

Michigan Law Review

Volume 114 | Issue 5

2016

Underbanked: Cooperative Banking as a Potential Solution to the Marijuana-Banking Problem

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Recommended Citation

Patrick A. Tighe, *Underbanked: Cooperative Banking as a Potential Solution to the Marijuana-Banking Problem*, 114 MICH. L. REV. 803 (2016).

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NOTE

UNDERBANKED: COOPERATIVE BANKING AS A POTENTIAL SOLUTION TO THE MARIJUANA-BANKING PROBLEM

Patrick A. Tighe*

Numerous states have recently legalized recreational marijuana, which has created a burgeoning marijuana industry needing and demanding access to a variety of banking and financial services. Due, however, to the interplay between the federal criminalization of marijuana and federal anti-money laundering laws, U.S. financial institutions cannot handle legally the proceeds from marijuana activity. As a result, most financial institutions are unwilling to flout federal anti-money laundering laws, and so too few marijuana-related businesses can access banking services. This Note argues that the most viable policy option for resolving this “underbanking” problem is a financial cooperative approach such as a cannabis-only financial cooperative. Even in light of federal anti-money laundering laws, this Note contends that the Federal Reserve is legally authorized to grant some cannabis-only financial cooperatives access to its payment system services under the Monetary Control Act of 1980.

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* J.D., May 2015, University of Michigan Law School. I would like to thank Professor Michael Barr for his invaluable insight and direction on this Note. I dedicate this Note in honor of my mother, Billie Ruth Tighe, and my uncle, Mike Faubion.

INTRODUCTION

A recent *New York Times* article illustrates the current landscape of marijuana legalization as follows:

In his second-floor office above a hair salon in north Seattle, Ryan Kunkel is seated on a couch placing \$1,000 bricks of cash—dozens of them—in a rumpled brown paper bag. When he finishes, he stashes the money in the trunk of his BMW and sets off on an adrenalized drive downtown, darting through traffic and nervously checking to see if anyone is following him.¹

The scene in Ryan Kunkel's office and his subsequent drive evoke thoughts of a Hollywood action movie, complete with furtive conduct, high-speed chases, and money. But in this brave new world of state-led initiatives to decriminalize marijuana, Kunkel's experience is far from exceptional. Under Washington law, Kunkel legally co-owns and operates five medical-marijuana dispensaries.² Although states are free to decriminalize marijuana,³ and the marijuana industry is booming in the twenty-three states that have done so, marijuana is still illegal under federal law. Due to the ongoing federal prohibition, marijuana-related business owners such as Kunkel struggle to access banking services, making it difficult to open bank accounts and deposit the proceeds from their businesses.

The federal government regulates almost all banks in the United States. Since federally regulated financial institutions cannot legally accept the proceeds from marijuana activity due to federal anti-money laundering laws,⁴ most financial institutions prohibit marijuana business owners from opening accounts and receiving other types of financial services. Despite the legal consequences, a minority of financial institutions provide banking services to marijuana-related businesses. But without access to the vast majority of financial institutions, state-legalized marijuana businesses effectively operate only in cash. From the state's perspective, a cash-only industry increases concerns about public safety and regulatory oversight. Struggling to access banking accounts, loans, and credit, marijuana-related businesses resort to elaborate schemes to protect their money—hiring private security, using private vaults, or taking alternating transportation routes. Due to the ongoing federal prohibition, this marijuana industry problem is properly characterized as “underbanking”—too many marijuana businesses are demanding access to banking and financial services without success.

1. Serge F. Kovalski, *Banks Say No to Marijuana Money, Legal or Not*, N.Y. TIMES (Jan. 11, 2014), <http://www.nytimes.com/2014/01/12/us/banks-say-no-to-marijuana-money-legal-or-not.html> [<http://perma.cc/5A7M-CX5A>].

2. *Id.*

3. Erwin Chemerinsky et al., *Cooperative Federalism and Marijuana Regulation*, 62 UCLA L. REV. 74, 100–13 (2015) (explaining why the federal government, even if it wanted to, could not stop state marijuana-legalization efforts using the federal government's preemption power under the Supremacy Clause).

4. *E.g.*, 18 U.S.C. §§ 1956, 1957 (2012).

Federal efforts to address the underbanking problem have been unsuccessful. Guidance from federal financial regulators—and efforts by state officials to clarify the federal guidelines—have not induced more banks to enter the market. Furthermore, although many proposals to solve this problem abound, most either require federal legislative action or will not actually resolve the problem. Even though a majority of Americans now favor legalization,⁵ congressional action to resolve this problem is unlikely given the current political environment in Washington, D.C.

Since congressional action is unlikely, states such as Colorado have taken action into their own hands. In 2014, Colorado passed legislation authorizing cannabis-only co-ops and granted a state charter to a cannabis-only credit union.⁶ While still requiring the Federal Reserve's approval, these co-ops and credit unions, once approved, will enable marijuana businesses to access basic banking services currently denied to them.

When Colorado passed this legislation, commentators called the initiative a “charade” and unrealistic,⁷ in large part because many critics believe that the Federal Reserve is unlikely to approve these ventures.⁸ Approval from the Federal Reserve, however, may not be as unlikely as critics suggest. Not only have federal regulators already demonstrated a willingness to assuage this problem,⁹ but the Federal Reserve is legally authorized to allow a cannabis-only credit union to access its payment system services.

This Note argues that the financial cooperative approach, especially a cannabis-only credit union, is the most viable option to resolve the underbanking problem, despite commentators' doubts. Part I explores how federal regulatory efforts have failed to induce banks to provide services to marijuana-related businesses. Part II argues that many of the commonly touted policy solutions to the underbanking problem would not sufficiently remedy the problem. Part III contends that a financial cooperative approach is not an unrealistic solution, as some critics suggest, because the Federal Reserve is legally authorized to grant some cannabis-only financial cooperatives access to the Federal Reserve's payment system services under the Monetary Control Act of 1980.

5. Marc Fisher & Richard Johnson, *A Brief History of Public Opinion on Marijuana Legalization*, WASH. POST (Feb. 21, 2014), http://www.washingtonpost.com/local/a-brief-history-of-public-opinion-on-marijuana-legalization/2014/02/21/77c04e40-9b4a-11e3-975d-107dfef7b668_graphic.html [https://perma.cc/GW84-7S5f].

6. COLO. REV. STAT. § 11-33-108(2)(a) (2014).

7. Julie Andersen Hill, *Banks, Marijuana, and Federalism*, 65 CASE W. RES. L. REV. 597, 639 n.220 (2015).

8. *Id.*; see *infra* text accompanying notes 162–163.

9. See *infra* Section I.C and accompanying notes (detailing how the Department of Justice, the Financial Crimes Enforcement Network (FinCEN), the Federal Deposit Insurance Corporation (FDIC), and the National Credit Union Administration (NCUA), among others, have attempted to alleviate this underbanking problem).

I. THE FAILURE OF FEDERAL EFFORTS TO REMEDY THE
UNDERBANKING PROBLEM

Section I.A explores how shifting public opinion and state laws decriminalizing marijuana have engendered a robust legal marijuana industry. Section I.B discusses how financial institutions are reluctant to provide services to many marijuana-related businesses because of federal anti-money laundering laws. Section I.C explains that, despite federal efforts clarifying how financial institutions can provide banking services to marijuana-related businesses, banks have not done so because the legal risks remain high. Collectively, Part I demonstrates that states that have legalized marijuana are left in a quagmire about how to provide banking services and get cash off the street.

A. *A Robust and Growing Marijuana Industry*

In 1970, only 12 percent of Americans supported legalizing the possession and use of marijuana.¹⁰ But in 2013, for the first time in this century, a majority (52 percent) of Americans supported legalizing marijuana.¹¹ With this shift in public opinion, state laws have changed accordingly. Despite the continuing federal prohibition on marijuana, twenty-three states and the District of Columbia have legalized medical marijuana.¹² In 2012, Colorado and Washington became the first two states in the country to legalize recreational marijuana.¹³ Colorado and Washington also became the first jurisdictions not only in the United States, but the world, to legalize the cultivation and distribution of marijuana.¹⁴ Following Colorado and Washington's lead, in 2014 Alaska, Oregon, and the District of Columbia legalized recreational marijuana.¹⁵

Unsurprisingly, this tide of state-led legalization has created a large and growing marijuana industry. The national marijuana market was valued

10. Fisher & Johnson, *supra* note 5.

11. *Id.*

12. *23 Legal Medical Marijuana States and DC*, PROCON.ORG, <http://medicalmarijuana.procon.org/view.resource.php?resourceID=000881#summary> [<http://perma.cc/GG95-NJA2>] (last updated July 1, 2015); see also Josh Harkinson, *Map: The United States of Legal Weed*, MOTHER JONES (Nov. 5, 2014, 6:38 PM), <http://www.motherjones.com/politics/2014/11/map-united-states-legal-marijuana-2014-2016> [<http://perma.cc/2UAW-XAB2>].

13. Jack Healy, *Voters Ease Marijuana Laws in 2 States, but Legal Questions Remain*, N.Y. TIMES (Nov. 7, 2012), http://www.nytimes.com/2012/11/08/us/politics/marijuana-laws-eased-in-colorado-and-washington.html?_r=0 [<http://perma.cc/Y653-YJRL>].

14. See generally JONATHAN P. CAULKINS ET AL., MARIJUANA LEGALIZATION: WHAT EVERYONE NEEDS TO KNOW 138–40, 160 (2012).

15. Matt Ferner, *Alaska Becomes Fourth State to Legalize Recreational Marijuana*, HUFFINGTON POST (Nov. 5, 2012, 4:52 AM), http://www.huffingtonpost.com/2014/11/05/alaska-marijuana-legalization_n_5947516.html [<http://perma.cc/N99L-F8ZK>].

around \$1.5 billion in 2013.¹⁶ By 2019, the industry is expected to grow to around \$10.2 billion.¹⁷ Additionally, states benefit by taxing this burgeoning market. For example, while substantially downgrading its initial tax estimates, Colorado collected nearly \$44 million in tax revenue from marijuana in 2014 alone.¹⁸

As the marijuana industry expands, marijuana-related businesses need access to a variety of banking services such as corporate accounts, payroll services, and credit and lending services.¹⁹ Due to the federal criminalization of marijuana, however, many marijuana-related businesses struggle to access the most basic financial services. Without the ability to open a banking account, marijuana-related businesses cannot deposit their revenue, write checks to pay suppliers and employees, or obtain loans to expand their operations.²⁰ This lack of access creates many concerns about public safety and regulatory oversight.

