

# Medical Cannabis Comes to Maryland: What Finance Professionals Need to Know About this “Budding” Industry

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*\*Views expressed are my own.*

- ▶ Roadmap:
  - ▶ Key Terms
  - ▶ Overview of Maryland Medical Cannabis Program
  - ▶ Federal Law Landscape
  - ▶ Legal Issues Presented by Conflicting Federal-State Laws: Banking, Tax, Investments & More
  - ▶ Issues to Consider in Maryland
  - ▶ Q&A

# Key Terms:

- ▶ Dispensary = A facility licensed by a state to dispense final medical cannabis products to the patient or consumer
- ▶ Grower = A facility licensed to cultivate and harvest cannabis plants for sale to dispensaries or processors
- ▶ Processor = A facility that transforms dried, harvested cannabis flower into a finished cannabis product in the form of an oil, tincture, edible, or wax
- ▶ Testing Facility= A third-party laboratory testing facility licensed to inspect cannabis products for specific contaminants and pesticides, as well as levels of cannabinoids/terpenes/flavonoids present in the specific product prior to consumer/patient sale
- ▶ MMCC= Maryland Medical Cannabis Commission i.e. the state agency charged with regulatory oversight of the medical cannabis program

# Maryland Medical Cannabis Program: The Numbers

- ▶ 14 Grower/Processor Licensees
- ▶ 122 Dispensary Licensees (50 Dispensaries Open and Operating)
- ▶ 2 Third-Party Testing Facilities
- ▶ ~30,000 Registered Patients
- ▶ ~1,000 Registered Providers Authorized to Issue Medical Cannabis Recommendations

# The Economics of Legalization

- ▶ **California: \$61.9 Million in Sales Tax Revenue During First Quarter of 2018**
- ▶ **Colorado: \$247,368,473 in Sales Tax Revenue in FY2017 (Medical and Recreational)**
- ▶ **Oregon: \$70,263,897 in Sales Tax Revenue for FY2017**
- ▶ **Washington: \$315 Million in Sales Tax Revenue for FY2017**

# Maryland Medical Cannabis Program: Dollars and Cents

- ▶ Sales and Use Tax not applied to sales of medical cannabis (i.e. medical cannabis flower, oil cartridge, tincture, salve etc.)
- ▶ Sales and Use Tax applicable to consumption devices and ancillary products (i.e. device used to “vape” cannabis oil, water and non-water pipes, storage containers etc.)
- ▶ Licensing and Renewal Fees = One-time fee of \$125k for dispensary & \$140k for grower/processor license holders; Renewal fees of \$4-6k every other year
- ▶ Jobs!

# So what's the problem?

- ▶ Federal law prohibits the possession, manufacture, and distribution of “marihuana” in any amount, regardless of medical or non-medical use via the Controlled Substances Act of 1972.
- ▶ The term “marihuana” is defined as “All parts of the plant *Cannabis sativa* L., whether growing or not; the seeds thereof; the resin extracted from any part of such plant; and every compound, manufacture, salt, derivative, mixture, or preparation of such plant, its seeds or resin.”
- ▶ The Drug Enforcement Administration has interpreted the CSA to prohibit the possession, manufacture, and distribution of cannabidiol “CBD” products, which is non-psychoactive. The drug is often used to treat Dravet Syndrome, as it is the only treatment known to decrease the number of grand mal seizures experienced by individuals suffering from the disease.

