (Dec. 2016).
  - [Attorney General William Barr](#) said, “[I]f states continue to pass these laws [legalizing cannabis], are we going to continue to forebear in those new states[?] I would like Congress to address this issue” (Apr. 2019).
  - [Treasury Secretary Steven Mnuchin](#) said, “The problem is there a conflict between the federal law and the state law. . . . There is not a Treasury solution to this, there is not a regulator solution to this” (Apr. 2019).
  - [Federal Reserve Board Chairman Jerome Powell](#) said, “[F]inancial institutions—and their regulators and supervisors—are in a very difficult position here with marijuana being illegal under federal law and . . . legal under a growing number of state laws. It puts financial institutions in a very difficult place and puts the supervisors in a difficult place. It would be nice to have clarity on that supervisory relationship” (Feb. 2019).
  - [Comptroller of the Currency Joseph Otting](#) said, “Congress is going to have to act at the national level to legalize marijuana if they want those entities involved in that business to utilize the U.S. banking system” (Jan. 2019).
  - [Under Secretary for Terrorism and Financial Intelligence Sigal Mandelker](#) said, “[The FinCEN G]uidance remains in place . . . . [But] this is really something I think that Congress needs to look at, because nothing that we do can or does change . . . what is prohibited under federal law” (Mar. 2019).

## Momentum toward Banking Clarity

---

- Over the last six years, 237 members of Congress have sponsored a version of the SAFE Banking Act and/or the STATES Act that would address the provision of direct and indirect financial services to CRBs.
- In light of this legislative and regulatory momentum, Isaac Boltansky, Director of Policy Research for Compass Point Research & Trading, predicts the following:

“ We continue to believe that the next Congress is likely to provide cannabis banking clarity for operators in legal states. . . . Public perception and state pressure should combine to catalyze Congressional action on cannabis, but our sense is that the likeliest next step is banking clarity. We believe the odds of cannabis legalization in the next Congress stand at 25%, but peg the [odds of banking clarity](#) for cannabis companies operating in legal states at 75%.”

—Isaac Boltansky, Compass Point Research & Trading, LLC (Nov. 26, 2018)

# THE SAFE BANKING ACT

## Overview

---

- The **Secure and Fair Enforcement Banking Act** (the **SAFE Banking Act**)
  - Most recently introduced in the House (H.R. 1595) by Reps. Ed Perlmutter (D-CO), Denny Heck (D-WA), Steve Stivers (R-OH), and Warren Davidson (R-OH) on March 7, 2019 and amended for a March 26 markup.
    - A version was also introduced in the Senate (S. 1200) by Sens. Jeff Merkley (D-OR) and Cory Gardner (R-CO).
  - Aims to improve public safety by expanding **financial services** (as defined below) to **cannabis-related legitimate businesses** and **service providers** and reducing the amount of cash at such businesses.
  - Provides a safe harbor from Federal banking regulators taking certain actions against depository institutions solely for providing financial services to cannabis-related legitimate businesses or service providers.
  - Provides that proceeds of a transaction conducted by a cannabis-related legitimate business or service provider shall not be considered proceeds of an unlawful activity under the MLCA solely because the transaction was conducted by such business.
  - Provides certain protections from (i) liability under any Federal law for depository institutions and insurers that provide financial services to cannabis-related legitimate businesses or service providers, and (ii) forfeiture of certain collateral for depository institutions that provide financial services to such businesses.
  - Requires financial institutions to comply with FinCEN's guidance when filing suspicious activity reports (**SARs**) related to cannabis-related legitimate businesses and service providers.
  - Requires the Federal Financial Institutions Examination Council (**FFIEC**) to issue guidance and examination procedures.
  - Requires the Federal banking regulators and Government Accountability Office (**GAO**) to submit reports and recommendations, such as on diversity and inclusion.