B. *Federal Law Has Created the Underbanking Problem*

Although this burgeoning industry needs banking services and is operating legally under state law, federal law prevents banks from providing services to marijuana-related businesses. The federal prohibition is a product of the interplay between the Controlled Substances Act (CSA) and federal anti-money laundering laws,²¹ such as the Bank Secrecy Act (BSA)²² and the Money Laundering Control Act of 1986 (MLCA).²³ In the United States, almost all financial institutions—including those chartered by state banking agencies—are regulated by the Federal Reserve, the Federal Deposit Insurance Corporation (FDIC), the Office of the Comptroller of the Currency

16. ARCVIEW GRP., *THE STATE OF LEGAL MARIJUANA MARKETS: EXECUTIVE SUMMARY 4* (3d ed. 2015), <http://www.arcviewmarketresearch.com/s/Executive-Summary-The-State-of-Legal-Marijuana-Markets-3rd-Edition-d2qk.pdf> [<http://perma.cc/2KQ8-SAEW>].

17. *Id.* at 6.

18. COLO. DEP'T OF REVENUE, OFFICE OF RESEARCH & ANALYSIS, *MARIJUANA TAXES, LICENSES, AND FEES TRANSFERS AND DISTRIBUTION* (2015), <https://www.colorado.gov/pacific/sites/default/files/1214%20Marijuana%20Tax%2C%20License%2C%20and%20Fees%20Report.pdf> [<http://perma.cc/HLU3-AQ7L>].

19. *See* Editorial, *Marijuana Dispensaries Need Access to Banking System*, BOS. GLOBE (Sept. 9, 2014), <http://www.bostonglobe.com/opinion/editorials/2014/09/09/legal-marijuana-sellers-need-access-banking-system/w2Dy5xWNqyHK09Ip5pZW5H/story.html> [<http://perma.cc/5W4C-A3B6>].

20. *See id.* (“Because the drug remains illegal under federal law, marijuana-related businesses nationwide have struggled to find banks that will accept their deposits.”).

21. Money laundering is the process of transforming the (monetary) proceeds from illegal activity into ostensibly legitimate money or other assets. LILIAN B. KLEIN, *BANK SECRECY ACT/ANTI-MONEY LAUNDERING 2* (2008).

22. 12 U.S.C. § 1956 (2012).

23. 18 U.S.C. § 1956(a)(1)–(2) (2012).

(OCC), or the National Credit Union Administration (NCUA).²⁴ Consequently, almost all banks and financial institutions are subject to federal law, including the CSA, BSA, and MLCA.²⁵

The CSA prohibits the manufacture and distribution of marijuana.²⁶ Moreover, federal law criminalizes aiding and abetting²⁷ and conspiring to violate federal law.²⁸ Consequently, it is illegal to aid and abet or to conspire to manufacture, distribute, or dispense marijuana. Thus federal law prohibits banks and other financial institutions from assisting with the manufacturing, distribution, or dispensing of marijuana.

The BSA and the MLCA require financial institutions to ensure that the monetary proceeds from marijuana activity do not enter the nation's banking system. The BSA aims "to prevent banks and other financial service providers from being used as intermediaries for, or to hide the transfer or deposit of money derived from, criminal activity."²⁹ To achieve this purpose, the MLCA prohibits individuals and entities, such as financial institutions, from laundering the proceeds from marijuana activity.³⁰

24. The United States has a dual banking system. To operate as a bank or financial institution, a financial institution must obtain either a federal or state charter. If a bank wants to operate with a national charter, it receives a charter from the Office of the Comptroller of the Currency (OCC). The OCC then regulates and supervises the financial institution. Moreover, all nationally chartered banks are members of the Federal Reserve and subject to its regulation. While a state bank receives its charter from a particular state, a state-chartered bank is required under federal law to obtain FDIC insurance (and be regulated by the FDIC) or become a member of the Federal Reserve (and be regulated by the Federal Reserve). A credit union can also obtain either a federal or state charter. If a credit union wants to operate with a national charter, it obtains a charter from the NCUA and is regulated by the NCUA. INTERNAL REVENUE SERV., INTERNAL REVENUE MANUAL § 4.26.9.4 (2006), http://www.irs.gov/irm/part4/irm_04-026-009.html#d0e1909 [<http://perma.cc/NA7R-BH6F>]. If a state-chartered credit union is required under state law to obtain federal insurance, it obtains insurance from the NCUA and is also subject to NCUA regulations. *Id.* Most states require state-chartered credit unions to obtain federal insurance from the NCUA. Hill, *supra* note 7, at 617–18. Consequently, almost all financial institutions are regulated by federal financial agencies and subject to federal law. *Id.* at 606–07.

25. Hill, *supra* note 7, at 607–12.

26. 21 U.S.C. §§ 841(a)(1), 802(6), 812(c) (2012).

27. 18 U.S.C. § 2 ("Whoever commits an offense against the United States or aids, abets, counsels, commands, induces or procures its commission, is punishable as a principal. . . . Whoever willfully causes an act to be done which if directly performed by him or another would be an offense against the United States, is punishable as a principal.").

28. *Id.* § 371 ("If two or more persons conspire either to commit any offense against the United States, or to defraud the United States, or any agency thereof in any manner or for any purpose, and one or more of such persons do any act to effect the object of the conspiracy, each shall be fined under this title or imprisoned not more than five years, or both.").

29. KLEIN, *supra* note 21, at vii.

30. 18 U.S.C. §§ 1956, 1957. A financial institution can launder money in a number of ways. If a financial institution knowingly "conducts or attempts to conduct . . . a financial transaction which in fact involves the proceeds of specified unlawful activity," the institution has engaged in money laundering if it either (1) intends "to promote the carrying on of specified unlawful activity"; (2) knows "that the transaction is designed in whole or in part . . . to conceal or disguise the nature, the location, the source, the ownership, or the control of the proceeds of specified unlawful activity"; or (3) knows "that the transaction is designed in

The BSA and other laws establish reporting mechanisms that allow financial institutions to demonstrate that they are not laundering money. First, the BSA requires financial institutions to engage in customer due diligence to verify the identity of the potential accountholder,³¹ the source of the funds in the account, the purpose of the account, and the customer's primary source of business.³² Second, financial institutions must file Suspicious Activity Reports (SARs) with the Financial Crimes Enforcement Network (FinCEN), a federal bureau within the U.S. Department of the Treasury that enforces the federal anti-money laundering laws.³³ These reports notify the federal government if "the bank knows, suspects, or has reason to suspect that . . . [t]he transaction involves funds derived from illegal activities or is intended or conducted in order to hide or disguise funds or assets derived from illegal activities."³⁴

Financial institutions and their employees face significant penalties for violating the MLCA and BSA. Financial institutions could lose their charters,³⁵ and bank employees could be barred from banking.³⁶ Furthermore, the BSA and MLCA authorize criminal prosecution of individuals for money laundering. Bank employees face up to twenty years in prison for each money-laundering transaction. Banks and their employees could also be fined \$500,000, or twice the value of the transaction, whichever is greater.³⁷ Additionally, any property involved in the transaction or traceable to the illegal proceeds, including bank accounts, could be subject to criminal³⁸ or civil forfeiture.³⁹

Despite these severe penalties, some financial institutions provide banking services to a small number of marijuana-related businesses. While concrete evidence is hard to come by, anecdotes abound. For instance, "more than a dozen cannabis businesses [in Washington allege that] they all keep corporate accounts at Chase, U.S. Bank and Wells Fargo, in addition to

whole or in part . . . to avoid a transaction reporting requirement under State or Federal law." *Id.* § 1956(a)(1). Additionally, a financial institution can launder money by "knowingly engag[ing] or attempt[ing] to engage in a monetary transaction in criminally derived property of a value greater than \$10,000." *Id.* § 1957(a). Under the MLCA, a "specified unlawful activity" entails "the manufacture, importation, sale, or distribution of a controlled substance" under the CSA, which includes marijuana activity. *Id.* §§ 1956(c)(7), 1957(f)(3); 21 U.S.C. § 812(c)(c)(10).

31. 31 C.F.R. § 1010.312 (2014).

32. FED. FIN. INST. EXAMINATION COUNCIL, BANK SECRECY ACT/ANTI-MONEY LAUNDERING EXAMINATION MANUAL 25, 63–65 (2010) [hereinafter FFIEC MANUAL], https://www.ffiec.gov/bsa_aml_infobase/documents/BSA_AML_Man_2010.pdf [<https://perma.cc/7MJM-TBYD>].

33. 31 C.F.R. § 1020.320(a)(2); FFIEC MANUAL, *supra* note 32, at 1, 67–80.

34. 31 C.F.R. § 1020.320(a)(2).

35. 12 U.S.C. §§ 93(d)(1), 1772d, 3105(i) (2012).

36. *Id.* § 1818(e)(7).

37. *Id.*

38. *Id.* § 982(a)(1).

39. *Id.* § 981(a)(1)(A).

small, local banks.⁴⁰ In Colorado, marijuana-related businesses closely guard where they bank. These businesses fear that their banks will stop giving them access if the banks become inundated with too many requests for banking services from other marijuana-related business.⁴¹

The marijuana-related businesses that access banking services either deceive financial institutions or identify financial institutions that are willing to turn a blind eye toward the account holder's business activity. By creating a non-marijuana-related holding company, some marijuana-related businesses deceive financial institutions into thinking their business activity is legal under federal law.⁴² Such deception is possible if the financial institution does not engage in thorough customer due diligence.⁴³

Less risk-averse financial institutions may be willing to provide services under the table. This is likely if, from the financial institution's perspective, the benefits of providing such services outweigh the potential civil and criminal liability.⁴⁴ Because many financial institutions are unwilling to knowingly violate federal anti-money laundering laws, marijuana-related businesses have fewer financial institutions with which to engage. Consequently, the financial institutions that do provide services can extract high fees for accepting proceeds from marijuana-related activity and charge above-market interest rates for extending credit. In return for flouting the law, these financial institutions receive large deposit balances from a business operating within a profitable and growing industry.⁴⁵

Providing these services may also benefit the financial institution's reputation. More marijuana-related businesses may seek to do business with the financial institutions that exposed themselves to significant risk. This heightened customer loyalty may prove helpful if the federal government ends its prohibition and financial institutions can legally provide such services. While a bank's willingness to provide services largely depends on its "risk appetite,"⁴⁶ anecdotal evidence suggests that some banks are willing to provide services if the benefits outweigh the severe penalties for doing so under the BSA and MLCA.

40. Jose Pagliery, *Legal Marijuana's All-Cash Business and Secret Banking*, CNN MONEY (Apr. 29, 2013, 3:56 PM), <http://money.cnn.com/2013/04/29/smallbusiness/marijuana-cash/> [<http://perma.cc/5RXW-8WX4>].

41. See David Migoya, *Where Colorado Pot Shops Bank Is Closely Guarded Trade Secret for Some*, DENV. POST (Feb. 28, 2014, 7:37 PM), http://www.denverpost.com/marijuana/ci_25244700/where-colorado-pot-shops-bank-is-closely-guarded [<http://perma.cc/377E-9WUS>].

