Weeding Through the Challenges of Banking the Marijuana Industry

Presented by:
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Old Dominion National Bank
Know your Marijuana Supply Chain

You need to be concerned with more than just:

- Growers of Marijuana
- Processers of the marijuana, where the buds are harvested from the plants. (Budtenders)
- Preliminary distribution – Product design and marketing

- Product Design
- Supply
- Production
- Manufacture

- Distribution
- Retail Sale
- End User Support
Know your Marijuana Supply Chain

Future supply chain components to look for: Extracts, oils, butters, and edibles, and drinkables will proliferate

In addition to product suppliers, marijuana retailers and dispensaries are also increasingly seeking:

- Lawyers,
- Accountants,
- Security consultants,
- Social media
- Couriers
- Quality Control
Know your Marijuana Law

United States: U.S. Cole Memo
United States: FinCEN Guidance
United States: Sessions Memo
Canada: Cannabis Act (Bill: C-45)
Canada: Provincial Regulation (Ex: Bill 174, 26, etc.)
Defining “Marijuana Related Business”

**TIER I:** “Touch” marijuana at any point from seed-to-sale. Generally correlates to the definition of “MRLB” in proposed federal legislation, although it also captures “illegitimate” marijuana businesses.
- Growers, processors, wholesalers, dispensaries, etc.

**TIER II:** Generally do not “touch” marijuana, but are focused on providing products and services specifically to Tier I MRBs and the marijuana industry as a whole. Majority of revenues expected to come from Tier I MRBs.
- Suppliers, security firms, licensing consultants, etc.

**TIER III:** Provide products and services to Tier I MRBs incidentally to base business, but Tier I MRBs and marijuana industry are not a focus.
- Professional services, landlords, financial services, etc.
Developing a Marijuana Related Business Plan

Steps to Decision Making

1. Classify what is a MRB
2. Identify which type of MRB fits within your risk appetite
3. Determine the products and services offered only to the specific MRB type
4. Identify and build specific MRB monitoring reports
5. Assess the number of FTEs needed
   * Frontline
   * Back office
6. Cost Benefit Analysis
Overall AML/CTF Program Risk Assessment

FI should be considering the following when updating their overall AML/CTF program risk assessment:

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
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</thead>
<tbody>
<tr>
<td><strong>1</strong></td>
<td><strong>2</strong></td>
</tr>
<tr>
<td>Address the legal, reputation, compliance, financial, geographic risk associated with banking marijuana-related businesses.</td>
<td>Specifically evaluate the increase in third party risk to address heightened regulatory expectations.</td>
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<td><strong>4</strong></td>
<td><strong>5</strong></td>
</tr>
<tr>
<td>Perform an analysis of the number of customers considered a marijuana-related businesses and the number of accounts serviced and average dollar amount in relation to the entire customer base.</td>
<td>Ensure the overall inherent risks of banking marijuana dispensaries are fully identified, risk rated and applicable red flags are included.</td>
</tr>
</tbody>
</table>
Risk Assessment

FI should address the adequacy of their surveillance monitoring, automated or manual, by identifying red flags linked to illicit marijuana businesses and align those risks to monitoring reports, rules, scenarios, thresholds, parameters or controls established within their AML/CTF monitoring program.

1. Red Flags/Typologies
2. Out of demographic cash deposits
3. Wire activity to/from HR geographies
4. Non-business related transactions
5. Disguised accounts, velocity, payments from multiple accounts from multiple institutions, etc.
## Suspicious Activity Monitoring Program

FI should decide on the appropriate presentation and level of documentation based on the bank’s risk profile. Below offers an example for documentation.