# THE SAFE BANKING ACT

## Definitions

---

- The SAFE Banking Act covers **depository institutions** that offer a **financial service** to cannabis-related legitimate businesses or service providers.
  - “**Depository institution**” means a depository institution (as defined in 12 U.S.C. § 1813(c)); or a Federal credit union or State credit union (as defined in 12 U.S.C. § 1752).
  - “**Financial service**”
    - means a “**financial product or service**,” as defined in 12 U.S.C. § 5481;
    - plus the following additional products and services:
      - the “**business of insurance**,” which is cross-referenced to mean “the writing of insurance or the reinsuring of risks by an insurer” as well as all necessary acts and related activities;
      - whether performed directly or indirectly, **functions related to payments or funds**, where such payments or funds are made or transferred by any means (e.g., payment cards, accounts, checks, or electronic funds transfers);
      - acting as a **money transmitting business** which directly or indirectly makes use of a depository institution in connection with effectuating or facilitating a payment for a cannabis-related legitimate business or service provider in compliance with 31 U.S.C. § 5330, and applicable State law; and
      - acting as an **armored car service** for processing and depositing with a depository institution or the Federal Reserve Board with respect to any monetary instruments.

### **financial product or service**

The term comes from the consumer provisions of the Dodd-Frank Act establishing the Consumer Financial Protection Bureau (**CFPB**).

- **Definition of “Financial Service”**

- The SAFE Banking Act’s definition of “financial service” relies on a cross-reference to “financial product or service” from Title X of the Dodd-Frank Act, which focuses on the consumer protection context and establishes the CFPB’s jurisdiction.
- Title X’s definition of “financial product or service” excludes capital markets and wholesale activities, such as underwriting, broker-dealer activities, asset management, and custody.
  - For our view that relying on the consumer definitions is a poor choice, see our blog post: Margaret Tahyar & Jeanine McGuinness, *HFSC Advances the SAFE Banking Act to the Full House*, Financial Regulatory Reform (Apr. 2019) [\[Link\]](#).

## THE SAFE BANKING ACT

# Definitions

---

- The SAFE Banking Act covers depository institutions that offer a financial service to **cannabis-related legitimate businesses** or **service providers**.
  - “**Cannabis-related legitimate business**” means a manufacturer, producer, or any person or company that:
    - A. engages in any activity described in subparagraph (B) pursuant to a law established by a State or a political subdivision of a State, as determined by such State or political subdivision; and
    - B. participates in any business or organized activity that involves handling cannabis or **cannabis products**, including cultivating, producing, manufacturing, selling, transporting, displaying, dispensing, distributing, or purchasing cannabis or cannabis products.
  - “**Service provider**”
    - A. means a business, organization, or other person that (i) sells goods or services to a cannabis-related legitimate business; or (ii) provides any business services, including the sale or lease of real or any other property, legal or other licensed services, or any other ancillary service, relating to cannabis; and
    - B. is not a cannabis-related legitimate business.
  - “**Cannabis product**” means any article containing cannabis, including articles that are concentrates, edibles, tinctures, cannabis-infused products, or topicals.

# Safe Harbor for Depository Institutions

- The SAFE Banking Act provides a **safe harbor** for **depository institutions**, which would prohibit a **Federal banking regulator** from:
  - Terminating or limiting a depository institution's deposit insurance, or taking any other adverse action against a depository institution solely because it provides financial services to cannabis-related legitimate businesses or service providers operating pursuant to State law
  - Prohibiting or penalizing a depository institution for or discouraging a depository institution from providing financial services to such businesses or to a State exercising jurisdiction over such businesses
  - Recommending or incentivizing a depository institution not to offer financial services to certain account holders involved in such businesses
  - Taking adverse or corrective actions on loans to such businesses, to certain persons involved in such businesses, or to owners or operators of real estate or equipment leased to such businesses solely because such businesses are cannabis-related businesses or service providers
  - Prohibiting or penalizing a depository institution (**or entity performing services for the depository institution**) for or discouraging such institution from engaging in a financial service for cannabis-related legitimate businesses or service providers.
- The safe harbor also extends to institutions applying for **depository institution charters**.

## Federal banking regulators

- Federal Reserve Board
- CFPB
- Federal Deposit Insurance Corporation (FDIC)
- Office of the Comptroller of the Currency (OCC)
- National Credit Union Administration (NCUA)
- Treasury Department
- FinCEN
- Office of Foreign Assets Control (OFAC)
- Any Federal agency or department that regulates banking or financial services, as determined by the Treasury Secretary

The safe harbor would not apply to prosecution by DOJ.