42. See U.S. DEP'T OF THE TREASURY, FIN. CRIMES ENF'T NETWORK, FIN-2014-G001, BSA EXPECTATIONS REGARDING MARIJUANA-RELATED BUSINESSES 5 (2014) [hereinafter BSA EXPECTATIONS], http://www.fincen.gov/statutes_regs/guidance/pdf/FIN-2014-G001.pdf [<http://perma.cc/8GVT-W5XR>].

43. See *supra* text accompanying notes 31–34.

44. *The Risk of "Legalized" Marijuana to the Banking Industry*, WOLTERS KLUWER FIN. SERVS., <http://www.wolterskluwerfs.com/points-ahead/risk-of-legalized-marijuana-to-banking-industry.aspx> [<http://perma.cc/FR4U-F6WY>].

45. *Id.*

46. *Id.*

Because most marijuana-related businesses cannot access basic banking services, the industry operates largely as a cash-only industry.⁴⁷ For example, since Visa and MasterCard are federally regulated financial institutions, they prohibit use of their debit and credit cards for purchases at marijuana-related businesses.⁴⁸ Consequently, consumers must use cash to purchase marijuana products at dispensaries. Without access to a bank account, marijuana-related businesses must store and secure the cash on-site or at some other location, including private residences.⁴⁹ Some businesses have even hired private security companies to process, store, and secure their proceeds.⁵⁰ Additionally, marijuana-related businesses rely on employees to handle large amounts of cash,⁵¹ increasing concerns about employee theft and mismanagement of funds since cash leaves little to no paper trail. Without access to financial institutions' payroll services, businesses must also pay their employees in cash. These employees may then similarly struggle to deposit their earnings in their checking accounts if a bank knows about their means of employment.⁵²

From the state's perspective, an industry that operates in cash presents two main issues. First, a cash-only industry increases public safety concerns. Since there is more cash on the streets to facilitate transactions, states worry more about crime, especially robbery and burglary.⁵³ The state has even suspended some businesses' licenses because there have been too many burglaries and robberies there.⁵⁴

The second problem is that a cash-only industry hinders effective regulatory oversight.⁵⁵ Because activists have pitched legalization in part on its ability to generate tax revenue for the state, ensuring that a marijuana-related business pays its state and local taxes is essential. Since the industry is largely cash-only, however there is no paper trail,⁵⁶ making it harder for state

47. See generally BSA EXPECTATIONS, *supra* note 42.

48. Robin Sidel, *Plastic and Pot Collide in Colorado*, WALL ST. J., Jan. 7, 2014, at C1.

49. Pagliery, *supra* note 40.

50. Bruce Kennedy, *Colorado Agrees to Cannabis "Credit Co-Ops"*, CBS NEWS (June 9, 2014, 7:18 AM), <http://www.cbsnews.com/news/colorado-agrees-to-cannabis-credit-co-ops/> [<http://perma.cc/KZ4B-835U>].

51. See Kovaleski, *supra* note 1.

52. *Id.*

53. See John Ingold & Ricardo Baca, *Burglaries at Denver Marijuana Shops Slow, but Industry Still Worried*, DENV. POST (June 16, 2014, 3:59 PM), http://www.denverpost.com/marijuana/ci_25969469/burglaries-at-denver-marijuana-shops-slow-but-industry [<http://perma.cc/2BPV-KD8W>] (noting that, despite these industry concerns, Denver's Department of Safety is reporting that the city's marijuana-related businesses—which are the majority of Colorado's marijuana-related businesses—are on pace to have the lowest amount of robberies and burglaries in three years).

54. See, e.g., *id.*

55. See, e.g., Pagliery, *supra* note 40.

56. *Id.* (“[The fact that] weed is bought with paper money . . . could hinder Washington's ability to properly tax pot businesses, because the state will have a difficult time tracking sales.”).

regulators to ensure that marijuana-related businesses pay the proper amount of taxes.⁵⁷ Since marijuana-related businesses cannot access banking services, they must pay their taxes in cash (and may even incur fees for paying taxes in cash).⁵⁸

In addition to states' public safety and regulatory oversight concerns, marijuana-related businesses also face other issues stemming from the underbanking problem. First, the underbanking problem restricts industry growth. While state officials may not be concerned with industry growth,⁵⁹ expanding business operations is difficult without access to credit.⁶⁰ Instead of obtaining a loan to purchase a new cultivation site or proper grow lighting, marijuana-related businesses must make purchases in cash. The cash-only nature of the business also creates a guise of illegality.⁶¹ That is, even though marijuana is legal under state law, business owners feel like criminals when forced to deal only in cash. This may discourage business owners from entering the recreational-marijuana market. From the industry's perspective, access to banking services lends legitimacy to their business.

C. Federal Regulators Have Not Resolved the Problem

Federal regulators have provided regulatory guidance in an effort to induce financial institutions to provide services, but they have had little success. First, in August 2013, the Department of Justice (DOJ) issued the Cole Memo to all U.S. Attorneys, providing guidance regarding marijuana enforcement under the CSA in light of state-led marijuana-legalization initiatives.⁶² The guidance applies to all federal enforcement activity, including criminal investigations and prosecutions, concerning marijuana in all states.⁶³ Essentially, the DOJ decided that federal law enforcement should not target marijuana activity operating legally under state law as long as (1) the state in question "will implement strong and effective regulatory and enforcement systems" and (2) the activity permitted under state law does not implicate one of the DOJ's eight marijuana enforcement priorities.⁶⁴

57. See KLEIN, *supra* note 21, at 2 ("Th[e] paper trail operates to deter illegal activity and provides a means to trace movements of money through the financial system.").

58. David Migoya, *IRS Fines Unbanked Pot Shops for Paying Federal Payroll Tax in Cash*, DENV. POST (July 2, 2014, 11:17 AM), http://www.denverpost.com/business/ci_26075425/irs-fines-unbanked-pot-shops-paying-federal-payroll [<http://perma.cc/C8PL-TQJR>].

59. See Memorandum from James M. Cole, Deputy Attorney Gen., to U.S. Attorneys, *Guidance Regarding Marijuana Enforcement 1–2* (Aug. 29, 2013) [hereinafter *Cole Memo*], <http://www.justice.gov/iso/opa/resources/3052013829132756857467.pdf> [<http://perma.cc/QUP8-45TD>].

60. See Kovaleski, *supra* note 1.

61. *Id.*

62. *Cole Memo*, *supra* note 59.

63. *Id.*

64. *Id.* ("[C]ertain enforcement priorities . . . are particularly important to the federal government: [p]reventing the distribution of marijuana to minors; [p]reventing revenue from the sale of marijuana from going to criminal enterprises, gangs, and cartels; [p]reventing the diversion of marijuana from states where it is legal under state law in some form to other

Following the Cole Memo, FinCEN issued guidelines to financial institutions on how they could comply with the BSA if they decided to provide financial services to marijuana-related businesses.⁶⁵ According to FinCEN's guidelines, a financial institution has to: (1) engage in additional and significant customer due diligence before providing services to a marijuana-related businesses⁶⁶ and (2) submit different types of marijuana-specific SAR filings when providing services to marijuana-related businesses.⁶⁷ The stated purpose of these guidelines is to "enhance the availability of financial services for, and the financial transparency of, marijuana-related businesses."⁶⁸

The FDIC and the NCUA followed suit, providing additional guidance. These two insurers guarantee that the financial institutions they insure comply with federal law, such as the BSA, by conducting regular examinations.⁶⁹ If a financial institution is found to be in violation of the BSA, the FDIC and NCUA can issue civil penalties or revoke the institution's deposit insurance (thereby effectively closing the institution).⁷⁰ The FDIC and NCUA instructed their examiners to verify that a financial institution is complying

states; [p]reventing state-authorized marijuana activity from being used as a cover or pretext for the trafficking of other illegal drugs or other illegal activity; [p]reventing violence and the use of firearms in the cultivation and distribution of marijuana; [p]reventing drugged driving and the exacerbation of other adverse public health consequences associated with marijuana use; [p]reventing the growing of marijuana on public lands and the attendant public safety and environmental dangers posed by marijuana production on public lands; and [p]reventing marijuana possession or use on federal property.").

65. BSA EXPECTATIONS, *supra* note 42, at 1.

66. *Id.* at 2–3 ("[C]ustomer due diligence . . . includes (i) verifying with appropriate state authorities whether the business is duly licensed and registered; (ii) reviewing the license application (and related documentation) submitted by the business for obtaining a state license to operate its marijuana-related businesses; (iii) requesting from state licensing and enforcement authorities available information about the business and related parties; (iv) developing an understanding of the normal and expected activity for the business, including the types of products to be sold and the type of customers to be served (e.g., medical versus recreational customers); . . . (vi) ongoing monitoring for suspicious activity, including for any of the red flags described in this guidance; and (vii) refreshing information obtained as part of customer due diligence on a periodic basis and commensurate with the risk. . . . [A] financial institution should [also] consider whether a marijuana-related business implicates one of the Cole Memo priorities or violates state law.").

67. *Id.* at 3. The different types of SAR filings include "Marijuana Limited," "Marijuana Priority," and "Marijuana Termination." A "Marijuana Limited" SAR is a report that a financial institution would file with FinCEN indicating that the institution: (1) is "providing financial services to a marijuana-related businesses" and (2) "reasonably believes, based on its customer due diligence," that the marijuana-related business "does not implicate one of the Cole Memo priorities or violate state law." *Id.* at 3–5. A "Marijuana Priority" SAR is a filing in which a financial institution indicates to FinCEN that it reasonably believes, based on its customer due diligence, that a marijuana-related business implicates one of the Cole Memo priorities or violates state law. A "Marijuana Termination" SAR is filed when a financial institution deems it necessary to terminate a relationship with a marijuana-related business in order to maintain an effective money-laundering compliance program. *Id.*

68. *Id.* at 1.

69. 12 U.S.C. §§ 1784(a), 1820(b) (2012); 12 C.F.R. § 741.1 (2015).

70. 12 U.S.C. § 1818(i), (a)(2), (e)(2).

with FinCEN's guidelines if the institution provides services to marijuana-related businesses.⁷¹ To date, the other federal financial agencies that enforce the BSA and MLCA—the Federal Reserve and the OCC—have not issued guidance, despite a joint request from the governors of Colorado and Washington to do so.⁷²

In spite of this effort, federal guidance has not alleviated the legal concerns of the financial and banking sector, for four reasons. First, while the DOJ and FinCEN have issued guidelines about nonenforcement, the underlying laws—the CSA, BSA, and MLCA—have not changed. It is still illegal for financial institutions to launder the proceeds from marijuana-related businesses, and the federal guidance does not offer financial institutions legal immunity from federal prosecution. Moreover, none of the guidelines detail what repercussions a bank may face if it makes a good-faith effort to comply but ultimately fails. Given the lack of legal immunity, these guidelines effectively require a bank to incriminate itself in order to comply. The bank must file official documentation with the federal government demonstrating that it is engaging in money laundering, which could expose the bank to great risk.

