

**MJBIZDAILY EXCLUSIVE REPORT**

# **NAVIGATING THE RAPIDLY EMERGING FIELDS OF CANNABIS AND HEMP LAW**

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# NAVIGATING THE RAPIDLY EMERGING FIELDS OF CANNABIS AND HEMP LAW

Legal medical marijuana and recreational sales could eclipse \$12 billion this year, according to the 2019 Marijuana Business Factbook, and might soar to roughly \$28 billion by 2023.

Those figures come from 36 states with medical marijuana laws and 10 that have commercial recreational cannabis statutes.

This report, compiled exclusively for the American Bar Association, will give you a deeper understanding of some of the legal trends and issues that vex a multibillion-dollar industry that remains unlawful at the federal level.

Some of those issues also carry over to marijuana's cousin, hemp. Even though the 2018 Farm Bill legalized cannabis with less than 0.3% THC by dry weight, many uncertainties remain.

Highlights from this report include:

- Marijuana policy reform discussions at the federal level are moving forward incrementally, with congressional hearings and bipartisan support constituting the new normal. Comprehensive reform, however, looks unlikely before the 2020 elections.
- The legal marijuana industry is mostly cash-based, creating issues around public safety and raising capital. Even hemp farmers and businesses report difficulties securing banking services.
- If you hang around the marijuana industry for any length of time, you'll hear complaints about 280E. This provision of the IRS tax code prohibits businesses deemed to be "trafficking in controlled substances" from taking ordinary tax deductions or credits.
- Stiffer environmental requirements focused on the use and management of energy, water, waste and pesticides are coming for cannabis. The shift reflects increasing concerns about climate change and pressures on natural resources.
- Patents are no longer completely out of reach for marijuana-related products involving and combining CBD extracts, THC, essential oils, vitamins, drugs and alcohol. Non-plant-touching devices also are receiving protections, such as extraction technologies, vaping devices and cultivation lights.
- An increasing number of civil lawsuits have been filed against marijuana businesses under the federal Racketeer Influenced and Corrupt Organizations Act (RICO). The argument is that even state-licensed marijuana enterprises constitute federally illegal drug trafficking activity. Experts disagree about the dire threat these lawsuits pose to the industry, but the legal costs are high.

The cannabis industry is ever-changing, and these are just a handful of the legal issues facing operators in the industry today.

# FEDERAL REFORM

Marijuana policy discussions on Capitol Hill have sparked a large dose of “Reefer Madness” and Rocky Mountain High jokes over the years.

But today the topic garners respect, marked by a new normal:

- Landmark congressional hearings.
- An increasing number of backers, including large industry groups such as the American Bankers Association.
- Strong public support.
- A 2018 election shift in the U.S. House to the Democrats, who tend to be more pro-marijuana.

But while marijuana reform has come far in Washington DC in recent years, odds aren't great that a comprehensive bill will pass before the 2020 elections.

**The biggest obstacle:** The U.S. Senate, led by Mitch McConnell, a Kentucky Republican. As majority leader, McConnell has virtual control over the Senate schedule.

And while he shepherded a Farm Bill that legalized hemp in 2018, his statements suggest he remains opposed to marijuana.

**The wild card:** President Donald Trump. If Trump wants something done on the issue, McConnell is likely to follow.

The 2019 Marijuana Business Factbook estimates that annual sales of legal cannabis in the United States could eclipse \$12 billion in 2019 and reach \$30 billion by 2023.

Billions of dollars are still lost to the illicit market, so legalization at the federal level could enable the industry to nab an even bigger portion of the overall demand.

Here are a few bills that the industry is monitoring closely:

- Secure and Fair Enforcement (SAFE) Banking Act, which would enable financial institutions to serve state-lawful cannabis businesses without fear of federal prosecution. The measure could be voted on by the full House this fall, but the Senate is a longshot.
- Strengthening the Tenth Amendment Through Entrusting States (STATES) Act, which would protect state-lawful cannabis businesses from federal interference. This bill seems to have lost support from the progressive wing of the Democratic Party because it does not include specific provisions to help individuals and communities disadvantaged by the war on drugs.
- Marijuana Opportunity Reinvestment and Expungement (MORE) Act of 2019, which would decriminalize and deschedule cannabis, as well as expunge certain cannabis offenses. As House Judiciary chair, U.S. Rep. Jerrold Nadler, a New York Democrat, has the clout to get this comprehensive reform bill heard at least in his committee.

## HEMP

The landmark 2018 Farm Bill removed hemp from the Controlled Substances Act and legalized hemp-derived cannabinoids (such as CBD) with no more than 0.3% THC.

The legislation marked the most consequential change to the Controlled Substances Act since its enactment in 1971.

Hemp Industry Daily projects hemp-derived CBD retail sales alone will soar from nearly \$1 billion this year to as much as \$7.5 billion in 2023.