<table>
<thead>
<tr>
<th>Risk &amp; Red Flag Description</th>
<th>Typology</th>
<th>Risk Mitigation/Controls</th>
<th>Mitigate Type</th>
<th>Probability</th>
<th>Impact</th>
<th>Overall Risk (PXI)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Identify &amp; List Red Flags</td>
<td>Method used to launder proceeds</td>
<td>Corresponding rules, scenarios, reporting, and/or monitoring</td>
<td>Automated/Manual</td>
<td>Possible</td>
<td>High</td>
<td>Moderate</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Risk</th>
<th>Risk Description</th>
<th>Inherent/Initial Risk Rating</th>
<th>Existing Controls</th>
<th>Residual/Adjusted Risk Rating</th>
<th>Action Items</th>
</tr>
</thead>
<tbody>
<tr>
<td>High level description of the AML/CTR risk related to the cannabis industry</td>
<td>Describe the risk in more detail</td>
<td>2 - Moderate</td>
<td>What existing controls do you currently have in place</td>
<td>1 - Low</td>
<td>Identify any action items to assist (as applicable) to further mitigate the risks.</td>
</tr>
</tbody>
</table>
## Account Review/Identification of FinCEN Red Flags (Example)

<table>
<thead>
<tr>
<th>Guidance Cites</th>
<th>Account Testing/Red Flags</th>
<th>Yes/No</th>
<th>Notes</th>
</tr>
</thead>
<tbody>
<tr>
<td>FIN-2014-G001</td>
<td>Receive substantially more revenue than may reasonably be expected given the relevant limitations imposed by the state in which it operates?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>FIN-2014-G001</td>
<td>Receive substantially more revenue than its local competitors or than might be expected given the population demographics?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>FIN-2014-G001</td>
<td>Deposit more cash than is commensurate with the amount of marijuana-related revenue it is reporting for federal and state tax purposes?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>FIN-2014-G001</td>
<td>Fail to or is unable to demonstrate that its revenue is derived exclusively from the sale of marijuana in compliance with state law, as opposed to revenue derived from (i) the sale of other illicit drugs, (ii) the sale of marijuana not in compliance with state law, or (iii) other illegal activity?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>FIN-2014-G001</td>
<td>Make cash deposits or withdrawals over a short period of time that are excessive relative to local competitors or the expected activity of the business?</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Guidance Cites</td>
<td>Account Testing/Red Flags</td>
<td>Yes/No</td>
<td>Notes</td>
</tr>
<tr>
<td>---------------</td>
<td>-----------------------------------------------------------------------------------------</td>
<td>--------</td>
<td>-------</td>
</tr>
<tr>
<td>FIN-2014-G001</td>
<td>Engage in rapid movement of funds, such as cash deposits followed by immediate cash withdrawals?</td>
<td>No</td>
<td></td>
</tr>
<tr>
<td>FIN-2014-G001</td>
<td>Allow deposits by third parties with no apparent connection to the accountholder?</td>
<td>No</td>
<td></td>
</tr>
<tr>
<td>FIN-2014-G001</td>
<td>Engage in excessive commingling of funds with the personal account of the business’s owner(s) or manager(s), or with accounts of seemingly unrelated businesses?</td>
<td>No</td>
<td></td>
</tr>
<tr>
<td>FIN-2014-G001</td>
<td>Include individuals conducting transactions for the business that appear to be acting on behalf of other, undisclosed parties of interest?</td>
<td>No</td>
<td></td>
</tr>
<tr>
<td>FIN-2014-G001</td>
<td>Submit financial statements that are inconsistent with actual account activity</td>
<td>No</td>
<td></td>
</tr>
<tr>
<td>FIN-2014-G001</td>
<td>Fail to or is unable to demonstrate the legitimate source of significant outside investments?</td>
<td>No</td>
<td></td>
</tr>
<tr>
<td>FIN-2014-G001</td>
<td>Engage in international or interstate activity, including by receiving cash deposits from locations outside the state in which the business operates, making or receiving frequent or large interstate transfers, or otherwise transacting with persons or entities located in different states or countries?</td>
<td>No</td>
<td></td>
</tr>
<tr>
<td>FIN-2014-G001</td>
<td>If a retail outlet: only sells marijuana, marijuana infused products and marijuana paraphernalia? If a retail outlet: only sells marijuana advertised for medical purposes if the retailer has a “medical marijuana endorsement.”</td>
<td>No</td>
<td></td>
</tr>
</tbody>
</table>
## Account Review/Identification of FinCEN Red Flags (Example)

