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Here's How The CARERS Act Could Change Cannabis Policy

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On March 16, 2015, President Obama made remarks that suggest his views on the legality of cannabis may be "evolving,"[1] but that states will and should lead the way.[2] Less than a week prior, on March 10, a bipartisan group of senators introduced the Compassionate Access, Research Expansion, and Respect States Act "[t]o extend the principle of federalism to State drug policy, provide access to medical marijuana, and enable research into the medicinal properties of marijuana."[3][4]

In sum and substance, this bill, if enacted in its present form, would accomplish the following: (1) exempting from prosecution under the federal drug laws "any person acting in compliance with State" laws pertaining to medical cannabis (2) reschedule cannabis under the Controlled Substances Act[5] from Schedule I to Schedule II except as to lawful medical uses, where it becomes 'unscheduled'; (3) remove from the CSA's definition of marijuana "cannabidiol;" (4) reform banking laws as they relate to a "marijuana-related legitimate business;" (5) allow for federally regulated cannabis research; and (6) allow health care providers of the U.S. Department of Veterans Affairs to give access to veterans who are residents of states with state medical cannabis programs.[6]

While passage of this legislation is uncertain, its introduction is the latest in a series of recent congressional actions. Most significantly, Congress, on a bipartisan basis, recently limited the scope of federal involvement in the enforcement of legal cannabis with Section 538 of the Omnibus Budget Act.[7] Section 538 specifically provides that "[n]one of the funds made available in this Act to the U.S. Department of Justice may be used, with respect to" a list of 32 states and Washington, D.C., "to prevent [them] from implementing their own State laws that authorize the use, distribution, possession, or *cultivation* of medical marijuana."[8] (emphasis added). However, Section 538 has a limited impact because: (1) there is a sunset on Section 538 given that it is a budget bill; (2) Section 538 apparently has no impact on tax and banking laws, regulations and guidelines; and (3) despite the limitations on the DOJ's cannabis enforcement powers and priorities under DOJ guidelines such as the Cole Memorandum, federal enforcement actions may still be in full effect because of other funding sources. If the CARERS Act were to become law, however, it would expand the scope of Section 538, provide greater clarity to the regulated cannabis industry, particularly with regard to banking laws and become a piece of "permanent" legislation.

Section 538 Exists for a Limited Time Only — CARERS Would Be Permanent

Since Section 538 is part of a funding bill, its authority ends when the Omnibus Budget Act expires on Sept. 30, 2015. The CARERS Act, on the other hand, would provide permanent modifications and reformations to existing federal law and enable the U.S. Drug Enforcement Administration, U.S. Food and Drug Administration and Department of Veterans Affairs to implement new regulations.[9] Whether Congress will pass such legislation, what the final form of such legislation would look like and when such legislation would be enacted and implemented are matters of speculation.

Section 538 Prohibits Use of Federal Funds to Enforce Cannabis Law in Certain States; CARERS Act Eliminates Federal Enforcement of Cannabis Laws Per Se Against People Complying with State Medical Cannabis Laws

Section 538 provides that federally appropriated funds cannot be utilized by the DOJ to enforce cannabis law in the medical field where lawfully permitted in the District of Columbia and 32 states listed in the CARERS Act. The DOJ can continue to prosecute, however, where: (a) it pertains to recreational, as opposed to medical, use of cannabis in the enumerated states; (b) it pertains to medical operations where they violate state law (e.g., diversions to the black market);[10] (c) all black market activities (e.g., sales in contravention of state law) in the enumerated states; and (d) activities in other states. As a practical matter, this is a major step forward and will provide significant assurance to operators, investors and ancillary providers in the designated states.

In other words, Section 538 says that U.S. attorneys and members of the DOJ will not be paid and should have no money available to prevent enumerated states from implementing medical cannabis laws. For example, Melinda Haag, a U.S. attorney in Oakland, has continued her three-year pursuit aimed at shutting down one of California's largest medical cannabis dispensaries;[11] it seems her office should not have federal funding available under the CARERS Act to maintain this crusade.[12]

CARERS, however, goes much further than Section 538 in two respects. First, the federal CSA will no longer apply in those states where medical cannabis is permitted, provided the individual complies with applicable state law. That is, the federal statute would decriminalize medical cannabis by stating that the federal CSA would not apply. See CARERS, Section 2. Again, as in Section 538, violations of state law would permit federal enforcement actions and CARERS does not apply to lawful recreational activities. Thus, in a state such as Colorado, which allow dual-operation dispensaries, recreational inventories and sales would still be subject to federal prosecution. Second, CARERS would nationally change the classification of cannabis from a Schedule I to a Schedule II controlled substance. See CARERS, Section 3. This would permit licensed physicians to issue prescriptions for medical cannabis without risking their federal license.

