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The Magazine for Career-Minded Professionals in the Anti-Money Laundering Field

Defining  
marijuana-related  
businesses



**MRB MONITOR**  
By Enhanced Compliance Solutions, Inc.

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**W**hat is a marijuana-related business? The answer—or more accurately the definition—must be considered and discussed by all financial institutions. Regardless of an institution's general policy toward marijuana-related businesses (MRBs), poorly constructed policies and procedures are a high risk to any effective compliance program. Although supervised institutions are encouraged to “take a risk-based approach in assessing individual customer relationships, rather than declining to provide banking services to entire categories of customers without regard to the risks presented,”<sup>1</sup> most financial institutions' current position toward the emerging marijuana industry is to just say, “No.” However, most institutions have not clearly defined “marijuana-related business” and, therefore, may have unclear or incomplete policies and procedures that can lead to inconsistent interpretation and implementation.

This article shares a comprehensive and cohesive framework for defining MRBs and for sorting general categories of MRBs into three risk-based tiers. Financial institutions, regulators and policy-makers may find this framework useful when developing, revising or updating their marijuana-related policies and procedures.

### Why is this relevant?

The Controlled Substance Act (CSA) classifies marijuana as a Schedule I drug, which is “considered the most dangerous class of drugs with a high potential for abuse and potentially severe psychological and/or physical dependence” and includes heroin, LSD and ecstasy.<sup>2</sup> As such, the CSA “makes it illegal under federal law to manufacture, distribute, or dispense marijuana” and “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.”<sup>3</sup> Even if marijuana is rescheduled as a Schedule II drug, which encompasses “drugs with a high potential for abuse” including opium, cocaine and methamphetamine, the marijuana industry will likely continue to be perceived as high risk and subject to ongoing legal and regulatory scrutiny. Furthermore, it is highly unlikely that marijuana would be rescheduled any time soon. On August 11, the Drug Enforcement Administration denied petitions to reschedule marijuana “because it does not meet the criteria for currently accepted medical use in treatment in the United States, there is a lack of accepted safety for its use under medical supervision, and it has a high potential for abuse.”<sup>4</sup>

According to the Financial Crimes Enforcement Network:

“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)...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.... Thorough customer due diligence is a critical aspect of making this assessment.”<sup>5</sup>

In order to effectively meet these guidelines, all financial institutions need to first determine how they define “marijuana-related business” and then develop

<sup>1</sup> “FDIC Encourages Institutions to Consider Customer Relationships on a Case-by-Case Basis,” FDIC, January 28, 2015, <https://www.fdic.gov/news/news/press/2015/pr15009.html>

<sup>2</sup> “Drug Schedules,” Drug Enforcement Agency, <https://www.dea.gov/druginfo/ds.shtml>

<sup>3</sup> “FIN-2014-G001: BSA Expectations Regarding Marijuana-Related Businesses,” FinCEN, February 14, 2014, [https://www.fincen.gov/statutes\\_regs/guidance/pdf/FIN-2014-G001.pdf](https://www.fincen.gov/statutes_regs/guidance/pdf/FIN-2014-G001.pdf)

<sup>4</sup> “DEA Announces Actions Related to Marijuana and Industrial Hemp,” DEA, August 11, 2016, <https://www.dea.gov/divisions/hq/2016/hq081116.shtml>

<sup>5</sup> “FIN-2014-G001: BSA Expectations Regarding Marijuana-Related Businesses,” FinCEN, February 14, 2014, [https://www.fincen.gov/statutes\\_regs/guidance/pdf/FIN-2014-G001.pdf](https://www.fincen.gov/statutes_regs/guidance/pdf/FIN-2014-G001.pdf)



risk-based policies and procedures specific to MRBs, including effective methods for consistently identifying and treating them.

### A three-tiered risk approach

The following is the framework MRB Monitor utilizes to define MRBs and to categorize MRBs into three risk-based tiers depending on the degree to which a business literally touches marijuana and interacts with other MRBs. This tiered approach may be helpful to financial institutions—including those that naively believe they have zero exposure to the industry—in determining what level of the marijuana supply chain they may be willing to knowingly offer services and to what extent they need to update policies, procedures and due diligence methods to effectively identify, measure and mitigate marijuana-related risk.