<table>
<thead>
<tr>
<th>Guidance Cites</th>
<th>Account Testing/Red Flags</th>
<th>Yes/No</th>
<th>Notes</th>
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</thead>
<tbody>
<tr>
<td>DOJ- Cole Memo</td>
<td>Does/how the MRB prevent the distribution of marijuana to minors?</td>
<td></td>
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<tr>
<td>DOJ- Cole Memo</td>
<td>Does/how the MRB prevent revenue from the sale of marijuana from going to criminal enterprises, gangs, and cartels (LCB and FI)?</td>
<td></td>
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<tr>
<td>DOJ- Cole Memo</td>
<td>Does/how the MRB prevent the diversion of marijuana from states where it is legal under state law in some form to other states (LCB)?</td>
<td></td>
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<tr>
<td>DOJ- Cole Memo</td>
<td>Does/how the MRB prevent state-authorized marijuana activity from being used as a cover or pretext for the trafficking of other illegal drugs or other illegal activity?</td>
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<tr>
<td>DOJ- Cole Memo</td>
<td>Does/how the MRB prevent violence and the use of firearms in the cultivation and distribution of marijuana?</td>
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<tr>
<td>DOJ- Cole Memo</td>
<td>Does/how the MRB prevent drugged driving and the exacerbation of other adverse public health consequences associated with marijuana use?</td>
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<tr>
<td>DOJ- Cole Memo</td>
<td>Does/how the MRB prevent the growing of marijuana on public lands and the attendant public safety and environmental dangers posed by marijuana production on public lands?</td>
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<tr>
<td>DOJ- Cole Memo</td>
<td>Does/how the MRB prevent marijuana possession or use on federal property</td>
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</tbody>
</table>
Customer Due Diligence for MRBs

KYMRB – Know Your Marijuana Related Business

Business and Customer Risk Assessment

KYC – MRB Specific Questionnaire

Diagram:
- Ownership and Control
- Locations & Markets Served
- Geographic Location & Domicile
- Purpose of Account
- Products and Services Offered
- Customer Base
- Source of Funds & Wealth
- Anticipated Account Activity
Risk Mitigation Through EDD – US Perspective

- Review state license, application, tax returns, financial statements, business and financial plan
- Verification of state license and registration
- Perform a background check and confirm identifying information against public records
- Review promotional materials, including website and conduct periodic onsite visits
- Request the existence of a written AML/CTF program
- Review 3rd parties and vendors and perform due diligence commensurate with risk
- Refresh and validate information on marijuana-related business including publicly available information
- Review written policies and procedures from marijuana related business
- Evidence of consideration as to whether the business appears to breach any enforcement policies
Best Practice Recommendations

- Update AML/BSA Risk Assessment and evaluate Enterprise Wide Risk Assessment
- Identify marijuana-related relationships at account opening and evaluate risks
- Revise AML/BSA/OFAC/CIP and Training program to address marijuana-related businesses
- Maintain a “Marijuana Termination” SAR log and notify second Bank through 314(b)
- Ensure marijuana-related business relationships are considered within the SAM and OFAC program
- Review and update the manual and/or automated transaction monitoring system to ensure thresholds and parameters have been set to assist in identifying red flags outlined in regulatory issues guidance
- Treat marijuana dispensaries as ineligible customer types for CTR exemptions
- Scrub customer base names and addresses against a listing of approved dispensaries’ names, owners and addresses to identify unknown accounts
- The Risk Committee or Board of Directors Reporting should be made aware of key risk indicators related to marijuana business-related accounts. Board of Directors should approve the Bank offering FI services to MRB.
Best Practice Recommendations