# Protections for Ancillary Businesses

---

## Protections for Ancillary Businesses

- For the purposes of the MLCA and all other provisions of Federal law, the **proceeds** from a transaction conducted by a cannabis-related legitimate business or service provider shall not be considered proceeds from an unlawful activity solely because the transaction was conducted by a cannabis-related legitimate business or service provider, as applicable.



Notably, this provision is *not* limited to any particular institution and appears to apply to depository institutions, other financial institutions, and even CRBs.

# Protections under Federal Law

---

- **Protections for Depository Institutions**

- **General Protections.** A [depository institution](#), [entity performing a financial service for or in association with a depository institution](#), or [insurer](#) that provides financial services to a cannabis-related legitimate business or service provider pursuant to State or local law within a jurisdiction that has legalized cannabis-related activity may not be held liable [pursuant to any Federal law or regulations](#):
  - solely for providing such financial services pursuant to State or local law or regulation; or
  - for further investing any income derived from the financial services.
- **Forfeiture Protections.** A [depository institution](#) that has a legal interest in the collateral for a loan made to an owner or operator of a cannabis-related legitimate business or service provider, or to an owner or operator of real estate or equipment that is leased or sold to a cannabis-related legitimate business or service provider, shall not be subject to [criminal, civil, or administrative forfeiture](#) of that legal interest [pursuant to any Federal law](#) for providing the loan or other financial services solely because the collateral is owned by a cannabis-related business or service provider.

- **Protections for Federal Reserve Banks**

- The [general](#) and [forfeiture](#) protections above also extend to [Federal Reserve Banks](#) that provide services to a depository institution that provides a financial service to a cannabis-related legitimate business or service provider pursuant to State or local law within a State or local jurisdiction that has legalized cannabis-related activity.

# Obligations for Financial Institutions and Federal Regulators

---

## No Obligation to Provide Financial Services

- The SAFE Banking Act does not compel a [depository institution](#), [entity performing a financial service for or in association with a depository institution](#), or [insurer](#) to provide financial services to cannabis-related legitimate businesses or service providers.

## Modified Reporting Obligations for Financial Institutions

- The SAFE Banking Act amends the Bank Secrecy Act's ([BSA](#)) requirements for filing SARs.
  - Requires financial institutions that report suspicious transactions to comply with appropriate guidance issued by FinCEN if the reason for the SAR relates to cannabis-related legitimate businesses or service providers
  - Requires the Treasury Secretary to ensure that guidance issued by FinCEN:
    - Is consistent with the SAFE Banking Act's purpose and intent; and
    - Does not [significantly](#) inhibit financial institutions from providing services to cannabis-related legitimate businesses or service providers in State or local jurisdictions that permit such cannabis-related activity.

## Guidance and Examination Procedures

- Within 180 days after the SAFE Banking Act's enactment, the FFIEC must develop [uniform guidance and examination procedures](#) for [depository institutions](#) that provide financial services to cannabis-related legitimate businesses and service providers.

# Other: Government Reports and Recommendations

---

The SAFE Banking Act requires the following studies and reports:

## Annual Diversity and Inclusion Report

- Federal banking regulators shall issue an annual report to Congress containing:
  - information and data on the availability of access to financial services for [minority-owned](#) and [women-owned](#) cannabis-related legitimate businesses; and
  - any regulatory or legislative recommendations for expanding access to financial services for [minority-owned](#) and [women-owned](#) cannabis-related legitimate businesses.

## GAO Study on Diversity and Inclusion

- The Comptroller General of the United States shall:
  - carry out a study on the barriers to marketplace entry and access to financial services for potential and existing [minority-owned](#) and [women-owned](#) cannabis-related legitimate businesses; and
  - issue a report to Congress, containing (1) all findings and determinations made in carrying out the study; and (2) any regulatory or legislative recommendations for addressing the above barriers and access issues

## GAO Study on Effectiveness of Certain Reports on Finding Certain Persons

- Within 2 years after the SAFE Banking Act's enactment, the Comptroller General of the United States shall carry out a study on the effectiveness of reports on suspicious transactions at finding individuals or organizations suspected or known to be engaged with [transnational criminal organizations](#) and whether any such engagement exists in States that allow certain cannabis-related activities.