Here are some key hemp provisions:

- A single, nationwide set of hemp rules will be overseen by the U.S. Department of Agriculture, which is expected to release rules in time for the 2020 growing season.
- States are allowed to submit individual hemp-regulatory plans to the USDA, which must be approved or rejected within 60 days – though there's some uncertainty about when that 60-day period actually begins.
- More than 40 states have at least limited hemp programs, and more than a dozen have active commercial programs.
- U.S. territories and Native American tribes also are allowed to regulate hemp.

Some thorny legal issues persist:

- The Farm Bill permits the interstate transportation of hemp and hemp products. But with federal hemp rules not yet in place, the crop is being seized as drug contraband in some states, such as Idaho.
- The U.S. Food and Drug Administration is getting increasingly involved in regulating CBD. The agency has reiterated that CBD is banned as an additive to food and dietary supplements and has subsequently cracked down on some companies making medical benefit claims.

## READ MORE

- [New normal in U.S. Congress: Marijuana hearings, reform bills & how they could affect the industry](#)
- [A New Day in Hemp](#)
- [FDA exec: Don't expect an exception for CBD](#)

# FINANCIAL MATTERS

## BANKING

The legal marijuana industry suffers from a lack of legitimate banking services, which creates a dangerous cash-only economy and a scramble for capital for operations and growth.

Some financial institutions have been willing to take the risk and the additional compliance costs to serve certain state-legal markets, but such services come at a high cost for marijuana businesses.

One executive told congressional lawmakers at a hearing earlier this year that his medical marijuana company pays a fee of \$3,000 a month just to maintain a bank account.

Politicians, prosecutors and financial industry associations increasingly are advocating for reform, saying that the current system not only poses public safety risks but also increases the likelihood for financial fraud such as money laundering.

The groups have rallied in support of legislation such as the SAFE Banking Act, which would enable financial institutions and insurance companies to serve cannabis-related firms without fear of punishment.

Proponents say such reform would improve financial transparency and help law enforcement identify suspicious transactions.

The situation likely will be different for hemp, which became legal nationwide with the enactment of the 2018 Farm Bill, but farmers and businesses in the industry also report difficulties securing banking services.

Many financial institutions say they are reluctant to serve the hemp industry until clear regulations are issued by federal banking regulatory agencies.

## TAXATION

Licensed marijuana entities can't take tax deductions and credits that ordinary businesses do.

That's because Section 280E of the IRS tax code specifies that no tax deduction or credit is permitted for any expense paid or incurred in carrying out a business that "consists of trafficking in controlled substances."

Marijuana is listed as a Schedule 1 drug under the Controlled Substances Act.

The U.S. Tax Court recently upheld that position in the closely monitored Harborside case involving a California-based cannabis dispensary chain.

Federal and appellate courts also have affirmed the federal government's position on 280E, and earlier this year, the U.S. Supreme Court declined to review a petition by a Colorado medical cannabis dispensary challenging the authority of the IRS.

Federal legislation that would address 280E for the state-legal marijuana industry has been introduced over the years. But a current bill isn't getting much traction on Capitol Hill.

The best hope for a change in the tax code at this point seems more likely through comprehensive marijuana reform.

Hemp businesses aren't subject to the burdensome 280E tax restrictions. In fact, in addition to taking typical deductions for expenses, those businesses have potential access to research and development tax credits, a tax credit that provides incentives to hire certain disadvantaged employees such as veterans and ex-convicts as well as other programs.

## READ MORE

- [Cannabis banking bill advances in committee; full U.S. House vote expected within weeks](#)
- [Most state attorneys general back cannabis banking reform; treasurers warming](#)
- [Banking, financing remain serious struggle for hemp, CBD businesses](#)
- [280E still applies to marijuana companies, U.S. Tax Court rules](#)
- [U.S. Supreme Court declines to hear 280E marijuana tax case](#)

# ENVIRONMENTAL REGULATIONS

States and municipalities across the United States are imposing stricter environmental requirements on cannabis growers, especially regarding the use and management of energy, water, waste and pesticides.

It's a trend that is likely to continue amid concerns about climate change and pressures on natural resources.

The regulations create a financial burden and uncertainty for cultivators, who typically operate on tight margins already.

California, known for its progressive environmental culture, has the toughest requirements in the country, according to marijuana business executives and consultants.

State officials articulate a priority to protect the environment from the "individual and cumulative effects" of marijuana cultivation.

One grower told Marijuana Business Daily last year he spent tens of thousands of dollars to meet California's environmental impact requirements. That included hiring a handful of consultants to conduct the assessments.

California requires growers to disclose how they plan to mitigate potential adverse environmental issues, including their effect on:

- Surface and groundwater quality.
- Water and energy use.
- Air quality.
- Wetlands, rivers, fisheries and plants.
- Pesticide use.
- Agricultural discharge.
- Cultural resources.

Many other states and municipalities also have adopted stricter environmental regulations.

Some examples:

- In Massachusetts, cultivators face energy regulations for indoor lighting.
- In Colorado and other markets, growers must comply with mandatory pesticide testing.
- In Oregon, growers must show they have a legal source of water.
- In Boulder, Colorado, marijuana facilities must report their energy use and offset consumption by creating a renewable-energy facility, participating in a verified solar garden or paying into a city fund.