- Consider allocating a compliance officer and/or FTE responsible for monitoring the marijuana-related business
- Consider setting appropriate limits to the MRB program? (type of license [producer, processor, and/or retailer] accepted, number of accounts, total amount allowed to be deposited, etc.)
- Establish risk-based pricing standards for MRB deposit and loan account. In addition to service fees, risk-based pricing for deposit accounts could include retainers to cover FI cost in event of a seizure.
- Ensure the institution has the staffing resources necessary to perform sufficient due diligence and ongoing monitoring on the MRB accounts, particularly given the size, nature, and risk inherent in the individual customers?
- Perform a transaction volume and dollar comparison of all marijuana dispensary accounts in relations to other marijuana-related businesses to identify any significant variances in businesses activity.
- Establish a contingency plan which includes an exit from the business line should their be a chance in the policies and forbearances from Federal and State Governments
Education and Training

1. Financial Institution
   - Who do I need to provide training to?
   - What do I need to provide training on?
   - Front-Line/Agents
   - Back-office
   - Board of Directors
   - Identify unusual activity/typologies
   - Red flags / Cannabis Act violations

2. Clients
   - What do I need to provide training on?
   - FI obligations/responsibilities
   - FI policies and procedures
   - How they can help
   - Reporting responsibilities

3. Regulators & Examiners
   - Compliance program enhancements
   - Education efforts
   - Examine against guidance
   - Who is responsible for what

The only thing you need to do now is to create the training program and execute it.
Where to start....
MRB Implementation Checklist

<table>
<thead>
<tr>
<th>Category</th>
<th>Task</th>
<th>Details/Comments</th>
<th>Responsible Party</th>
<th>Completed Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>Policies</td>
<td>BSA Policy</td>
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<td></td>
<td>OFAC Policy</td>
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<tr>
<td></td>
<td>CIP/New Acct Opening Policies</td>
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<tr>
<td>Procedures</td>
<td>New Acct Opening Procedures</td>
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<tr>
<td></td>
<td>Update Cash Reporting/Exemption aggregation procedures</td>
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<tr>
<td></td>
<td>Suspicious Activity Monitoring and Reporting Procedures &amp; Standards</td>
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<td></td>
<td>Update OFAC scanning Procedures</td>
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<tr>
<td></td>
<td>Update CDD, EDD and HR Customer Monitoring Procedures and Standards</td>
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<tr>
<td>Bank Forms</td>
<td>Acct Opening Worksheets</td>
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<tr>
<td></td>
<td>MRB Acct Opening Questionnaire and/or Refresh Worksheet</td>
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<tr>
<td>Onboarding Process</td>
<td>What will you collect?</td>
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<tr>
<td></td>
<td>What types of MRBs will you allow?</td>
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<td></td>
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<tr>
<td></td>
<td>What fee will you assess?</td>
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<tr>
<td>System Changes</td>
<td>Relationship Codes/Train -Codes</td>
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<td></td>
<td>Ability to collect additional CDD information, including expected activity</td>
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<td></td>
<td>Ability to create reports (or update SAMs) of accts whose activity differs from expected or peer groups</td>
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<tr>
<td>Training</td>
<td>Training branch personnel</td>
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<td></td>
<td>Training central operations/back-office personnel</td>
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<td></td>
<td>Training BSA/AML/Compliance department</td>
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<tr>
<td></td>
<td>Other departments (as necessary)</td>
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</table>
Cannabis Task Force Committee

- Leverage professional networks to develop a cannabis task force/committee/peer group
- Utilize industry experts, regulatory relationships & professional networks
  - Peer Compliance Officers
  - Regulatory Agencies
  - Law Enforcement
  - Health Canada
  - FINTRAC

- Meetings
  - Regulatory and industry updates
  - Understanding/shaping best practices
  - Emerging Trends
5 Key Takeaways

1. Successfully banking MRBs can be accomplished; however, a FI needs to be as aware as possible of all of the legal uncertainty and challenges when pursuing banking.

2. Cost Benefit Analysis: Consider the revenue of banking MRBs vs. scrutiny from Regulators and Law Enforcement.

3. You need clear, written marijuana-related policies and procedures, which you enforce consistently (simply saying "no marijuana" is not enough).

4. Show regulators that you have adequate and effective methods to identify marijuana-related accounts...willful blindness is not a safe strategy!

5. Training is everything. Remember, "An educated customer is a benefit to bank compliance."