### The **Strengthening the Tenth Amendment Through Entrusting States Act** (the **STATES Act**)

- The STATES Act was most recently introduced on April 4, 2019 by:
  - Senators Elizabeth Warren (D-MA) and Cory Gardner (R-CO) in the Senate (S. 1028); and
  - Representatives Earl Blumenauer (D-OR) and David Joyce (R-OH) in the House (H.R. 2093).
- The purpose of the bill is to **amend the CSA** to create a new rule regarding the CSA’s application to marijuana.
- The bill provides that the CSA generally would not apply to marijuana-related conduct that is legal under State law.
- The bill would protect the financial services sector by providing that:
  - The proceeds of any marijuana transaction conducted in compliance with State law would not be deemed the proceeds of an unlawful transaction under the **MLCA** or **any other provision of law**; and
  - Marijuana-related conduct that is legal under State law would not serve as a basis for criminal or civil asset forfeiture.
- **President Donald Trump** said in June 2018 that he “probably will end up supporting” the bill.
- **Attorney General William Barr** said in April 2019, “I’ve just circulated [the bill] to the [DOJ] for comment. . . . I’d much rather that approach . . . the approach taken by the STATES Act . . . than where we currently are.”

# Amendment to the CSA; Protections for Financial Institutions

---

- The STATES Act would amend the CSA by inserting a [new section \(710\)](#) that specifically governs marijuana-related activities:
  - Renders inapplicable CSA prohibitions on the manufacture, production, possession, distribution, dispensation, administration, or delivery of marijuana where such activity complies with:
    - (a) [State law](#) or (b) [tribal law](#),
    - [Subject to exceptions under Section 710\(c\) and \(d\)](#) (see page 22).
- Of particular importance to financial institutions is the STATES Act’s new rule of construction, which provides that proceeds from CRBs operating in compliance with the STATES Act will not trigger prosecution under the MLCA.
  - [Marijuana-related activity](#) in compliance with State law and the STATES Act shall not:
    - Be unlawful;
    - Constitute “trafficking” of a controlled substance within the meaning of the CSA (21 U.S.C. § 841) or any other provision; or
    - Constitute the basis for criminal forfeiture under the CSA (21 U.S.C. § 881) or civil forfeiture under 18 U.S.C. § 981.
  - [Proceeds from transactions](#) involving marijuana-related activity in compliance with State law and the STATES Act shall not:
    - Be deemed the proceeds of an unlawful transaction under the MLCA or any other law.

# Exceptions that Trigger CSA and MLCA Violations

---

- The STATES Act would *not* protect financial institutions from prosecution under the MLCA if the financial institution provides services to a CRB that participates in certain cannabis-related activity, including, for example:
  - distribution to persons under 21 years old (other than distribution of medical marijuana in compliance with State law) (21 U.S.C. § 859) ([Section 710\(c\)\(1\) and \(4\)](#))
  - violating the CSA with other controlled substances ([Section 710\(d\)\(1\)](#))
  - conducting marijuana-related activities that violate State or tribal law ([Section 710\(d\)\(2\)](#))
  - employing or hiring a person under 18 years old for the manufacture, production, possession, distribution, dispensation, administration, or delivery of marijuana ([Section 710\(d\)\(3\)](#)).
- As a [practical matter](#) for due diligence, it may be difficult for a financial institution to determine whether a CRB complies with the provisions under [Section 710\(c\)–\(d\)](#).

# Other: Government Study and Report

---

## GAO Study on Effects of Cannabis Legalization on Traffic Safety

- The STATES Act requires the Comptroller General of the United States to conduct a study on the effects of cannabis legalization on traffic safety, which includes a detailed assessment of:
  - traffic crashes, fatalities, and injuries in States that have legalized cannabis use, including whether States are able to accurately evaluate cannabis impairment in those incidents;
  - actions taken by the States that have legalized cannabis to address cannabis-impaired driving, including any related challenges;
  - testing standards used by States that have legalized cannabis to evaluate cannabis impairment in traffic crashes, fatalities, and injuries, including any scientific methods used to determine impairment and analyze data; and
  - Federal initiatives aiming to assist States that have legalized cannabis with traffic safety, including recommendations for policies and programs to be carried out by the National Highway Traffic Safety Administration.
- Within 1 year after the STATES Act’s enactment, the Comptroller General of the United States must submit a report on the results of the study to the appropriate congressional committees.



