

Legal Sidebar

Credit Union's Plan to Serve the Marijuana Industry Goes Up in Smoke

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The [Fourth Corner Credit Union](#) (TFCCU) is attempting to become the nation's first depository institution devoted to providing financial services to medical and recreational marijuana businesses operating in compliance with state law. Although TFCCU's credit union charter has been approved by the Colorado Division of Financial Services, its ability to begin providing services to the marijuana industry is contingent upon acquiring deposit insurance through the National Credit Union Administration (NCUA) (or possibly from a private insurer) and getting approval from the Federal Reserve Bank of Kansas City (FRB-KC) to establish a FRB [Master Account](#). As TFCCU [explains](#):

Every depository institution must have (and does in fact have) access to the Federal Reserve payments system, either by having a master account, or by having access through a correspondent. Without such access, a depository institution is nothing more than a vault. Cash deposited at a financial institution is transported to the Federal Reserve Bank branch. It is credited to the depository institution's account and the cash becomes an electronic credit. Credits and debits from transactions with other depository institutions are settled in the institution's account at the Federal Reserve Bank where an institution's master account is maintained. In basic terms, an account at the Federal Reserve Bank is the depository's bank account.

In short, an FRB Master Account is the key to gaining access to the electronic payment system on which modern commerce heavily relies. After around nine months of waiting for a decision that generally only takes [5-7 days](#), TFCCU finally received word from FRB-KC that its application for a Federal Reserve Bank Master Account was rejected. FRB-KC's rejection came on the heels of NCUA's decision to deny TFCCU federal deposit insurance. TFCCU responded by filing lawsuits against both [FRB-KC](#) and [NCUA](#) seeking declaratory judgments overturning the decisions.

As has been noted in several [previous](#) Legal [Sidebar posts](#) and a CRS [report](#), although more than 20 states have enacted laws legalizing dispensing of medical marijuana and four of them (Colorado, Washington, Oregon, and Alaska) authorize state-licensed retailers to sell small amounts of marijuana in-state for recreational use, the sale of marijuana—even as permitted under state law—is unlawful under federal law. Marijuana is classified as a [Schedule I](#) Controlled Substance under the federal Controlled Substances Act (CSA). The [manufacture, distribution, or possession](#) of marijuana is subject to federal criminal penalties. Moreover, the federal [Bank Secrecy Act \(BSA\)](#) and [criminal anti-money laundering \(AML\) statute](#) prohibit anyone from conducting monetary transactions in property derived from the sale of marijuana. This likely would include an FRB processing payments derived from recreational marijuana sales for a depository institution. Financial transactions with marijuana-related businesses generally must be reported as suspicious because they fall clearly within the language of the federal AML statutes.

Because of these reporting requirements and the fact that processing such transactions might provide a basis for a federal prosecution for aiding and abetting the underlying violation of the CSA, [many banks](#) appear to be declining to provide financial services, such as opening checking accounts or establishing credit card merchant relationships, to state-authorized marijuana-related businesses. A Department of Justice (DOJ) announcement regarding its marijuana [prosecution policy](#) and [guidance](#) issued by Treasury's Financial Crimes Enforcement Network (FINCEN), which is designed to provide a roadmap for banks to comply with the BSA when providing banking services to state-authorized marijuana-related businesses, apparently have not led to large numbers of banks and credit unions

establishing relationships with marijuana dispensaries.

TFCCU [wants](#) to fill this void. TFCCU states that it has [developed](#) a BSA/AML compliance regime designed specifically to comply with the federal guidance for providing financial services to state-legalized marijuana industry. According to the credit union, the compliance regime was developed in consultation with “a world-renowned anti-fraud and anti-money-laundering expert ... [and] experts in the fields of law, technology, the psychology of fraud and money laundering, specialist risks insurance, marijuana regulation, forensic accounting and law enforcement.” The compliance regime would include “[a]n industry first ‘Active AML Unit’” within TFCCU that would “combine desk-top research and fact finding now used by financial institutions with field audits of member businesses, intelligence gathering, and working with local law enforcement and State and municipal regulators of the legalized cannabis industry.”

In spite of these efforts, NCUA [denied](#) TFCCU’s application for insurance stating that, for a number of reasons, the “NCUA cannot conclude that the credit union has established proper policies and procedures to effectively manage its BSA/AML program ... [thus creating] an unacceptable risk to the share insurance fund.” Approximately two weeks later, FRB-KC notified TFCCU that it denied the credit union’s master account application due to the fact that NCUA would not provide it deposit insurance.

TFCCU’s [complaint](#) against NCUA alleges, among other things, that the way in which NCUA decided to deny the application for deposit insurance violated TFCCU’s rights under the Fifth Amendment’s Due Process Clause and that, by justifying the denial of the application for the reasons that it did, “NCUA acted arbitrarily, capriciously, not in accordance with law and abused its discretion” in violation of the federal Administrative Procedure Act (APA). The [complaint](#) against FRB-KC alleges that, pursuant to federal law ([12 U.S.C. §248a\(c\)\(2\)](#)) and FRB guidance, FRB-KC lacks the discretion to deny a Master Account to a depository with a state-approved charter that is in good regulatory standing. Thus, TFCCU argues that it “is entitled to a Master Account at the FRB-KC.”

Rulings in favor of TFCCU in these lawsuits have the [potential](#) to greatly expand the marijuana businesses’ access to financial services, which, in turn, could help the fledgling industry thrive. However, success in the courtroom wouldn’t necessarily guarantee that TFCCU would get everything it desires. For example, TFCCU probably wouldn’t consider it much of a victory if, as a result of the litigation, FRB-KC opened a Master Account for TFCCU but refused to process any payments through the account that FRB-KC suspects are linked to unlawful marijuana sales.