While CARERS recognizes a state's right to legalize and regulate medical cannabis, it does not legalize recreational cannabis at the federal level. Accordingly, the DOJ's Aug. 29, 2013, letter-memorandum known as the "Cole Memo," which detailed eight federal cannabis enforcement priorities for U.S. attorneys, might indicate how the DOJ and DEA would enforce the CSA against marijuana as a Schedule II drug — so long as the Cole Memo remains in effect.[13]

The Cole Memo's guidance "rests on its expectation that states and local governments that have enacted laws authorizing marijuana-related conduct [] will implement strong and effective regulatory and enforcement systems that will address the threat those state laws could pose to public safety,

public health, and other law enforcement interests."[14][15] The DOJ's memorandum dated Feb. 14, 2014, reiterated that the Cole Memo did "not alter in any way the department's authority to enforce federal law, including federal laws relating to marijuana, regardless of state law."[16]

Section 538 Has No Immediate Impact on Federal Tax or Banking Law; CARERS Reforms Banking Law and Partially Modifies Application of Tax Law

Although there is an apparent lack of impact on tax or banking laws by Section 538, Section 6 of CARERS is dedicated to a reformation of banking law that would benefit funding for legal cannabis-related businesses — both medical and recreational — but would leave partially untouched the adverse implications and uncertainties arising as a result of the tax laws.

Regarding the current state of banking laws, the U.S. Department of Treasury, in February 2014, issued guidelines indicating that banks will not be punished for providing services to "legitimate" cannabis businesses in states that have legal cannabis ("FinCEN Guidelines").[17] Even though the FinCEN Guidelines do not differentiate between recreational and medical cannabis laws, they are anchored in the Cole Memo's priorities. The guidelines primarily declare that banks may lend to "legitimate" cannabis business and modify the requisite filing by banks of suspicious activity reports on a cannabis business.[18][19] However, in the DOJ's Feb. 14 memo, which accompanied the FinCEN Guidance, the DOJ stated that "[t]he provisions of the money laundering statutes, the unlicensed money remitter statute, and the Bank Secrecy Act remain in effect with respect to marijuana-related conduct."[20] Accordingly, risks remain to banks that may lend to a legal cannabis business, as no "underlying marijuana-related conviction under federal or state law" is required for the Department of Treasury or DOJ to pursue financial institutions for prosecutions under these laws.[21] Thus, Section 538 does not seem to impact requirements or regulations under banking laws, except that it prohibits the DOJ's use of appropriated funds to prosecute during the current fiscal year. Banks are thereby likely to be very cautious about lend to legal cannabis businesses, or allowing them to open an account, if they do so at all.

CARERS, however, would broadly alter the banking laws, while keeping at least partially intact the FinCEN Guideline's suspicious activity report provisions.[22] Specifically, Section 6(b) of CARERS grants a safe harbor for "depository institutions" from "Federal banking regulator[s]," as defined within CARERS § 6(a), that deal with recreational or medical cannabis businesses acting in compliance with state laws. In short, a federal banking regulator is forbidden from taking the following actions against a depository institution: (1) terminating depository insurance; (2) prohibiting, penalizing or discouraging, including by recommending or incentivizing a depository institution, from providing financial services to legal cannabis businesses; and (3) taking adverse or corrective supervisory actions on a loan to an owner or operator of a legal cannabis business or lessor of real estate or equipment to a legal cannabis business. Furthermore, depository institutions are immunized from federal investigation and prosecution and are not subject to: (1) federal criminal law solely for providing financial services to a legal cannabis business, or (2) criminal, civil or administrative forfeiture for providing a loan to an owner or operator of a legal cannabis business. Therefore, CARERS Section 6 should encourage banks to lend money to legal cannabis businesses, allow them to open depository and other accounts and engage in other banking activities.

Regarding tax law, Section 280E of the tax code prohibits businesses from deducting expenses, other than the costs of goods sold, if they are engaged in the "trafficking in controlled substances (within the meaning of Schedule I and Schedule II of the [CSA])".[23] Presently, cannabis is a Schedule I controlled substance. Section 538 neither changes this provision nor prohibits the IRS from auditing such a

company, assessing taxes or otherwise bringing an enforcement action. Arguably, however, the DOJ could not utilize appropriated funds with regard to forfeiture actions.[24]

CARERS, on the other hand, would cease the application of Section 280E to businesses whose trade is legal medical cannabis. Accordingly, for example, a private medical cannabis dispensary acting in compliance with state law should be able to deduct business expenses. However, concerning legal recreational cannabis, CARERS does not modify the harsh impact of Section 280E. Thus, a recreational dispensary would be unable to deduct expenses from its federal taxes. In a dual-operation state such as Colorado, this unequal treatment of legal cannabis under tax law will harm businesses financially, while also creating difficulty in a business' assessment and calculations of its own taxes.