Second, these guidelines are not legally binding.⁷³ The current, or new, executive administration could change them. A financial institution could then be held liable for civil and criminal penalties on the basis of the incriminating documentation (for example, the marijuana-specific activity reports) it produced under the current federal enforcement guidelines.

Third, these guidelines are incomplete. Only three out of the five main federal regulators charged with enforcing federal anti-money laundering laws have issued BSA guidelines to date. Financial institutions and the marijuana industry need guidance from the Federal Reserve and the OCC, not just FinCEN, FDIC, and NCUA, in order to assess whether to enter the marijuana banking market.

Finally, if a financial institution is still willing to provide services despite these legal risks, it would have to comply with new and untested SAR filing

71. See, e.g., Letter from Doreen R. Eberley, Dir., Fed. Deposit Ins. Corp., to Ken Boldt, Acting Comm'r, Div. of Banking, Colo. Dep't of Regulatory Agencies (July 15, 2014); Letter from Larry Fazio, Dir., Office of Examination and Ins., Nat'l Credit Union Admin., to Scott Jarvis, Dir., Wash. State Dep't of Fin. Insts. (July 18, 2014), <http://www.dfi.wa.gov/documents/banks/ncua-marijuana-letter.pdf> [<http://perma.cc/KX4G-J6AA>].

72. Letter from John Hickenlooper, Governor of Colo., & Jay Inslee, Governor of Wash., to Janet Yellen, Chairman, Bd. of Governors of the Fed. Reserve, Thomas J. Curry, Comptroller of the Currency, Office of the Comptroller of the Currency, Martin J. Gruenberg, Chairman, Fed. Deposit Ins. Corp., & Debbie Matz, Chairman, Nat'l Credit Union Admin. (May 23, 2014), <http://www.dfi.wa.gov/documents/banks/governors-letter-05-23-14.pdf> [<http://perma.cc/N3K7-MV9P>].

73. Cole Memo, *supra* note 59 (noting that this is only guidance and not binding law); Audrey Wright-Cipriano, *Buzz Kill*, INDEP. BANKER (July 29, 2014), <http://independentbanker.org/2014/07/lender-life-10/> [<http://perma.cc/JY2B-RFXF>] (quoting the communications director for the National Organization for the Reform of Marijuana Laws, stating that FinCEN's guidance is not binding and needs to be codified into law to adequately protect financial institutions).

and customer due diligence requirements. Before the marijuana-specific SARs, SAR filings and customer due diligence were already incredibly tedious and resource intensive.⁷⁴ Now, with FinCEN's new guidelines, financial institutions must file "Marijuana Limited" SARs and continuing activity reports whenever a marijuana-related business deposits, withdraws, or transfers money from or to its account.⁷⁵ Financial institutions also must engage in ongoing customer due diligence to ensure that a marijuana-related business complies with state and local laws and the DOJ's Cole Memo priorities.⁷⁶ FinCEN's marijuana-specific BSA guidance potentially discourages smaller banks—banks that might be more willing to assume the risks of providing services to marijuana-related businesses—from doing so because these banks lack the resources and mechanisms necessary to comply with the heightened reporting requirements.

Despite these efforts to assuage industry concerns with the federal guidance,⁷⁷ federal regulators have not induced financial institutions to provide banking services to the marijuana industry. According to FinCEN, only "105 individual financial institutions from states in more than one third of the country [are] engaged in banking relationships with marijuana-related businesses."⁷⁸ This amounts to less than 1 percent of financial institutions in the country.⁷⁹ While FinCEN has received around 1,000 SARs from financial institutions, almost half of these SARs are "Marijuana Termination" SAR filings, indicating that a bank has terminated its relationship with a marijuana-related business.⁸⁰

74. Shaheen Pasha, *Government Spying on Your Bank Accounts: Financial Institutions Pass Along Personal Information if There's a Hint of Suspicious Activity*, CNN MONEY (Aug. 9, 2006, 3:32 PM), http://money.cnn.com/2006/08/09/news/economy/banks_secretcy/ [<http://perma.cc/8PLS-E67J>].

75. See BSA EXPECTATIONS, *supra* note 42, at 3–4.

76. *Id.* at 3.

77. The state of Washington also hosted a forum in June 2014 for financial institutions about how to comply with FinCEN's BSA guidelines for marijuana-related businesses. At this forum, a representative from FinCEN discussed FinCEN's guidance and answered bankers' questions. Through these forums, the state of Washington has tried to induce banks to provide services to marijuana-related businesses by providing information and reducing BSA compliance concerns. James Pearson, *DFI Open Forum on Banking the Marijuana Industry*, ANTHEM (July 1, 2014), <http://www.nwcua.org/compliance/blog/dfi-open-forum-on-banking-the-marijuana-industry> [<http://perma.cc/K9KL-6ZLR>].

78. Jennifer Shasky Calvery, Dir., Fin. Crimes Enf't Network, Remarks at the 2014 Mid-Atlantic AML Conference 4 (Aug. 12, 2014), http://www.fincen.gov/news_room/speech/pdf/20140812.pdf [<http://perma.cc/4WFK-W2JH>].

79. In 2010, there were 7,666 FDIC-insured financial institutions in the United States and around 7,000 federal- and state-chartered credit unions. See U.S. CENSUS BUREAU, STATISTICAL ABSTRACT OF THE UNITED STATES: 2012, BANKING, FINANCE, AND INSURANCE 735, 738 (2012), <http://www.census.gov/compendia/statab/2012/tables/12s1162.pdf> [<http://perma.cc/R6U-QEMF>].

80. See Calvery, *supra* note 78, at 4–5.

Additionally, few banks are willing to publicly announce that they are providing such services. In Washington, only two banks have publicly announced they are providing banking services to marijuana-related businesses: Numerica Credit Union and Salal Credit Union.⁸¹ In Colorado, only one credit union, Fourth Corner Credit Union, openly provides financial services to marijuana-related businesses.⁸²

Overall, federal guidance—and state efforts to clarify such guidance—has failed to encourage financial institutions to enter the marijuana-banking market. Thus, scholars and state legislators have proposed other ideas to alleviate this problem. As the next Part demonstrates, however, none of these policy proposals are feasible.

II. CURRENT POLICY PROPOSALS MISS THE MARK

In light of the public safety and regulatory concerns characteristic of a cash-only industry, states that have legalized marijuana—whether for medicinal or recreational purposes—must determine how to remedy the underbanking problem in the absence of effective federal action. Existing proposals include (1) instituting a cooperative federalism approach; (2) amending the CSA either to remove marijuana altogether or to reschedule it as a Schedule II substance; or (3) using decentralized virtual currency. As this Part demonstrates, some of these proposals would resolve the underbanking problem but are politically unfeasible. Other proposals, even if implemented, would not legally solve the problem because they fail to adequately address the cause of the problem. Despite their flaws, these proposals are positive developments because they contribute to a discussion about the issue and help increase pressure on Congress to act.

A. *Instituting a Cooperative Federalism Approach*

Some scholars propose cooperative federalism as a solution to the underbanking problem.⁸³ Cooperative federalism is “a partnership between the States and the Federal Government, animated by a shared objective.”⁸⁴ In other words, the federal government and state or local government work

81. Missy Baxter, *Washington Credit Unions Move to Serve Pot Biz*, CREDIT UNION TIMES (May 16, 2014), <http://www.cutimes.com/2014/05/16/washington-credit-unions-move-to-serve-pot-biz> [http://perma.cc/PQN6-464E].

82. David Migoya, *Colorado Pot Credit Union Could Be Open by Jan. 1 Under State Charter*, DENV. POST (Nov. 20, 2014, 5:30 PM), http://www.denverpost.com/business/ci_26980328/colorado-pot-credit-union-could-be-open-by?source=infinite [http://perma.cc/23EN-4V2W].

83. See, e.g., Chemerinsky et al., *supra* note 3.

84. *Arkansas v. Oklahoma*, 503 U.S. 91, 101 (1992); see also Chemerinsky et al., *supra* note 3, at 116 (“[C]ooperative federalism allows federal and state laws to solve problems jointly rather than conflict with each other. In the interest of cooperation, certain federal statutes permit cooperative agreements between the federal government and the states to solve issues of mutual concern.”).

together, rather than independently, to tackle a specific public problem. Instead of imposing a one-size-fits-all program on the states, the federal government sets a standard, requirement, or priority for the states to meet. Then, each state or local government chooses to: (1) develop state- or locality-specific implementation plans, regulations, or enforcement strategies to achieve the federal standards⁸⁵ or (2) allow the federal government to directly intervene and implement a federal program in the state or locality.⁸⁶ In essence, Congress offers the states “the choice of regulating [an] activity according to federal standards or having state law pre-empted by federal regulation.”⁸⁷ In theory, under cooperative federalism the states and the federal government work together to resolve policy issues while respecting states’ rights.

In the marijuana context, Professor Chemerinsky proposes a cooperative federalism approach. Under this approach, “the federal government . . . allow[s] states to govern marijuana laws and regulations within their borders so long as the state regulatory schemes comply with specified federal requirements.”⁸⁸ If a state met specified federal criteria, the federal government would permit the state to opt out of the CSA’s marijuana provisions.⁸⁹ Consequently, “[s]tate law satisfying these federal guidelines would exclusively govern marijuana activities within those states opting out of the CSA but nothing would change in those states content with the CSA’s terms.”⁹⁰ Chemerinsky suggests that the specified federal criteria could mirror the guidelines and enforcement priorities set forth in the DOJ’s Cole Memo.⁹¹ To ensure that the cooperative federalism model addresses the underbanking problem, Chemerinsky’s proposal could be adapted to include a BSA/MLCA

85. Roderick M. Hills, Jr., *The Political Economy of Cooperative Federalism: Why State Autonomy Makes Sense and “Dual Sovereignty” Doesn’t*, 96 MICH. L. REV. 813, 815 (1998) (“According to this conventional wisdom, state and local officials do not enforce merely their own laws in their distinct policymaking sphere. . . . These nonfederal governments help implement federal policy in a variety of ways: by submitting implementation plans to federal agencies, by promulgating regulations, and by bringing administrative actions to enforce federal statutes. Thus, cooperative federalism offers us a vision of independent governments working together to implement federal policy.”); see also Michael S. Greve, *Against Cooperative Federalism*, 70 MISS. L.J. 557, 558 (2000).

86. Greve, *supra* note 85, at 558 (“[T]he states may choose to administer the federal program or else, cede the regulatory field to the federal government.”).

87. *New York v. United States*, 505 U.S. 144, 167 (1992).

88. Chemerinsky et al., *supra* note 3, at 114.

89. *Id.*

90. *Id.* at 74.

