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DEPARTMENT OF INSURANCE AND FINANCIAL SERVICES
OFFICE OF CREDIT UNIONS
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DATE: December 19, 2017
LETTER NO.: 2017-CU-03
TO: The Board of Directors and Management of Michigan State-Chartered Credit Unions
SUBJECT: DIFS Issuance of Letter regarding Financial Services and Medical Marihuana¹

The legalization of marihuana for medical purposes under Michigan law, despite remaining illegal under federal law, has the potential to significantly impact the financial services industry. Therefore, financial institution boards must exercise great care toward informed decisions when setting policy regarding if and/or how to provide financial services to the marihuana industry.

The Department of Insurance and Financial Services (DIFS) is providing the attached reference information as a starting point for state chartered credit union officials as they consider the relevant risks and ensure the safety and soundness of their institutions.

This information should not be considered as a replacement for sound legal guidance or further due diligence. Appropriate counsel should be sought and the board should thoroughly understand, and set appropriate policy to mitigate risk exposure prior to providing services in this or any arena.

Sincerely,

John J. Kolhoff, Director
Office of Credit Unions

¹ Michigan law employs the spelling “marihuana” rather than the more common “marijuana” – both terms are used throughout this document with the same meaning.



RICK SNYDER
GOVERNOR

STATE OF MICHIGAN
DEPARTMENT OF INSURANCE AND FINANCIAL SERVICES
LANSING

PATRICK M. McPHARLIN
DIRECTOR

DATE: December 19, 2017
TO: Michigan State Financial Institutions
SUBJECT: Financial Services and Michigan Medical Marihuana¹

The legalization of marihuana for medical purposes under Michigan law has considerable potential impact on state financial institutions, particularly since marijuana remains illegal under federal law. Boards of directors must make informed decisions when setting policy direction regarding providing services to businesses and individuals operating within or on the periphery of the medical marihuana industry. Even a determination to not provide such services must be a deliberate board decision reached through the process outlined below and with the understanding that appropriate risk management systems are necessary to support the prohibition.

Given the significant risks involved, financial institution boards of directors and management teams must:

- Decide whether the institution will provide financial services to medical marihuana industry participants after examining the costs and benefits in addition to the risks of offering such services.
- Perform due diligence to thoroughly understand the legal considerations and the risks as well as the operational framework necessary for conformance with guidance and compliance with Bank Secrecy Act (BSA)/anti-money laundering (AML) expectations.
- Document the institution's decision-making process and development of policies and procedures – board minutes must reflect the considerations, discussions and conclusions.
- Demonstrate the institution has the requisite resources, including staff expertise and capability, for initial and ongoing conformance with guidance and compliance with internal policies and BSA/AML expectations.

Boards and management teams of state financial institutions should carefully review this document, the accompanying FAQs, and any federal guidance, and discuss the implications with legal counsel when considering whether and how to provide financial services to state compliant marihuana related businesses² and/or whether to accept related tax proceeds for transmission to the Michigan Department of Treasury.

¹ Michigan law employs the spelling "marihuana" rather than the more common "marijuana" – both terms are used throughout this document with the same meaning.

² The term "state compliant marihuana related businesses (or MRBs)" refers to businesses and individuals operating within Michigan's medical marihuana laws and rules and any applicable local ordinances, and subject to a strong and effective state and local regulatory and law enforcement system contemplated by the related federal guidance.

Background

Since the Michigan Medical Marijuana Act was passed by voters in November 2008, questions have arisen regarding financial institutions providing services to businesses and individuals engaged in marijuana-related activities. The federal Controlled Substances Act continues to make it illegal to manufacture, distribute or dispense marijuana. In response to this conflict between state and federal law, certain federal authorities have issued guidance addressing marijuana enforcement priorities and Bank Secrecy Act/anti-money laundering responsibilities. The federal guidance rests on the expectation that the state has implemented strong and effective regulatory and enforcement systems to control the cultivation, distribution, sale, and possession of marijuana.

During September 2016, three bills were signed into Michigan law to create a state licensing and regulatory framework for medical marijuana. The Department of Licensing and Regulatory Affairs (LARA) is in the process of establishing this new regulatory structure, which will include promulgating administrative rules, accepting applications and issuing licenses. LARA's Bureau of Medical Marijuana Regulation (BMMR) is responsible for the oversight of medical marijuana in Michigan. The BMMR regulates the state's medical marijuana facilities and licensees, including growers, processors, transporters, provisioning centers, and safety compliance facilities. The bureau also oversees the state's patient registry program and administers the Michigan Medical Marijuana Act. BMMR website: www.michigan.gov/medicalmarihuana.