Conclusion

The passage of Section 538 does not end risks to the legal cannabis industry, while CARERS gives a form of federal protection to persons acting in compliance with a state's medical cannabis law. Section 538 ends on Sept. 30, 2015, and the current Congress may expand, limit, eliminate or keep the same the language of Section 538 in future legislation. Moreover, there is no guarantee of passage of CARERS or the two House bills, and President Obama does not appear poised to expend political capital pushing for any one bill regarding cannabis. Even if CARERS were to pass and be signed into law, the Cole Memo would appear to remain in force for those states without medical cannabis laws, all states with recreational cannabis laws and for any person not in compliance with state cannabis law. Nonetheless, CARERS would reform banking laws and probably thereby encourage more banks to work with legal cannabis businesses in states with legal recreational or medical cannabis. While legal medical cannabis businesses would also receive better tax treatment under CARERS, recreational businesses would still be harmed by Section 280E. Thus, it is clear that risks to the legal cannabis industry would continue under CARERS, albeit less so than under Section 538.

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[1] See Christopher Ingraham, "On marijuana, Obama is content to evolve rather than to lead the way," The Washington Post, March 17, 2015, 4:17 pm, http://www.washingtonpost.com/blogs/wonkblog/wp/2015/03/17/on-marijuana-obama-is-content-to-evolve-rather-than-to-lead-the-way/.

[2] See Niraj Chokshi, "Obama: States decriminalizing pot could pressure Congress to reschedule the drug," The Washington Post, March 16, 2015, http://www.washingtonpost.com/blogs/govbeat/wp/2015/03/16/obama-states-decriminalizing-pot-could-pressure-congress-to-reschedule-the-drug/.

[3] S.683, CONGRESS.GOV, https://www.congress.gov/bill/114th-congress/senate-bill/683/text (last visited March 18, 2015) (hereinafter "CARERS"); see also German Lopez, "Marijuana is now legal in

Washington, D.C. Here's what you need to know." Vox, Feb. 26, 2015, 12:01 a.m., http://www.vox.com/2015/2/26/8108105/marijuana-legalization-washington-dc. Other legislation has been introduced in the House. See April M. Short, "Two Bills To Federally Legalize Marijuana Were Just Introduced In Congress," Reset.me, Feb. 20, 2015, http://reset.me/story/two-bills-legalize-marijuana-federally-just-introduced-congress/. One, the Regulate Marijuana Like Alcohol Act, would let states choose to legalize cannabis free from fear of federal intervention. H.R. 1013, congress.gov, https://www.congress.gov/bill/114th-congress/house-bill/1013 (last visited March 21, 2015). The other, the Marijuana Tax Revenue Act, would tax cannabis sales at the federal level. H.R. 1014, congress.gov, https://www.congress.gov/bill/114th-congress/house-bill/1014/text (last visited March 21, 2015).

[4] As of this writing there are five co-sponsors of the proposed legislation.

[5] 21 U.S.C. § 812.

[6] See CARERS, supra note 4.

[7] H.R. 83, Consolidated and Further Continuing Appropriations Act, 2015, available at http://thomas.loc.gov/cgi-bin/query/F?c113:1:./temp/~c113wDnXRZ:e632:. President Obama signed it into law on Dec. 16, 2014. Interestingly, this Act is the same one that made an attempt to block the implementation of D.C.'s law.

[8] Pub. L. No. 113-59, § 538 (2014), available at http://www.gpo.gov/fdsys/pkg/CPRT-113HPRT91668/pdf/CPRT-113HPRT91668.pdf. The term "implementing" is not defined in Section 538 of the Act. The Ninth Edition of Black's Law Dictionary also does not define the term, but the Fifth Edition of the American Heritage Dictionary of the English Language defines it as "to put into practical effect; carry out." Other dictionaries provide similar definitions.

[9] Obviously, like any other piece of legislation, a future Congress could make changes or repeal the law.

[10] Arguably, if there is a technical violation of state law (e.g., mislabeling, potency, etc.,) even if inadvertent, the prohibition of the use of the appropriated funds would not apply.

[11] See Josh Harkinson, "Why Is This US Attorney So Gung-Ho on Prosecuting a Respected Medical-Pot Dispensary?" Mother Jones, Feb. 17, 2015, http://www.motherjones.com/mojo/2015/02/melinda-haag-weird-federal-war-oakland-harborside-pot-dispensary.