# COMPARING THE SAFE BANKING ACT AND STATES ACT

## Overview

	Pros	Cons
<b>SAFE Banking Act</b>	<ul style="list-style-type: none"> <li>• Addresses issues specific to the banking sector               <ul style="list-style-type: none"> <li>– Expressly protects depository institutions and insurers</li> <li>– Bars actions by Federal banking regulators</li> <li>– Amends the BSA and requires FinCEN to have in place guidance consistent with the act</li> <li>– Instructs the FFIEC to issue guidance and examination procedures</li> </ul> </li> <li>• Provides that proceeds of a transaction conducted by a cannabis-related legitimate business or service provider shall not be considered proceeds of an unlawful activity under the MLCA solely because the transaction was conducted by a cannabis-related legitimate business or service providers</li> </ul>	<ul style="list-style-type: none"> <li>• Does not amend the CSA</li> <li>• Limits certain protections mainly to depository institutions               <ul style="list-style-type: none"> <li>– Omits broker-dealers, underwriters, asset managers, and custodians</li> </ul> </li> <li>• Adopts Title X of the Dodd-Frank Act’s definition of “financial product or service,” which excludes key financial services</li> <li>• Only applies safe harbor to actions taken by Federal banking regulators, which do not include the DOJ</li> <li>• Relies on Federal agency guidance, which is revocable</li> <li>• Conditions protections on a CRB engaging in activities “pursuant to” State law</li> </ul>
<b>STATES Act</b>	<ul style="list-style-type: none"> <li>• Amends the CSA               <ul style="list-style-type: none"> <li>– Protects CRBs, in addition to service providers</li> <li>– Addresses indirect businesses</li> </ul> </li> <li>• Provides that proceeds from any transaction in compliance with State law and the STATES Act shall not be deemed to be the proceeds of an unlawful transaction or any other law</li> </ul>	<ul style="list-style-type: none"> <li>• Does not expressly reference the financial services sector               <ul style="list-style-type: none"> <li>– Offers no guidance for customer due diligence requirements and issues no directives to Federal agencies to do so</li> </ul> </li> <li>• Conditions protection on the CRB “acting in compliance with” State law</li> </ul>

# Approach to Removing Federal Barriers

---

- The SAFE Banking Act provides a **safe harbor** and other protections primarily for the banking sector.
  - The bill also delegates to Federal agencies the task of maintaining or developing guidance:
    - The Treasury Secretary must ensure that guidance on SARs issued by FinCEN comports with the bill's purpose and intent and does not significantly inhibit the provision of financial services to cannabis-related legitimate businesses or service providers.
    - The FFIEC must develop uniform guidance and examination procedures for depository institutions.
- The STATES Act **amends the CSA** so that certain cannabis-related activities that are lawful in the State jurisdiction no longer serve as a predicate offense for triggering prosecution under the MLCA.
  - The bill structurally changes the CSA:
    - Protects CRBs that comply with State laws unless certain amended CSA provisions are implicated.
  - The protections do not expressly reference the financial services sector:
    - But importantly, the bill includes a general rule of construction for recipients of proceeds from transactions conducted in compliance with the STATES Act.
    - It is unclear what actions Federal banking regulators should or may take (for example, how the bill would affect SAR obligations and diligence requirements).