Federal Guidance

Critical federal guidance for financial institutions considering providing services to state compliant MRBs include:

- Memoranda from United States Deputy Attorney General James M. Cole to All United States Attorneys:
 - dated August 29, 2013, with subject "Guidance Regarding Marijuana Enforcement" (known as "the Cole Memo"):
www.justice.gov/iso/opa/resources/3052013829132756857467.pdf
 - dated February 14, 2014, with subject "Guidance Regarding Marijuana Related Financial Crimes" ("the companion DOJ Memo"):
www.justice.gov/sites/default/files/usao-wdwa/legacy/2014/02/14/DAG%20Memo%20-%20Guidance%20Regarding%20Marijuana%20Related%20Financial%20Crimes%20%2014%2014%20%282%29.pdf
- Guidance FIN-2014-G001 from the U.S. Department of Treasury, Financial Crimes Enforcement Network (FinCEN), dated February 14, 2014, with subject "BSA Expectations Regarding Marijuana-Related Business":
www.fincen.gov/sites/default/files/shared/FIN-2014-G001.pdf

Financial institutions with questions about this guidance are encouraged to contact FinCEN's Resource Center at (800) 767-2825 or FRC@fincen.gov.

State nonmember banks should also see the FDIC's "Statement on Providing Banking Services" issued as Financial Institution Letter FIL-5-2015, dated January 28, 2015: www.fdic.gov/news/news/financial/2015/fil15005.html



Frequently Asked Questions (FAQs)

Providing Financial Services to Medical Marihuana¹ Industry Participants

1. What factors should a financial institution board consider in its decision whether to provide banking services to medical marihuana industry participants?

- Consider availing yourself of independent legal counsel to properly analyze and advise concerning the combined benefits and risks associated with providing services to medical marihuana industry participants.
- Have counsel explain the difference between law and a policy of prosecutorial discretion (or priority setting) related to enforcement of a law.
- Read together and understand the Cole Memo (8/29/2013), the FinCEN Guidance (2/14/2014), and the companion DOJ Memo to U.S. Attorneys (2/14/2014). What do they say in combination?
 - The 8 Principles of the Cole Memo plus the “red flags” spelled out in the FinCEN Guidance must be read together.
 - The Cole Memo (8/29/2013) and the companion DOJ Memo (2/14/2014) must be read together.
- Become familiar with Michigan’s medical marihuana licensing and regulatory framework and the processes available to verify entities are state compliant marihuana related businesses². www.michigan.gov/medicalmarihuana
 - Entities involved in unlicensed activity cannot be afforded financial services under the Cole Memo.

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² The term “state compliant marihuana related businesses (or MRBs)” refers to businesses and individuals operating within Michigan’s medical marihuana laws and rules and any applicable local ordinances, and subject to a strong and effective state and local regulatory and law enforcement system contemplated by the related federal guidance.

- Consider the staffing capability and expertise your institution has in the areas of anti-money laundering (AML) compliance, including Bank Secrecy Act (BSA) knowledge and how to adapt the FinCEN Guidance within the framework of that capability and expertise.
- Consider the practicalities of cash management, your facility's capacity and security issues associated with handling greater amounts of cash than with other merchants.
- Consider the potential impact on your institution's liquidity and interest rate risk positions.
- Consider if there are reputational risks with your existing customer or member base associated with providing services to marijuana merchants.

2. Do the Cole Memo, FinCEN Guidance and companion DOJ Memo change federal law?

- No. As outlined earlier, boards should thoroughly understand the difference between law and priority setting relative to law enforcement.
- The Cole Memo and the companion DOJ Memo are instructions to U.S. Attorneys on the allocation of federal law enforcement resources.
- The FinCEN Guidance is telling financial institutions to exercise *enhanced due diligence*, consistent with the Cole Memo and the companion DOJ Memo, including, as follows:
 - How to perform "know your customer" and monitor the operations of a marijuana business to determine whether it does not implicate one of the 8 Principles of the Cole Memo or the "red flags" specifically set forth in the FinCEN Guidance; and
 - How to report to the FinCEN the activities of these marijuana businesses in relation to transactions involving the institution.

3. What are the monitoring procedures expected under the FinCEN Guidance?

- The "know your customer" requirements in considering whether to open an account for a marijuana business are fairly straightforward and laid out in the FinCEN Guidance.
- The monitoring procedures for existing accounts – including consideration of a range of "red flags" to look for – are also fairly straightforward and laid out in the FinCEN Guidance.
- The "Marijuana Limited" Suspicious Activity Report (SAR), "Continued Activity" SAR, "Marijuana Priority" SAR, and "Marijuana Termination" SAR requirements are detailed and straightforward and should be understandable and capable of being complied with by your institution's BSA/AML compliance staff.

4. Under the FinCEN Guidance, can a state medical marijuana industry participant be subject to adverse enforcement?

Federal enforcement?

- Yes, if it violates one or more of the 8 Principles of the Cole Memo and/or one or more of the activities listed as a “red flag” in the FinCEN Guidance.

State enforcement?

- Yes, if it violates state law or rules.