91. See *id.* Chemerinsky suggests that whether a state could opt of the CSA would depend on if the state could institute a strong and effective marijuana regulatory system that would not implicate one of the aforementioned federal marijuana enforcement priorities. *Id.* at 114.

waiver for financial institutions that decide to provide banking services to marijuana-related businesses operating legally under state law.⁹²

A major advantage of Chemerinsky's proposal is that it facilitates legislative compromise on a controversial issue. A slight majority of Americans support the legalization of marijuana, which means that many Americans still oppose it.⁹³ Instead of forcing Congress to engage in the politically difficult process of repealing parts of the CSA that criminalize marijuana, Chemerinsky's approach reserves the option for states to either follow the CSA or not with regards to marijuana. Moreover, a cooperative federalism approach provides political cover to states' rights conservatives who may not generally support marijuana legalization but who seek to enhance federal respect of state autonomy. Thus, a cooperative federalism approach may be politically easier to achieve than, say, a repeal of specific aspects of the CSA, because a diverse political coalition may unite to support it.

A problem with Chemerinsky's cooperative federalism approach is that it requires federal *legislative* action. While this approach may facilitate legislative compromise, the current political and legislative environment is particularly caustic to advancing any legislative initiatives.⁹⁴ In 2013, U.S. Representative Perlmutter introduced a bill entitled, "Marijuana Businesses Access to Banking Act of 2013."⁹⁵ While the bill would have resolved the underbanking problem, it effectively died in committee.⁹⁶ Given this environment, Congress is unlikely to support a substantial new piece of legislation to remedy this problem. Thus, the possibility of passing a bill through both houses of Congress, let alone a bill regarding a cooperative federalism approach for marijuana, is highly unlikely.

Nevertheless, a cooperative federalism approach to marijuana legalization would resolve the underbanking problem *if* Congress passed such a law.

92. Whether FinCEN's marijuana-specific SAR filing requirements would still apply under a cooperative federalism approach is a question of policy that the legislative or executive branch would have to address.

93. See, e.g., Fisher & Johnson, *supra* note 5.

94. The 113th Congress (2013–2014) is widely acknowledged as the most unproductive Congress in (recent) history, having only passed around fifty-five substantive laws in its first session. E.g., Chris Cillizza, *Yes, President Obama Is Right. The 113th Congress Will Be the Least Productive in History*, WASH. POST (Apr. 10, 2014), <http://www.washingtonpost.com/blogs/the-fix/wp/2014/04/10/president-obama-said-the-113th-congress-is-the-least-productive-ever-is-he-right/> [<http://perma.cc/E9AS-843X>]; Drew DeSilver, *Congress Ends Least-Productive Year in Recent History*, PEW RES. CTR. (Dec. 23, 2013), <http://www.pewresearch.org/fact-tank/2013/12/23/congress-ends-least-productive-year-in-recent-history/> [<http://perma.cc/K3XU-YUXW>].

95. H.R. 2652, 113th Cong. (2013).

96. AM. BANKERS ASS'N, FREQUENTLY ASKED QUESTIONS: MARIJUANA AND BANKING 1 (2014), <https://www.aba.com/Tools/Comm-Tools/Documents/ABAMarijuanaAndBankingFAQFeb2014.pdf> [<https://perma.cc/9GHW-896M>]. Recently, however, the Senate has voted out of committee an amendment to the Financial Services and General Government Appropriations bill that would "allow state-compliant marijuana businesses to engage in relationships with financial institutions." Danielle Keane, *Senate Committee Votes in Favor of Marijuana Banking Bill*, NORML (July 23, 2015), <http://blog.norml.org/2015/07/23/senate-committee-votes-in-favor-of-marijuana-banking-bill/> [<http://perma.cc/EF69-T8RN>].

Although federal legislative action is unlikely, a bill proposing a cooperative federalism approach generates additional pressure for federal legislative action, especially since this proposal might facilitate legislative compromise between states' rights conservatives and pro-drug legalization liberals.

B. *Amending the CSA*

One of the most commonly proposed policy solutions to the underbanking problem is amending the CSA. Some legislators propose removing marijuana as a controlled substance under the CSA, thereby ending the federal marijuana prohibition.⁹⁷ Others argue that marijuana should be rescheduled from something other than a Schedule I or Schedule II substance under the CSA.⁹⁸ In 2011 some state governors, including those of Washington and Rhode Island petitioned the DEA to reschedule marijuana as a Schedule II substance.⁹⁹ Possibly reacting to political pressure, in June 2014 the DEA requested that the FDA review the medical evidence about the safety and effectiveness of marijuana, which could lead to a rescheduling of marijuana.¹⁰⁰ While removing marijuana from the purview of the CSA would resolve the underbanking problem, merely rescheduling it would not sufficiently remedy the problem.

Removing marijuana as a controlled substance under the CSA would remedy the underbanking problem if Congress could pass such legislation. If Congress excluded marijuana from the CSA (like alcohol and tobacco, which are explicitly excluded as controlled substances),¹⁰¹ businesses could legally manufacture, distribute, and sell under federal law. If marijuana were no longer a controlled substance, manufacturing, importing, selling, and distributing marijuana would not be considered a "specified unlawful activity" under the MLCA.¹⁰² Consequently, there would be no federal money-laundering concern, and financial institutions could legally provide services to marijuana-related businesses under federal law. This proposal, however, also

97. See, e.g., Ending Federal Marijuana Prohibition Act of 2013, H.R. 499, 113th Cong. (2013).

98. See, e.g., States' Medical Marijuana Patient Protection Act, H.R. 689, 113th Cong. § 2 (2013).

99. John Ingold, *Colorado Asks DEA to Reclassify Marijuana*, DENV. POST (Dec. 29, 2011, 1:00 AM), http://www.denverpost.com/ci_19634321 [<http://perma.cc/688R-V5Y4>].

100. See Matt Ferner, *FDA to Evaluate Marijuana for Potential Reclassification as Less Dangerous Drug*, HUFFINGTON POST (June 25, 2015, 11:59 AM), http://www.huffingtonpost.com/2014/06/24/fda-marijuana_n_5526634.html [<http://perma.cc/G7YG-LPD4>]. Under the CSA, the FDA conducts a scientific and medical analysis of the drug under consideration, makes a recommendation to the DEA that the drug be placed in a given schedule, and then the DEA considers the FDA's analysis, conducts its own assessment, and makes a final proposed rule about how to schedule the drug. *Id.*

101. 21 U.S.C. § 802(6) (2012) ("The term 'controlled substance' . . . does not include distilled spirits, wine, malt beverages, or tobacco . . .").

102. 18 U.S.C. §§ 1956(c)(7), 1957(f)(3) (2012).

requires federal legislative action, which is unlikely given the current political landscape.¹⁰³ This proposal is even more unlikely to generate federal legislative action than the cooperative federalism proposal, since removing marijuana from the CSA does not provide political cover to states' rights conservatives.

Rescheduling marijuana, on the other hand, would not sufficiently resolve the underbanking problem. Under the CSA, marijuana is a Schedule I controlled substance.¹⁰⁴ How a particular substance is scheduled under the CSA effects how restrictively the DEA regulates that substance. A substance that is classified as "Schedule I" has more restrictive licensing requirements, for example, than a substance classified as Schedule II-IV. Since marijuana is a Schedule I substance, physicians cannot prescribe it.¹⁰⁵ Without a prescription for marijuana, an individual cannot possess it under federal law.¹⁰⁶

If Congress rescheduled marijuana as a Schedule II substance, financial institutions could handle the proceeds derived from the sale of a prescription for marijuana without running afoul of federal anti-money laundering laws. Physicians can also technically prescribe Schedule II substances.¹⁰⁷ If marijuana could be prescribed, the sale of marijuana to those with a valid prescription would no longer constitute "unlawful activity" under the MLCA.

A major problem with the rescheduling proposal is that the FDA is highly unlikely to approve marijuana for marketing, meaning physicians will be unable to prescribe it. The CSA operates in conjunction with the Food, Drug, and Cosmetic Act (FDCA). The FDCA requires companies to demonstrate that their drugs are safe and effective for their intended uses before marketing them in the United States,¹⁰⁸ including drugs that are classified as controlled substances.¹⁰⁹ When approving a drug for marketing, the FDA considers a variety of factors, including whether the manufacturer can consistently manufacture a high-quality product and whether the product can provide a consistent dose of the substance.¹¹⁰

103. In fact, H.R. 499, the Ending Federal Marijuana Prohibition Act of 2013—a bill which would have removed marijuana from the CSA's purview—died in committee. See *H.R.499 - Ending Federal Marijuana Prohibition Act of 2013*, CONGRESS.GOV, <https://www.congress.gov/bill/113th-congress/house-bill/499> [<https://perma.cc/8FMK-ZY66>].

104. 21 U.S.C. § 812(c)(10).

105. See *id.* § 829 (stating that substances in Schedules II–V only can be prescribed by a practitioner).

106. See *id.* § 844(a) (making it illegal to possess a controlled substance without a valid prescription from a physician or other medical practitioner).

107. See *id.* § 829(a). That said, even if marijuana was a Schedule II substance, an individual would still violate federal law if he or she possessed marijuana without a prescription.

108. See *id.* § 355(a)–(b).

109. 21 C.F.R. § 290.1 (2015).

110. *Mixed Signals: The Administration's Policy on Marijuana, Part Four—the Health Effects and Science: Hearing Before the Subcomm. on Gov't Operations of the H. Comm. on Oversight & Gov't Reform*, 113th Cong. 34–36 (2014) [hereinafter *Mixed Signals Hearing*] (statement of Douglas C. Throckmorton, Deputy Dir. for Regulatory Programs, Ctr. for Drug Evaluation & Research, Food & Drug Admin., U.S. Dep't of Health & Human Servs.).

Marijuana fails to satisfy the FDA's safety and effectiveness requirements for marketing. Marijuana is a botanical product, and as with all botanical products, a variety of factors affect marijuana's manufacturing and dosage consistency.¹¹¹ First, each marijuana plant can vary significantly in its composition of tetrahydrocannabinol (THC).¹¹² Some marijuana plants produce differing amounts of cannabinoids. Consequently, marijuana patients cannot receive a reproducible dose of active ingredients every time.¹¹³ Therefore, physicians cannot consistently prescribe a certain amount of marijuana to produce an intended effect. Second, since botanical materials can be contaminated by dangerous microbes such as fungi, marijuana is susceptible to these microbes depending on how it is cultivated, harvested, and stored.¹¹⁴ For these reasons, the FDA has not approved marijuana as a safe and effective drug that can be prescribed.¹¹⁵

While rescheduling marijuana as a Schedule II substance will make it technically easier for physicians to prescribe marijuana, the FDA is highly unlikely to approve marijuana for sale by prescription. In fact, the FDA has never approved any botanical material "for sale by prescription," including all of the "botanical raw materials that are listed in Schedule II of the CSA."¹¹⁶ Rather, the FDA approves specific medical products produced by a particular innovator or generic manufacturer.¹¹⁷ This approach explains why the FDA has not approved marijuana prescription sales but has approved the sale of Marinol and Cesamet—specific medical products which incorporate synthetic THC—by prescription.¹¹⁸

If the FDA does not permit marijuana to be sold by prescription, a financial institution could not handle the proceeds from the sale of marijuana, even if rescheduled. Without FDA approval, any sale of marijuana would still be illegal under the CSA and would constitute "unlawful activity" under the MLCA.