#### Tier I MRBs

Tier I MRBs are considered the riskiest because they literally touch marijuana at some point along the supply chain and most clearly “manufacture, distribute, or dispense marijuana.”<sup>6</sup> Tier I MRBs generally encompass businesses licensed by a state or “marijuana-related legitimate business,” as defined in proposed federal marijuana banking bills.<sup>7</sup> Tier I MRBs include, but are not limited to, the following categories:

- Cannabis seeds
- Processing
- Testing
- Retail delivery
- Planting
- Packaging
- Transporting
- Cannabidiol
- Cultivation
- Infused products
- Medical dispensary
- Industrial hemp



- Harvesting
- Wholesaling
- Recreational retail

Within each of these categories are a number of possible subcategories. For example, “Cultivation” might include outdoor, indoor and mixed (i.e., both indoor and outdoor). “Processing” includes a wide variety of companies, such as those that process the marijuana plant or extract oils for use in edible products. Some Tier I categories, such as “Testing” and “Transporting,” may be less obvious than growing, processing, distributing or selling marijuana and are therefore more likely to be overlooked by compliance teams. “Testing” labs that analyze marijuana for toxins and “Transportation” companies that move marijuana from point A to point B may not necessarily be licensed by a state as a “marijuana businesses,” but are included in Tier I of this framework because they literally touch marijuana and might reasonably be expected to earn all of their revenue from other Tier I MRBs. Other categories like “Cannabidiol” products and “Industrial hemp” are often mistakenly believed to be legal (even at the federal level), but in fact are not and, therefore, are sometimes ignored or excluded by compliance

protocol. The layman might be surprised by the number of categories associated with Tier I MRBs. In the earliest days of the marijuana industry, MRBs were often vertically integrated and performed all of the activities related to the growing, processing and sale of marijuana and related products. However, as the marijuana industry continues to grow and evolve, it is becoming more fragmented as companies specialize in each step of the process.

Lastly, any entity that has a financial or controlling interest (regardless of ownership percentage) in a Tier I MRB, including shell companies and management that may be seeking “to conceal or disguise involvement in marijuana-related business activity,”<sup>8</sup> are also categorized as Tier I MRBs.

#### Tier II MRBs

Tier II MRBs are considered less risky than Tier I MRBs because they do not directly “manufacture, distribute, or dispense marijuana” and are typically not licensed by a state as a “marijuana business” per se. However, Tier II MRBs are considered “marijuana businesses” within the framework because they are specifically focused on providing pro-



<sup>6</sup> Ibid.

<sup>7</sup> U.S. Senate, “S. 1726: Marijuana Businesses Access to Banking Act of 2015,” July 9, 2015, <https://www.congress.gov/bill/114th-congress/senate-bill/1726/text>; U.S. House of Representatives, H. R. 2076, April 28, 2015, <https://www.govtrack.us/congress/bills/114/hr2076/text>

<sup>8</sup> “FIN-2014-G001: BSA Expectations Regarding Marijuana-Related Businesses,” FinCEN, February 14, 2014, [https://www.fincen.gov/statutes\\_regs/guidance/pdf/FIN-2014-G001.pdf](https://www.fincen.gov/statutes_regs/guidance/pdf/FIN-2014-G001.pdf)

ducts and services to Tier I MRBs and the marijuana industry in general. The majority, if not all, of a Tier II MRB's revenue might reasonably be expected to come from Tier I MRBs and marijuana-related activities. Therefore, Tier II MRBs might be considered to be "aiding and abetting" the more clearly defined and federally illegal Tier I MRBs. According to a January 2016 *ACAMS moneylaundering.com* article, "U.S. officials are drafting guidance for financial institutions concerned that accepting deposits from third-party companies serving state-licensed marijuana vendors may violate federal rules against money laundering," but as of August 2016, no guidance has been issued.<sup>9</sup> Tier II MRBs are sometimes referred to as "ancillary" or "indirect" MRBs as opposed to "direct" Tier I MRBs. Tier II MRBs include, but are not limited to, the following categories:

- Hydroponic supplies
- Payment processors
- Packaging supplies
- Advertising and public relations
- Licensing consulting
- Training and education
- Industry associations
- Marijuana software

### Tier III MRBs

Tier III MRBs are considered the least risky tier and not a "marijuana businesses" in the strictest sense. Unlike Tier II MRBs, Tier III MRBs are not specifically focused on selling to Tier I MRBs or the marijuana industry. In addition, selling to Tier I MRBs is incidental to a Tier III MRB's overall business and revenue. However, Tier III MRBs are specific businesses known to serve Tier I MRBs and, as such, might still be considered to be "aiding and abetting" an illegal activity in a strict sense. Tier III MRBs can be any type of business, but generally include professional services firms (e.g., attorneys, accountants, registered agents, etc.) and commercial property owners. A scenario might include a professional services firm knowingly helping a Tier I MRB to create a "management" company with the presumed goal of helping

the MRB evade detection as marijuana-related. Another scenario might include a real estate investor who leases commercial property to a Tier I MRB.

### Wiggle room

This framework allows for some wiggle room and financial institutions can apply it to "take a risk-based approach in assessing individual customer relationships."<sup>10</sup> A few examples might include:

- *Increase Risk Tier:* Although most professional services firms known to serve Tier I MRBs might be categorized as Tier III (the lowest risk), if a particular firm is known to focus specifically on the marijuana industry and one might reasonably expect most of its revenue to come from Tier I MRBs, it could reasonably be categorized as Tier II.
- *Decrease Risk Tier:* Although most armored car companies known to serve Tier I MRBs might be categorized as Tier I (the highest risk tier), if a particular company does not focus on the marijuana industry, generates only a small percentage of its revenue from Tier I MRBs and does not touch marijuana (e.g., perhaps they only move cash), it might reasonably be categorized as Tier II or Tier III.
- *Exclude Completely:* A financial institution may choose to completely exclude utility companies from this framework, even though they may be known to serve Tier I MRBs, since the percent of their revenue from Tier I MRBs is extraordinarily small.

### A note about marijuana licensing status

Most states that have legalized marijuana have done so in conjunction with robust marijuana application processes, rules and regulations, generally culminating in Tier I MRBs being "licensed" by the state. However, some legalized states do not have any framework for licensing or regulating Tier I MRBs (e.g., California, Michigan, Montana), yet Tier I MRBs clearly exist and operate within those states. For

this reason, whether or not a particular business is "licensed" is not directly relevant when determining if that business is marijuana-related. To take this logic one step further, this framework considers businesses with pending, failed and revoked/canceled marijuana licenses to also be Tier I MRBs.

### Conclusion

The decision to do business with any customer ultimately rests with each financial institution, which is privileged to refuse to open an account or to close an account, as long as the reason for doing so is not motivated by discrimination against a protected class.<sup>11</sup> The goal of this article is not to convince financial institutions to serve or not serve MRBs as an entire category, but to share a framework for developing comprehensive policies and procedures to consistently and effectively make risk-based decisions regarding marijuana-related businesses. **A**

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*MRB Monitor helps financial institutions identify potential risk, fraud and money laundering related to the emerging marijuana industry.*

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<sup>9</sup> Colby Adams, "FinCEN Weighs Bank Guidance for Ancillary Businesses Linked to Weed Trade," *ACAMS moneylaundering.com*, January 27, 2016, <http://www.moneylaundering.com/News/Pages/137002.aspx>

<sup>10</sup> "FDIC Encourages Institutions to Consider Customer Relationships on a Case-by-Case Basis," FDIC, January 28, 2015, <https://www.fdic.gov/news/news/press/2015/pr15009.html>

<sup>11</sup> "Exam Procedure Update: Marijuana-Related Businesses," Washington State Department of Financial Institutions, May 20, 2016, [www.dfi.wa.gov/documents/credit-unions/marijuana-exam-procedures.pdf](http://www.dfi.wa.gov/documents/credit-unions/marijuana-exam-procedures.pdf)