5. To what extent can financial institutions use the oversight and monitoring of the Bureau of Medical Marijuana Regulation (BMMR) for their own compliance with the FinCEN Guidance?

- Review the FinCEN Guidance and determine:
 - How and when an institution can rely on public records and other public information of the BMMR to monitor marijuana businesses; and
 - When an institution must consider “red flags” that are not necessarily known to the BMMR (and to the extent they are capable of being ascertained by your institution).

6. Can a Michigan financial institution rely on law enforcement, state or federal regulatory agencies or another third party in their oversight and monitoring of their compliance with state law and the current federal enforcement priorities?

- No. The institution’s board is responsible for developing and enforcing appropriate policies to protect the safety and soundness of the institution.
- Ultimately these decisions and the funding of appropriate systems to mitigate the heightened risk profile of this activity is squarely the board’s responsibility.
- As noted above, boards must have an understanding of the current legal environment impacting providing financial services to this industry.

7. Do the Cole Memo, the FinCEN Guidance and the companion DOJ Memo specifically address lending to marijuana businesses?

- The Cole Memo, the FinCEN Guidance and the companion DOJ Memo do not specifically address lending, even though lending is a banking activity.
- Nonetheless, the Cole Memo, the FinCEN Guidance and the companion DOJ Memo provide a set of general standards by which a program of lending to state compliant marijuana businesses could be made in the exercise of proper risk management.

- There is elevated risk in lending by a financial institution due to:
 - The lack of any written guidance to date from the DOJ or financial regulators concerning lending (i.e., only the FinCEN Guidance related to deposits and withdrawals); and
 - The risk that the collateral on secured loans (if any) may be subject to civil or criminal forfeiture.

8. To the extent that the Cole Memo, the FinCEN Guidance and the companion DOJ Memo do not address lending, what are the considerations and set of standards financial institutions should apply with respect to lending to marijuana businesses?

- No lending should be made to any marijuana business that is not a state compliant MRB.
- The types of entities or activities, either directly or indirectly related to the marijuana industry, the board is willing to fund.
- Reserves for loans to state compliant MRBs should be set aside in relation to the specific credit risk profile of the lending relationships.
- Loan terms and pricing should be appropriate relative to the increased risk profile and the necessary risk mitigation activities.
- Covenants appropriate to provide support that the entity operates within the legal parameters of state law and applicable local ordinances.
- The impact on policy collateral requirements of seizure and forfeiture of assets enforcement options available to state, local and federal law enforcement.
- Appropriate protections for the institution in the event of a disruption of the borrower's ability to repay due to legal difficulties.
- Staff resources with sufficient understanding of the market value and liquidation process of industry specific collateral.
- Managers of financial institutions should endeavor to identify loans made to persons who are not engaged in marijuana business but who have a relationship with a marijuana business (e.g., landlord/tenant) that involves collateral for a financial institution loan.

9. If a board decides its institution will not provide financial services to medical marijuana industry participants, does anything further need to be done?

- Yes. The board should communicate this decision via a formal approved policy, and the institution's risk management systems must be sufficient to support the prohibition, including practices, such as:
 - Customer/member due diligence questions during onboarding.
 - Ongoing customer/member screening against state compliant MRB listings for names and addresses.

- Suspicious activity monitoring systems to help identify cash intensive businesses, with further due diligence to ensure cash is not derived from marijuana.
- SAR filings if marijuana-related activity is suspected/detected.
- Staff training.

10. What is DIFS’s position on providing financial services to entities involved directly or indirectly in the medical marijuana industry?

- The State of Michigan and DIFS believe that good public policy dictates state compliant marijuana related businesses should have access to financial services for a host of reasons, notably the safety of our communities.
- The high risk of this activity and the potential impact on any financial institution under the current environment makes it imperative that decisions whether to provide such services be made while fully cognizant of the risks and only after developing appropriate risk management and mitigation systems.
- The impact to the institution’s overall risk profile of the marijuana related activity will be reviewed as part of the examination assessment and ratings process. Examiners will continue to utilize a risk based scoping procedures. Regulatory expectations of the institution’s risk management functions must be commensurate with the inherent risk of the activity to the institution’s safety and soundness.

Disclaimer: The Department of Insurance and Financial Services (DIFS) issues these FAQs as reference information for Michigan state financial institutions. This publication should not be viewed as legal guidance. Boards are encouraged to consult legal counsel for advice based upon their institution’s specific facts, current guidance, and the law.

DIFS does not endorse any vendor providing products or services to the financial industry. Financial institutions are expected to perform appropriate due diligence on all service providers and retain sufficient documentation to support decisions to engage vendors.

Financial institutions providing services to the medical marijuana industry must monitor the current legislative, regulatory and legal environment to determine if continuing to provide such services is feasible. The federal guidance referenced within this document are current as of this writing. The environment could substantially change quickly, particularly the Cole Memo guidance regarding prosecutorial discretion.