Moreover, even if the FDA approved the sale of marijuana by prescription, rescheduling marijuana as a Schedule II substance fails to adequately address the sale of recreational marijuana. Consumers do not have to obtain prescriptions for recreational marijuana. If marijuana-related businesses sold

111. *Id.* at 36.

112. See Kevin A. Sabet, *Much Ado About Nothing: Why Rescheduling Won't Solve Advocates' Medical Marijuana Problem*, 58 WAYNE L. REV. 81, 87 (2012).

113. *Mixed Signals Hearing*, *supra* note 110, at 36; see Sabet, *supra* note 112, at 87–88.

114. Sabet, *supra* note 112, at 87–88.

115. *Mixed Signals Hearing*, *supra* note 110, at 30 ("FDA conducted a review of the available data for marijuana and recommended that marijuana remain in Schedule I, the most restrictive schedule, both because of its high potential for abuse and because there was not sufficient evidence that marijuana had an accepted medical use in treatment in the United States.").

116. Sabet, *supra* note 112, at 88.

117. See CAULKINS ET AL., *supra* note 14, at 99.

118. See *Mixed Signals Hearing*, *supra* note 110, at 67 (statement of Rep. Connolly) (noting that Marinol is a Schedule III drug that is a form of THC); *Cesamet*, LEAF SCIENCE, <http://www.leafscience.com/pharmaceuticals/cesamet/> [<http://perma.cc/NS24-VTQP>].

marijuana to consumers without prescriptions, a financial institution could still not handle the proceeds from these sales because the proceeds would constitute “unlawful activity” under the MLCA.

In sum, while removing marijuana from the CSA resolves the underbanking problem, rescheduling marijuana does not. The rescheduling proposal is an insufficient legal response because it requires an additional legal step—FDA approval of the sale of marijuana by prescription—which is unlikely to succeed, and because it fails to respond adequately to demands posed by the sale of marijuana for recreational purposes.

C. Using Decentralized Virtual Currency

Decentralized virtual currency, such as Bitcoin¹¹⁹ or PotCoin,¹²⁰ is another proposed workaround to the underbanking problem. Some in the marijuana industry have even installed Bitcoin or PotCoin ATMs in their dispensaries.¹²¹ Decentralized virtual currency is not a legitimate policy solution to the underbanking problem, however, because it still implicates federal anti-money laundering laws. Further, criminals often use such currencies as a front for illicit activity, including international drug cartel activity.¹²² Thus, state and industry members should avoid resorting to this option.

“Virtual currencies are online payment systems that may function as real currencies but are not issued or backed by central governments.”¹²³ Since decentralized virtual currency does not require a single administrator or central repository (such as a financial institution) to verify transactions, these currencies can avoid (or evade) many U.S. federal and state financial and banking laws.¹²⁴ This perhaps led some industry members to believe that virtual currencies could avoid federal anti-money laundering laws.

Consider an example of how virtual currency would facilitate transactions in the marijuana industry. Customers would enter a marijuana dispensary with their own Bitcoin or would exchange their U.S. currency for virtual currency at a Bitcoin ATM.¹²⁵ With the now-exchanged Bitcoin, the

119. Kate Cox, *Bitcoin: What the Heck Is It, and How Does It Work?*, CONSUMERIST (Mar. 4, 2014), <http://consumerist.com/2014/03/04/bitcoin-what-the-heck-is-it-and-how-does-it-work/> [<http://perma.cc/5B8B-D5TH>] (“It’s a virtual medium of exchange, not issued by, backed by, or tied to any particular nation or government.”).

120. See POTCOIN, <http://www.potcoin.com> [<http://perma.cc/M48K-J29H>] (explaining that PotCoin is a digital currency).

121. Kashmir Hill, *Marijuana Shop’s Plan to Accept Bitcoin Goes Up in Smoke*, FORBES (Feb. 10, 2014, 8:30 AM), <http://www.forbes.com/sites/kashmirhill/2014/02/10/irony-alert-major-bitcoin-processor-rejects-pot-shop-as-too-legally-dubious/> [<http://perma.cc/J3C2-783L>].

122. See *infra* notes 139–142 and accompanying text.

123. Omri Marian, *Are Cryptocurrencies Super Tax Havens?*, 112 MICH. L. REV. FIRST IMPRESSIONS 38, 38 (2013).

124. JERRY BRITO & ANDREA CASTILLO, BITCOIN: A PRIMER FOR POLICYMAKERS 2 (2d prtg. 2013).

125. See *id.* at 8.

customers would then purchase marijuana products from the marijuana dispensary owner, paying with the Bitcoin.¹²⁶ The entire transaction would be done electronically, and the business would then receive its revenue in Bitcoin.¹²⁷ In essence, the Bitcoin would function as the medium of exchange, taking the place of U.S. currency.

Because decentralized virtual currencies operate as a substitute for U.S. currency during business transactions, some believe federal anti-money laundering laws do not apply to these “currencies.” But decentralized virtual currencies do not avoid federal law, whether in a closed system or open system. A closed system means that the marijuana business owners never exchange the Bitcoin back into U.S. currency but operate their businesses solely using Bitcoin—paying their employees in Bitcoin, making business purchases in Bitcoin, etc.¹²⁸ An open system is one in which marijuana businesses freely exchange Bitcoin for U.S. currency in order to conduct their business operations.¹²⁹

Under a closed system, decentralized virtual currency does not avoid federal anti-money laundering laws and enforcement. For instance, even if the decentralized virtual currency is not exchanged for U.S. dollars, virtual currency can still constitute a “commodity” and is subject to regulation by the U.S. Commodity Futures Trading Commission (CFTC).¹³⁰ While the CFTC does not have policies and procedures specific to virtual currencies,¹³¹ Bitcoin could be interpreted as a commodity if used in futures¹³² or swaps contracts.¹³³ If Bitcoin is a commodity in these particular instances, it is still subject to federal money-laundering enforcement. Under federal law, certain types of brokers and advisors who deal with futures or swaps are required to establish money-laundering programs.¹³⁴ Some are even required to develop

126. *Id.* at 4–5.

127. *Id.*

128. U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-13-516, VIRTUAL ECONOMIES AND CURRENCIES: ADDITIONAL IRS GUIDANCE COULD REDUCE TAX COMPLIANCE RISKS 3–4 (2013), <http://www.gao.gov/assets/660/654620.pdf> [<http://perma.cc/SFM9-AJ5E>].

129. *Id.* at 3–5.

130. 7 U.S.C. § 1(a)(9) (2012).

131. See *The Commodity Futures Trading Commission: Effective Enforcement and the Future of Derivatives Regulation: Hearing Before the S. Comm. on Agric., Nutrition & Forestry*, 113th Cong. 7 (2014) (statement of Timothy G. Massad, Chairman, Commodity Futures Trading Comm'n).

132. A futures contract is a financial contract obligating the buyer to purchase an asset (or the seller to sell an asset) at a predetermined future date and price. Marvin M. Lager, *The Uncertain Definition of a Futures Contract*, L.A. LAW., Mar. 1985, at 40.

133. A swaps contract is “an agreement between two parties to exchange sequences of cash flows for a set period of time.” Michael McCaffrey, *An Introduction to Swaps*, INVESTOPEDIA (Jan. 18, 2007), <http://www.investopedia.com/articles/optioninvestor/07/swaps.asp> [<http://perma.cc/28YH-GQAM>].

134. 31 U.S.C. §§ 5312(c)(1)(A), 5312(a)(2), 5318(a)(2) (2012).

BSA compliance programs, SAR filing requirements, and enhanced customer identity programs.¹³⁵ Consequently, under a closed system, individuals dealing with futures and swaps of Bitcoins stemming from marijuana transactions could run afoul of federal anti-money laundering laws. Thus, even without exchanging Bitcoins for U.S. dollars, virtual currency does not allow businesses to evade federal anti-money laundering laws under all circumstances.

Furthermore, once Bitcoin is exchanged for U.S. dollars in an open system, Bitcoin is still subject to other federal anti-money laundering laws and regulations. In an open system, a virtual currency exchanger—a type of financial institution that exchanges virtual currency for different types of currency—is classified under federal law as a “money transmitter.”¹³⁶ A money transmitter is considered a type of money service business,¹³⁷ and all money service businesses are subject to the BSA and other federal anti-money laundering laws.¹³⁸ Consequently, any virtual currency exchanger would have to comply with federal anti-money laundering laws, including FinCEN’s marijuana-specific BSA guidance.

One of the main advantages of virtual currency—circumventing the federal anti-money laundering laws—is not, in fact, an advantage at all. Whether in a closed or open system, virtual currency cannot evade federal anti-money laundering laws. While a closed system may not implicate federal laws in all circumstances, it is an unattractive business alternative. Most companies, service providers, and consumers do not accept or rely on Bitcoin, so few businesspersons want to operate solely in that currency.¹³⁹ A closed system would simply be impractical, and most people want to convert their Bitcoin into hard currency, such as U.S. dollars. Therefore, an open system is preferable to a closed system. But the open system provides no practical advantage over the current banking system, making virtual currency an impracticable policy alternative.

Additionally, Bitcoin and other virtual currencies are risky. Not only are they subject to significant volatility,¹⁴⁰ but they are often used to funnel funds for criminal enterprises, including international drug cartel activity.¹⁴¹

135. Cf. 31 C.F.R. § 1026.200–.320 (2014) (detailing the reporting and recording requirements for “futures commission merchants and introducing brokers in commodities”).

136. *Id.* § 1010.100(ff)(5); U.S. DEP’T OF THE TREASURY, FIN. CRIMES ENF’T NETWORK, FIN-2014-R001, APPLICATION OF FINCEN’S REGULATIONS TO VIRTUAL CURRENCY MINING OPERATIONS (2014), http://www.fincen.gov/news_room/rp/rulings/pdf/FIN-2014-R001.pdf [<http://perma.cc/U3L2-4L4V>].

137. 31 C.F.R. § 1010.100(ff)(5).

138. *Id.* § 1022.210–.540.

139. See Simone Pathe, *Most Americans Unfamiliar with and Won’t Use Bitcoin*, PBS (Feb. 5, 2014, 12:56 PM), <http://www.pbs.org/newshour/rundown/americans-unfamiliar-wont-use-bitcoin/> [<http://perma.cc/K6ND-GPQ9>] (“76 percent of Americans are still unfamiliar with the digital currency and nearly 80 percent of consumers have never and would never consider using an alternative currency.”).