[12] Section 538 notwithstanding, the DOJ may still have available funding from sources other than Congress that allows it to enforce federal marijuana laws against states that have legal marijuana, including medical marijuana. For example, the DOJ maintains pursuant to the Comprehensive Crime Control Act of 1984 an assets forfeiture fund to receive the proceeds of forfeitures and to pay the costs associated with them, including accomplishing the legal forfeiture of property such as marijuana. See 28 U.S.C. § 524. The attorney general is authorized to use the fund to pay any necessary expenses associated with forfeiture operations, such as property seizure, detention, management, forfeiture and disposal. Id. Accordingly, the moneys in the fund are apparently available to use in the seizure and forfeiture of legal marijuana. However, CARERS would appear to protect any person acting in compliance with certain state laws relating to medical marijuana from federal prosecution regardless of the funding source of that prosecution.

[13] See Press Release, Department of Justice Office of Public Affairs, "Justice Department Announces Update to Marijuana Enforcement Policy" (Aug. 29, 2013), http://www.justice.gov/opa/pr/justice-department-announces-update-marijuana-enforcement-policy; Department of Justice Office of the Deputy Attorney General, Guidance Regarding Marijuana Enforcement (Aug. 29, 2013), available at http://www.justice.gov/iso/opa/resources/3052013829132756857467.pdf (hereinafter "Cole Memo").

[14] See id.

[15] Indeed, despite the existence of Section 538, the Cole Memo is influencing states' implementation of recreational marijuana regulatory schemes. For example, the Oregon Liquor Control Commission recently declared that all marijuana sold in a recreational shop must be tracked from seed to sale. See Noelle Crombie, "OLCC doesn't want medical marijuana dispensaries and recreational shops at single location," oregonlive.com, http://www.oregonlive.com/marijuana/index.ssf/2015/02/olcc_doesnt_want_medical_marij.html (last updated March 2, 2015, 9:07 a.m.). In choosing to extend the state's regulation of medical marijuana dispensaries to marijuana production and processing, two of the commissioners cited the Cole Memo as a reason. See id.

[16] See Department of Justice Office of the Deputy Attorney General, Guidance Regarding Marijuana Related Financial Crimes (Feb. 14, 2014), available at http://www.justice.gov/usao/waw/press/newsblog%20pdfs/DAG%20Memo%20-%20Guidance%20Regarding%20Marijuana%20Related%20Financial%20Crimes%202%2014%2014%20(2).pdf (hereinafter "Feb. 14 Memo").

[17] See Department of Treasury Financial Crimes Enforcement Network, FIN-2014-G001,Guidance, BSA Expectations Regarding Marijuana-Related Businesses (Feb. 14, 2014), available at http://www.fincen.gov/statutes_regs/guidance/pdf/FIN-2014-G001.pdf (hereinafter "FinCEN Guidance"); Press Release, Department of Treasury Financial Crimes Enforcement Network, "FinCEN Issues Guidance to Financial Institutions on Marijuana Businesses" (Feb. 14, 2014), available at http://www.fincen.gov/news_room/nr/html/20140214.html; see also Serge F. Kovaleski, "U.S. Issues Marijuana Guidelines for Banks," nytimes.com, Feb. 14, 2014, http://www.nytimes.com/2014/02/15/us/us-issues-marijuana-guidelines-for-banks.html.

[18] See FinCEN Guidance, supra, note 18. The guidelines' existence does not appear to necessarily impact whether banks will allow business to open accounts. See David Migoya, "IRS to bankless Colorado dispensary contesting fines: Too bad," The Denver Post, Feb. 16, 2015 1:21:05 p.m., http://www.denverpost.com/business/ci_27537093/irs-bankless-colorado-dispensary-contesting-fines-too-bad.

[19] Suspicious activity reporting by banks is a major part of the Bank Secrecy Act. See Federal Financial Institutions Examination Council Bank Secrecy Act/Anti-Money Laundering InfoBase, "Suspicious Activity Reporting — Overview," https://www.ffiec.gov/bsa_aml_infobase/pages_manual/OLM_015.htm (last visited March 21, 2015).

[20] See Feb. 14 Memo, supra note 17.

[21] See id.

[22] See CARERS, supra note 4, at § 6(d).

[23] See 26 U.S.C. § 280E.

[24] Section 280E of the tax code prohibits trades or businesses that are legal under state laws from deducting taxes or receiving a credit for amounts paid or incurred during a taxable year if those businesses or trades "consist[] of trafficking in controlled substances (within the meaning of Schedule I and Schedule II of the [CSA])". SeeInternal Revenue Service Advisory Council Office of Professional Responsibility Subgroup, 2014 Public Report 25-27, (Nov. 19, 2014), available at http://www.irs.gov/PUP/taxpros/2014-IRSAC-Full-Report.pdf; see also Migoya, supra note 19.