# To put the federal-state law conflict in perspective....

- ▶ Crossing state lines with any amount of cannabis is drug trafficking per federal law, even if crossing from one legalized state to another (i.e. Oregon to Washington)
- ▶ Without uniform regulatory oversight of the industry, it is incredibly difficult to ensure compliance when operating facilities in more than one state
- ▶ The licensing application process is incredibly time-consuming and expensive, so acquiring a license is no small feat



# The Federal Law “Safeguard”

- ▶ Prohibits the Department of Justice from using federal funds to prevent states from implementing laws authorizing the cultivation, manufacture, and distribution of medical cannabis
- ▶ DOJ challenged the meaning of the provision and argued that it did not protect medical cannabis patients and businesses from federal enforcement, as DOJ argued it only protected state actors charged with implementation and enforcement of medical cannabis laws and regulations
- ▶ In 2016, the 9th Circuit Court of Appeals held that the provision extended protection to medical cannabis businesses operating in full compliance with state medical cannabis laws and regulations (No other appeals court has issued a ruling on the matter)
- ▶ Congress first passed the Rohrabacher-Farr Amendment in 2014 as part of a stop-gap spending bill. Since that time, Congress has continuously renewed the provision via short-term appropriations legislation, with the most recent renewal extending the Rohrabacher-Blumenauer Amendment through October 2018
- ▶ As a result, medical cannabis states with robust regulations and enforcement mechanisms are able to avoid federal enforcement actions

# The existing conflict in federal-state law generates a number of unique legal issues for the industry...

- ▶ Billion dollar industry with no (or few) place(s) to bank
- ▶ Inability to secure traditional bank loans
- ▶ Even if you manage to open a bank account, your account could be closed by the bank without warning, meaning any account funds are seized by the bank as well
- ▶ Use of credit cards, PayPal, checks etc. is not an option

# From a Bank and Credit Union Perspective....

- ▶ Banking or providing financial services to a marijuana-related business means....
  - ▶ Compliance with “FinCen” Guidance is mandatory
  - ▶ Filing Suspicious Activity Reports “SARS” for cash transactions or related transactions totaling \$10,000
  - ▶ Failure to monitor and report suspicious activity via SAR is a violation of the Banking Secrecy Act and anti-money laundering laws
  - ▶ You can lose FDIC Insurance
  - ▶ You may be unable to obtain master account access from the Federal Reserve

# Do Businesses in the Cannabis Industry Pay Federal Income Tax?

▶ You Bet!

- ▶ In fact, Section 280E of the IRS Tax Code prohibits the deduction of Business and Operating Expenses for any income derived from “illegal activity”
- ▶ This means most cannabis businesses pay an effective tax rate of over 90%
- ▶ The deductions allowed for Cost of Goods Sold “COGS” is subject to interpretation, but the US Tax Court has previously allowed for COGS deductions by cannabis businesses

# And contrary to popular belief, cannabis investments are hardly a safe bet....

- ▶ Cannabis companies in the United States are not able to issue SEC-registered securities due to federal prohibition
- ▶ If a cannabis company issues non-SEC registered securities, there are restrictions on the sale and transfer of these non-registered securities
- ▶ The cannabis industry is rampant with “snake oil salesmen” so “pump-and-dump” schemes are quite common—prompting SEC officials to issue an official statement on cannabis investments

# And not to mention...

- ▶ Civil Asset Forfeiture = Seizing business assets inc. property without a criminal conviction
- ▶ Perfectly legal remedy invoked by state and local law enforcement agencies in order to generate revenue for enforcement actions
- ▶ Landlords leasing to cannabis businesses are subject to criminal law penalties under federal law, regardless of whether they have knowledge of the tenant's use of the property. The risk of civil asset forfeiture means the landlord could go to jail and pay hefty fines, in addition to losing a property leased to a cannabis business tenant.
- ▶ Any property with a lien or mortgage is a non-starter, as title insurance companies will not allow federally illegal activity to occur on the property because of civil asset forfeiture risk

# Looking to the future...

- ▶ Record-high support for medical marijuana legalization across the U.S., regardless of political affiliation, age, and demographic...it's not if but when cannabis is legalized at the federal level.
- ▶ In Maryland, recreational legalization is on the back burner for now as the medical program finally gets up and running
- ▶ The states that began legalizing medical and recreational cannabis long before Maryland provide fascinating case studies and should serve as models for Maryland lawmakers and regulatory agencies

Questions?



Thank You!

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