140. See BRITO & CASTILLO, *supra* note 124, at 20–21.

141. See *id.* at 23–26.

In the Cole Memo, the DOJ indicated that it would not prosecute marijuana-related activity occurring legally under state law as long as such activity does not implicate certain federal marijuana enforcement priorities.¹⁴² One of these priorities is preventing marijuana-related businesses from covering for illegal drug cartel activity.¹⁴³ The widespread use of virtual currency in the legal marijuana industry could raise federal law enforcement concerns.

Because decentralized virtual currencies implicate federal anti-money laundering laws to the same extent as hard currency, and these virtual currencies raise concerns about illicit criminal activity that could implicate federal marijuana enforcement priorities, states should ensure that marijuana-related businesses do not resort to such means. Currently, Colorado does not define a virtual currency exchanger as a money service business under state law.¹⁴⁴ But New York is in the process of doing so.¹⁴⁵ Since virtual currency does not remedy the underbanking problem, states should amend their money transmitter laws to prevent use of this means.¹⁴⁶

III. FINANCIAL COOPERATIVES PROVIDE A VIABLE PATH FORWARD

Federal guidance and commonly touted policy proposals have not and will not remedy the underbanking problem. Therefore, some states have attempted to resolve this problem themselves. For instance, in 2014, Colorado authorized state-licensed marijuana-related businesses to form “cannabis credit co-ops”—a type of financial services cooperative¹⁴⁷—and even approved a state charter for a cannabis-only credit union.¹⁴⁸ Both of these efforts are part of what this Note refers to as the financial cooperative approach. While many commentators rejected the cannabis co-op proposal

142. See Cole Memo, *supra* note 59, at 2–3.

143. *Id.* at 1.

144. See COLO. REV. STAT. § 12-52-103(2), (4.3) (2014) (excluding any reference to “virtual currency exchanger” or “money service business” when defining “money transmission”).

145. See Regulation of the Conduct of Virtual Currency Businesses, 37 N.Y. Reg. 17 (proposed Feb. 25, 2015) (to be codified at N.Y. COMP. CODES R. & REGS. tit. 23, § 200.1–.22); N.Y. DEP’T OF FIN. SERV., PROPOSED NEW YORK CODES, RULES AND REGULATIONS, <http://www.dfs.ny.gov/about/press2014/pr140717-vc.pdf> [<http://perma.cc/GLB7-BC2N>] (“*Virtual Currency Business Activity* means . . . (1) receiving Virtual Currency for transmission or transmitting the same; (2) securing, storing, holding, or maintaining custody or control of Virtual Currency on behalf of others; (3) buying and selling Virtual Currency as a customer business; [or] (4) performing retail conversion services, including the conversion or exchange of Fiat Currency . . .”).

146. A state could limit use of virtual currency by amending the definition of a “money service business” under state law to include virtual currency exchangers.

147. See COLO. REV. STAT. § 11-33-102–108.

148. See Migoya, *supra* note 82.

as a “charade”¹⁴⁹ and as something the Federal Reserve would never authorize,¹⁵⁰ the financial cooperative approach is not as futile as some commentators suggest.

Regardless of what the Federal Reserve may do for policy or political reasons,¹⁵¹ it does have the legal authority to grant a cannabis-only credit union access to its payment system services.¹⁵² Although the Federal Reserve recently denied a cannabis-only credit union access, it did not do so because granting access to a cannabis-only credit union would violate federal anti-money laundering laws.¹⁵³ While this approach still requires federal regulators to grant access, the major advantage of this approach is that it does not require federal *legislative* action. Section III.A explores the financial cooperative approach and specifically the cannabis-only credit union. Section III.B argues that the Federal Reserve has legal authority to grant a cannabis-only credit union access to the Federal Reserve’s payment system services under the Monetary Control Act of 1980 (MCA).

A. *The Financial Cooperative Approach*

Generally, a cooperative “is an autonomous association of persons united voluntarily to meet their common economic, social, and cultural needs and aspirations.”¹⁵⁴ In the context of banking, a financial cooperative is “an institution without capital stock that is organized and operated for

149. David Migoya, *Is the Fed Going to Do What the Banks Won’t Already Do? No.*, DENV. POST, May 18, 2014, at 6K (quoting Bert Ely, a banking structure consultant).

150. See Heather Draper, *Colorado’s New Cannabis Co-Ops Law: Bankers, Pot Advocates Agree It Probably Won’t Work*, DENV. BUS. J. (June 9, 2014, 7:35 AM), http://www.bizjournals.com/denver/blog/finance_etc/2014/06/colorados-new-cannabis-co-ops-law-bankers-pot.html [<http://perma.cc/6PWS-SZB4>] (quoting Don Childears, President and CEO of the Colorado Bankers Association).

151. The Federal Reserve denied access to a cannabis-only credit union in July 2015. See Nathaniel Popper, *Banking for Pot Industry Hits a Roadblock*, N.Y. TIMES (July 30, 2015), http://www.nytimes.com/2015/07/31/business/dealbook/federal-reserve-denies-credit-union-for-cannabis.html?_r=0 [<http://perma.cc/HHX5-Z4HW>].

152. *Id.* (“[I]t will be an uphill battle for the credit union to prove that the Fed does not have the power to turn down the institution.”).

153. Cf. Trevor Hughes, *Federal Bankers: No Account for Colo. Cannabis Credit Union*, USA TODAY (July 31, 2015, 5:50 PM), <http://www.usatoday.com/story/money/business/2015/07/31/federal-bankers-no-account-colo-cannabis-credit-union/30943749/> [<http://perma.cc/WPT2-GXSA>] (noting that the reason for the Federal Reserve’s denial of access to a “master account” was the National Credit Union Administration’s refusal to grant deposit insurance).

154. *Co-Operative Identity, Values and Principles*, INT’L CO-OPERATIVE ALLIANCE, <http://ica.coop/en/whats-co-op/co-operative-identity-values-principles> [<http://perma.cc/LEL7-X8W4>]; see also CHARLES T. AUTRY & ROLAND F. HALL, *THE LAW OF COOPERATIVES 2* (2009) (“(1) [A cooperative] is owned and controlled by the people who use its services or buy its products (its ‘owner/customers’); (2) its primary focus is to provide its services or goods to its owner/customers and not to the general public; (3) it is democratically controlled by its owner/customers, and each owner/customer has one vote regardless of the amount of services or products it purchases from the cooperative; and (4) the primary objective of the cooperative is to maximize benefits to its owner/customers rather than profits.”).

mutual purposes and without profits.”¹⁵⁵ Most financial cooperatives are subject to supervision and examination by a state or federal authority.¹⁵⁶ The credit union is among the most well-known types of financial cooperatives.¹⁵⁷

One option a state could pursue under the financial cooperative approach is to grant a charter for the formation of a cannabis-only credit union.¹⁵⁸ A credit union is a member-owned, not-for-profit financial cooperative that provides savings, credit, and other financial services to its members.¹⁵⁹ A cannabis-only credit union would provide banking and financial services to marijuana-related businesses that are members of the credit union. While credit unions provide many of the same services as other financial institutions, their structure and focus is different. Unlike banks and other financial institutions, which are owned by stockholders and are for-profit institutions, credit unions “pool their members’ savings deposits and shares to finance their own loan portfolios rather than rely on outside capital.”¹⁶⁰ Credit unions seek to provide “a safe place to save and borrow at reasonable rates,” whereas banks generally offer higher interest rates and fees.¹⁶¹

155. AUTRY & HALL, *supra* note 154, at 105.

156. *Id.*

157. *Id.* at 4 (stating that, collectively, credit unions have over 85 million members and assets of over \$700 billion).

158. Another option is for states to pass legislation licensing the formation of cannabis-specific financial cooperatives. Colorado did this in 2014. Under the Marijuana Financial Services Cooperatives Act, the state of Colorado allowed marijuana-related businesses to form “cannabis credit co-op[s].” COLO. REV. STAT. § 11-33-108(2)(a) (2014). Empowered to provide many services, a co-op can accept deposits from members, “[m]ake loans to its members . . . [and] to other [cannabis] co-ops . . . make deposits in state and national financial institutions insured by an agency of the federal government that voluntarily accepts those deposits,” and engage in certain investments. *Id.* § 11-33-107(1). Co-op members include “licensed marijuana businesses, industrial hemp businesses, and entities that provide goods or services to licensed marijuana businesses.” *Id.* § 11-33-106(1). But in order for a marijuana-related business to become a member of the co-op and consequently access its banking services, a business must “provide [] documentation to the co-op of an inability to get comparable services from a bank or credit union.” *Id.* § 11-33-103(5). While a co-op is required to obtain a surety bond, *see id.* § 11-33-113(1)(c), a co-op can obtain approval from the Federal Reserve System Board of Governors. *Id.* § 11-33-104(4)(a). The co-op is not required to obtain federal deposit insurance. *See id.* § 11-33-104(3)(a) (“If federal deposit insurance provided by the federal deposit insurance corporation or national credit union administration becomes available for banks, savings and loan associations, and credit unions organized to provide financial services to the licensed marijuana industry, the commissioner may determine that the continued issuance of charters under this article is no longer necessary or desirable.”). As Professor Hill notes, cannabis-specific financial co-ops likely cannot access the Federal Reserve’s payment services. *See Hill, supra* note 7, at 638–43.

159. *See What Is a Credit Union?*, WORLD COUNCIL OF CREDIT UNIONS, <http://www.wccu.org/about/creditunion> [<http://perma.cc/CK8K-EVB6>].

160. *Id.*

161. Nat’l Credit Union Admin., *How Is a Credit Union Different than a Bank?*, MYCREDIT UNION.GOV, <http://www.mycreditunion.gov/about-credit-unions/pages/how-is-a-credit-union-different-than-a-bank.aspx> [<http://perma.cc/LP3G-MKDZ>].

One advantage of this approach is that a state can use its existing legal authority and regulatory system to grant a charter to a cannabis-only credit union. Since states already authorize state charters for credit unions, this approach does not require the passage of new state legislation. However, all federal-chartered and most state-chartered credit unions are required to obtain federal share insurance from the NCUA,¹⁶² and it is unclear whether the NCUA would provide share insurance to a cannabis-only credit union.¹⁶³ Another disadvantage is that a cannabis-only credit union would also have to comply with FinCEN's BSA requirements, including the marijuana-specific BSA requirements, if the credit union sought federal share insurance.¹⁶⁴

To date, only Colorado has approved a state-chartered, cannabis-only credit union, the Fourth Corner Credit Union.¹⁶⁵ No other state has followed suit. While the Fourth Corner Credit Union requires federal insurance from the NCUA, the credit union can operate under Colorado law while awaiting NCUA approval.¹⁶⁶ Not long before the Federal Reserve's decision in July 2015, however, the NCUA denied share insurance to the Fourth Corner Credit Union.¹⁶⁷

B. *The Federal Reserve's Legal Authorization*

Commentators have criticized Colorado's decision to pursue a financial cooperative solution.¹⁶⁸ Many of these critics assume that the Federal Reserve is unlikely to grant these co-ops access to its payment services.¹⁶⁹ Whether the Federal Reserve *will* grant access is a separate question from whether the Federal Reserve is *legally authorized* to grant access to a cannabis-only credit

162. As Hill reports, "[m]ost states . . . require federal insurance for state-chartered credit unions." Hill, *supra* note 7, at 617–18. But nine states (Alabama, California, Idaho, Illinois, Indiana, Maryland, Nevada, Ohio, and Texas) do not require federal insurance for state-chartered credit unions. Because Colorado and Washington require federal insurance for a state-chartered credit union, a state-chartered, cannabis-only credit union in Colorado or Washington would have to obtain NCUA approval, whereas a cannabis-only credit union in California would not have to seek NCUA approval. *See id.* at 623 n.129.