Cultivators are making countermoves, such as forming cooperatives to share the costs of environmental analysis and reporting.

## READ MORE

- [Navigating environmental rules needn't be messy for cannabis growers](#)
- [Finding the right team to manage concerns with air, water and more](#)
- [Marijuana growers stare down costly, burgeoning environmental regulations](#)
- [Massachusetts sets new rules that limit energy use by marijuana growers](#)
- [Cost of new mandatory marijuana pesticide testing tough to absorb for Colorado's growers](#)
- [Marijuana companies face new regulations, oversight tied to water use](#)



# INTELLECTUAL PROPERTY

While marijuana remains federally illegal, cannabis-related businesses still have been able to receive federal protections for their intellectual property and build brand awareness and value through patents and trademarks.

The U.S. Patent and Trademark Office (USPTO) generally doesn't care that marijuana is illegal at the federal level, patent attorneys say.

In part, thank the pharmaceutical industry for that. Drug manufacturers often apply for patents before getting approval from the U.S. Federal Drug Administration.

The USPTO has granted patents for a range of marijuana-related products involving and combining CBD extracts, THC, essential oils, vitamins, drugs and alcohol.

Non-plant-touching devices also are getting patents, such as extraction technologies to improve dosage delivery methods, vaping devices, indoor grow systems, cultivation lights and more.

Cannabis strains, mostly CBD-dominant ones, also have received protection.

Cannabis-related applicants need to present data showing that their inventions achieve superior effects or surprising results.

Some patents, such as ones related to genetics, raise concerns that the Patent Office might not fully understand the overlap and hybridization of cannabis strains. The result is that a marijuana company might inadvertently infringe on a patent.

Growers and breeders also worry that the trend toward patenting plant genetics could lead to an industry controlled by large corporate entities such as agricultural giants, forcing producers to pay more for seeds and clones.

Federal trademarks are trickier since cannabis products can't be trademarked because of marijuana's federally illegal status.

Some companies have been successful in trademarking logos for non-plant items such as T-shirts and other apparel, business consulting services and their websites.

The idea is to at least begin to create a fence around your brand, so you have some protection against infringement by other companies.

But enforcement of a trademark might be curtailed if the other party uses the Controlled Substances Act as a defense.

Hemp-derived products don't have such federal trademark restrictions, now that hemp is legal under the Farm Act of 2018.

## READ MORE

- [Marijuana companies' intellectual property is crucial – here's how to protect it](#)
- [Making your mark and protecting it](#)
- [How Phylos Bioscience sent shockwaves through the cannabis industry with 'Big Ag' disclosure](#)

# RACKETEERING

Federal civil racketeering lawsuits against marijuana businesses—particularly growers—are starting to become more common.

The cases, filed under the federal Racketeer Influenced and Corrupt Organizations Act (RICO), argue that marijuana enterprises, even state-licensed businesses, constitute federally illegal drug trafficking activity.

Claims generally are cookie-cutter in nature: Cannabis companies diminish surrounding property values, pose public-safety risks and create nuisances such as skunklike smells.

Experts disagree about the potential risk the lawsuits pose to the industry, but the cases and the decisions are being watched closely because of the potential implications adverse decisions could have on the industry and individual defendants.

Under RICO, defendants who lose their cases might be required to pay up to three times financial damages plus attorney fees.

The suits typically list “co-conspirators,” or entities that have supported a marijuana company’s operation, such as a landlord, government licensing agency—even customers.

One lawsuit in Oregon named 200 defendants.

Here are some recent major decisions involving racketeering cases:

- **January 2019:** A federal judge dismissed a federal racketeering claim against an allegedly unlicensed marijuana cultivator in Northern California, saying the plaintiffs failed to prove a business or property loss as required by the statute.
- **November 2018:** A case against Healthy Pharms in Cambridge, Mass., was dismissed, but the marijuana company reportedly paid a substantial amount to settle the claims.
- **October 2018:** A Colorado jury sided in favor of a marijuana grower in a case filed by a neighbor, absolving the defendant of any damages. The case had been closely watched because it was the first marijuana racketeering case to go to a jury.
- **August 2018:** A federal judge in Oregon dismissed racketeering claims against a state-licensed marijuana cultivation facility. The judge ruled that the plaintiffs—a group of five neighbors—failed to prove a “concrete financial loss,” such as through an effort to sell or rent their properties.

## READ MORE

- [Number of cannabis racketeering suits increases, posing financial threat to targeted firms](#)
- [Federal judge throws out racketeering claim against California cannabis grower](#)
- [Massachusetts cannabis RICO case settled out of court for ‘substantial’ amount](#)
- [Jury rules in favor of Colorado marijuana grower in racketeering lawsuit](#)
- [Oregon judge tosses racketeering claim against medical marijuana grower](#)
- [California cannabis grower sues another under federal racketeering statutes](#)