## COMPARING THE SAFE BANKING ACT AND STATES ACT

# Breadth of Protection

---

- The SAFE Banking Act’s **safe harbor** and **forfeiture protections** focus on **depository institutions** that provide **financial services** consistent with the definition of “financial product or service” in Title X of the Dodd-Frank Act.
  - **Focus on Depository Institutions.** The protections do *not* explicitly protect broker-dealers, underwriters, asset managers, and custodians that rely on nonbank entities.
    - **However:**
      - The **protections from Federal liability** provision would also shield insurers and entities performing financial services for or in association with depository institutions, such as payment card companies and merchant service providers.
      - A new section on **treatment of proceeds** of cannabis-related legitimate businesses and service providers would extend beyond depository institutions to also cover other financial institutions and even CRBs.
  - **Cross-Reference to Title X.** Title X’s definition focuses on the consumer protection context and would exclude certain financial services to businesses, such as capital markets and wholesale activities.
    - See Margaret Tahyar & Jeanine McGuinness, *HFSC Advances the SAFE Banking Act to the Full House*, Financial Regulatory Reform (Apr. 2019) [[Link](#)].
  - Taken together, these two limitations prevent the SAFE Banking Act from covering financial service providers and financial services that would be vital to facilitating the U.S. cannabis sector’s transformation into big business.

## COMPARING THE SAFE BANKING ACT AND STATES ACT

# Breadth of Protection

---

- The STATES Act extends protection to [financial institutions](#) and [CRBs](#) generally since it would amend the CSA, and recipients of proceeds from transactions that comply with State law would not violate the MLCA.
  - Compared to the SAFE Banking Act, the STATES Act covers a broader range of financial service providers and financial services.
  - However, even if the cannabis-related activity complies with State law, prosecution under the CSA and MLCA could still occur if other activities targeted by [Section 710\(c\)–\(d\)](#) of the amended CSA were implicated, including:
    - distributing recreational marijuana to persons under 21 years of age;
    - employing persons under 18 years of age; and
    - creating substantial risk of harm to human life.

## COMPARING THE SAFE BANKING ACT AND STATES ACT

# Further Challenges

---

- Neither bill federally legalizes cannabis or preempts State law.
    - Financial institutions would need to observe State and local laws regulating cannabis, which would likely be complex within each State and varied across State jurisdictions.
  - The protections of both bills turn, at least to some extent, on a CRB’s compliance with State laws.
    - What happens when there is a nonmaterial lack of compliance with State laws?
    - The [SAFE Banking Act](#) only expressly shields depository institutions that bank CRBs engaged in specified activities “pursuant to” State law.
      - “pursuant to” is not defined, leaving uncertain the extent of compliance needed for a CRB to be a “cannabis-related legitimate business” and for its depository institution to be protected under the SAFE Banking Act.
    - The [STATES Act](#) only exempts proceeds from transactions with CRBs acting “in compliance with” State law.
      - “in compliance with” is not defined, leaving uncertain the extent of diligence needed for a CRB and its financial services provider to be protected under the STATES Act.
      - A CRB’s failure to comply with State law or Sections 710(c)–(d) of the amended CSA appears to reinstate liability under the CSA and MLCA for its financial services provider, irrespective of the rigor of due diligence.
    - Is the SAFE Banking Act’s “pursuant to” standard less stringent than the STATES Act’s “in compliance with” standard?
  - Though moving in the right direction of clarity and better than the status quo, *neither* the [SAFE Banking Act](#) *nor* the [STATES Act](#) currently goes far enough to alleviate concerns with providing financial services to CRBs.
-

# Davis Polk Contacts

---

CONTACTS	PHONE	EMAIL
John Banes	+1 212 450 4116	<a href="mailto:john.banes@davispolk.com">john.banes@davispolk.com</a>
Luigi L. De Ghenghi	+1 212 450 4296	<a href="mailto:luigi.deghenghi@davispolk.com">luigi.deghenghi@davispolk.com</a>
Randall D. Guynn	+1 212 450 4239	<a href="mailto:randall.guynn@davispolk.com">randall.guynn@davispolk.com</a>
John B. Reynolds, III	+1 202 962 7143	<a href="mailto:john.reynolds@davispolk.com">john.reynolds@davispolk.com</a>
Margaret E. Tahyar	+1 212 450 4379	<a href="mailto:margaret.tahyar@davispolk.com">margaret.tahyar@davispolk.com</a>
Jeanine P. McGuinness	+1 202 962 7150	<a href="mailto:jeanine.mcguinness@davispolk.com">jeanine.mcguinness@davispolk.com</a>
Will Schisa	+1 202 962 7129	<a href="mailto:will.schisa@davispolk.com">will.schisa@davispolk.com</a>

If you have any questions regarding the matters covered in this publication, please contact any of the lawyers listed above or your regular Davis Polk contact.