163. For instance, the insuring of a cannabis-only credit union by the NCUA could be viewed as openly approving a financial institution that is violating federal drug and anti-money laundering laws. *Cf. id.* at 640–41 (noting that the Federal Reserve's reluctance to engage in potential violations of federal law indicates that the NCUA would have similar hesitations). For this reason, the NCUA may deny insurance to a state-chartered, cannabis-only credit union.

164. *See supra* notes 64–68 and accompanying text.

165. *See Migoya, supra* note 82.

166. *Id.*

167. *See Popper, supra* note 151.

168. *See Hill, supra* note 7, at 643 ("One thing, however, is clear: Colorado's cannabis credit co-op legislation is not itself the solution to the marijuana banking problem.").

169. *Id.* at 639.

union or co-op.¹⁷⁰ This Section argues that the MCA authorizes the Federal Reserve to grant a cannabis-only credit union access to the Federal Reserve's payment system services. It then contends that the federal anti-money laundering laws also permit the Federal Reserve to provide such access.

1. Interpretation of the Monetary Control Act of 1980

For a state to pursue a viable financial cooperative approach that would remedy the underbanking problem, a financial cooperative would need a master account with the Federal Reserve and access to the Federal Reserve's payment system.¹⁷¹ Under the MCA, the Federal Reserve must offer payment system services to all "depository institutions."¹⁷² In fact, even if a financial institution is not a member of the Federal Reserve, the Federal Reserve is still required to provide its services at the same price as it does to its member institutions.¹⁷³ The MCA defines depository institutions as banks, credit unions, mutual savings banks, savings banks, saving associations, and federal home loan banks.¹⁷⁴ Here, the central question is whether a cannabis-only credit union is a depository institution under the MCA.

A cannabis-only credit union is legally authorized under the MCA to have an account with the Federal Reserve. The MCA states that any NCUA-insured credit union or any credit union which is *eligible to apply* for federal share insurance through the NCUA constitutes a depository institution.¹⁷⁵ A credit union is eligible to apply for the NCUA's federal share insurance if the credit union is "organized and operated according to the laws of any

170. The Federal Reserve did deny a cannabis-only credit union, the Fourth Corner Credit Union, a "master account" and access to the Federal Reserve's payment system services. Popper, *supra* note 151. The Federal Reserve stated that it made this decision because the cannabis-only credit union could "not prove[] how it would 'mitigate the risk associated with serving a single industry that does not have an established track record of success and remains illegal at the federal level.'" *Id.* Note, however, that the Federal Reserve did not deny access because it lacked the legal authority to do so under the MCA. Moreover, the Federal Reserve's decision is complicated by the fact that the cannabis-only credit union was denied insurance by the NCUA just a few days earlier. The question remains whether the Federal Reserve would have granted access if the credit union obtained insurance. Nevertheless, how the Federal Reserve responded here is a different question from whether the Federal Reserve has the legal authority to make such a decision.

171. Financial institutions use the Federal Reserve payment systems to provide payment services to customers. The Federal Reserve's payment systems include: (1) Fedwire for large electronic payments between financial institutions; (2) coin and currency services; (3) a centralized check collection system; and (4) the Automated Clearinghouse network for processing batched electronic small-dollar payments. Hill, *supra* note 7, at 627–28.

172. 12 U.S.C. § 248a(c)(2) (2012) ("All Federal Reserve bank services covered by the fee schedule shall be available to nonmember depository institutions and such services shall be priced at the same fee schedule applicable to member banks . . .").

173. *Id.*

174. *Id.* § 461(b)(1)(A).

175. *Id.* § 461(b)(1)(A)(iv).

State.”¹⁷⁶ So, if a cannabis-only credit union is organized and operated according to a state’s laws, the Federal Reserve is legally authorized to provide access to its payment system services because the credit union is eligible to apply for federal share insurance.

One problem is that most states require a credit union to insure its accounts with the NCUA before it can be granted a state charter.¹⁷⁷ Without the federal share insurance, a credit union will not only be denied a state charter, but the credit union would also not be organized and operated according to state law. If a credit union is not organized and operated according to state law, it cannot be considered a depository institution under the MCA’s credit union eligibility prong.¹⁷⁸ In effect, states with a federal share insurance requirement for state-chartered credit unions prevent the Federal Reserve from legally recognizing a credit union as a depository institution under the MCA.

A state could get around this problem by passing a law allowing for a cannabis-only credit union to be chartered and operated without obtaining federal share insurance. In lieu of federal insurance, the state could require the cannabis-only credit union to obtain private insurance, or the state could allow the credit union to operate without any insurance. Under this hypothetical solution, this state-chartered credit union could be considered a depository institution under the MCA because the credit union would still be eligible to apply for federal insurance.¹⁷⁹

Political and policy reasons aside, the Federal Reserve does have legal authority to recognize a cannabis-only credit union as a depository institution under the MCA.¹⁸⁰ This is especially true if the cannabis-only credit union is not required by state law to obtain federal insurance, or is required only to apply for federal share insurance through the NCUA.

2. Money-Laundering Complicity

Even if the Federal Reserve is legally authorized to provide a master account and its payment system services to a cannabis-only credit union,

176. *Id.* § 1781(a).

177. *See* INTERNAL REVENUE SERV., *supra* note 24; Hill, *supra* note 7, at 617–18.

178. 12 U.S.C. § 461(b)(1)(A). This account arguably represents what happened in Colorado since the NCUA denied the cannabis-only credit union federal share insurance, and then shortly thereafter, the Federal Reserve denied the credit union a master account. *See* Popper, *supra* note 151.

179. *See* 12 U.S.C. § 461(b)(1)(A)(iv) (requiring only that a credit union be eligible to apply for NCUA insurance).

180. *See id.* § 1781 (stating that the Federal Reserve Board may insure unions organized and operated by the State).

some argue that the Federal Reserve would not do so because it would effectively be violating federal anti-money laundering laws¹⁸¹ or aiding and abetting the manufacturing and distribution of marijuana in violation of federal law.¹⁸²

While the Federal Reserve and its employees could be viewed as openly violating federal drug laws, the concern about money laundering complicity is misplaced. Federal law states that the Federal Reserve is authorized to “examine at its discretion the accounts, books, and affairs of . . . each *member bank* and to require such statements and reports as it may deem necessary.”¹⁸³ The Federal Reserve is also authorized to request an examination of the foreign operations of state banks *which are members* of the Federal Reserve¹⁸⁴ and may provide for “special examination” of *member banks* so as “to inform the Federal reserve bank of the condition of its member banks and of the lines of credit which are being extended by them.”¹⁸⁵ Pursuant to these examination powers, the Federal Reserve has issued a variety of regulations requiring member banks, including state member banks, to implement BSA compliance programs and SAR filing requirements.¹⁸⁶

These aforementioned statutes and regulations regarding the Federal Reserve’s examination powers are confined to member banks, however. Depository institutions encompass both member and nonmember banks, and a cannabis-only credit union, if granted access to the Federal Reserve, would be a nonmember depository institution.¹⁸⁷ Consequently, these examination powers would not extend to a cannabis-only credit union.¹⁸⁸ In fact, the Federal Reserve is authorized only to “require any depository institution . . . to make . . . reports of its liabilities and assets as the [Federal Reserve] Board may determine to be necessary or desirable to enable the Board to discharge its responsibility to monitor and control monetary and credit aggregates.”¹⁸⁹

While the Federal Reserve is authorized to examine financial institutions for compliance with federal anti-money laundering laws, this authorization is constrained to member banks.¹⁹⁰ Since a cannabis-only credit union

181. See, e.g., Hill, *supra* note 7, at 640–41 (“If the Federal Reserve provided payment services to a cannabis credit-co-op, the Federal Reserve and its employees would be engaging in money laundering. . . . [I]t is difficult to imagine the Federal Reserve openly defying federal drug law.”).

182. See, e.g., *id.* at 641 (“They might also be conspiring to manufacture and distribute marijuana, aiding and abetting the manufacture and distribution of marijuana, and acting as accessories after the fact . . .”).

183. 12 U.S.C. § 248(a)(1) (emphasis added).

184. *Id.* § 481.

185. *Id.* § 483.

186. See 12 C.F.R. § 208.60–.64 (2015).

187. See 12 U.S.C. § 1813(c)(1) (“The term ‘depository institution’ means any bank or savings association.”).

188. See *id.* § 248(a)(1) (stating that the Federal Reserve is authorized to examine accounts only of “member” banks).

189. *Id.* § 248(a)(2).

190. See *id.* § 248(a)(1); 12 C.F.R. § 208.60–.64.

would be a nonmember depository institution, the Federal Reserve would not be authorized to examine such an institution for compliance with federal anti-money laundering laws.¹⁹¹ Consequently, the concern about non-compliance with federal anti-money laundering laws may not be an appropriate legal justification for denying a cannabis-only credit union access to the Federal Reserve's payment system services.

In sum, the Federal Reserve is legally authorized to grant access to a cannabis-only credit union, even in light of the Federal Reserve's obligation to enforce federal anti-money laundering laws. Whether the Federal Reserve will actually grant access to cannabis-only institutions is a different question. Nevertheless, if the Federal Reserve does provide access to a cannabis-only credit union, it will significantly ameliorate the underbanking problem.

CONCLUSION

The underbanking problem is a vexing issue facing states and the marijuana industry alike. While calls for federal legislative action are important, Congress is unlikely to act anytime soon. Congress has, however, shown willingness to allow federal regulators to address the underbanking problem facing the states. While it is uncertain whether the Federal Reserve will actually grant access to its payment system services to a cannabis-only credit union, the Federal Reserve is legally authorized to do so under the Monetary Control Act, despite federal anti-money laundering laws. By granting access, the Federal Reserve would significantly mitigate the underbanking problem. Ultimately, when compared to the alternative policy proposals, a financial cooperative approach provides the most viable path forward.

191. See 12 U.S.C. § 248(a)(1) (stating that the Federal Reserve is authorized to examine accounts of "member" banks only, without stating whether it is authorized to examine accounts of "non-member" banks).