



JOHN CHIANG
TREASURER
STATE OF CALIFORNIA

November 7, 2017

Dear Fellow Californians:

California is entering a new era with the legalization of adult recreational cannabis.

Medical cannabis has been permitted in California for more than two decades. Now, the decriminalizing of adult recreational cannabis, which voters overwhelmingly approved in November 2016, will vastly expand the scale of the industry. It is estimated that legal cannabis will generate more than \$7 billion in annual sales in its first few years of operation, beginning on January 1, 2018.

California regulatory agencies, law enforcement, and entrepreneurs have been working diligently to prepare for a smooth transition to legalization.

But the nascent industry faces an enormous challenge. The production, distribution, sale, and possession of cannabis remain illegal under federal law. Cannabis and many of its byproducts continue to be listed as Schedule I controlled substances, akin to heroin.

The clash between state and federal law threatens to cripple legal California cannabis businesses before they even get up and running. One of the main threats to legalization is that banks generally will not open accounts for cannabis businesses out of fear they will be penalized under federal law.

Lack of access to banking services that are taken for granted by other legal businesses—opening accounts, writing checks, accepting credit cards, transferring money—forces cannabis businesses to deal in large amounts of cash, which makes them targets for assaults and puts the general public in danger. Security and procedural concerns about handling massive amounts of cash also create a nightmare for state and local government revenue-collecting agencies. In addition, the inability of cannabis operations to get banking services means that many of them may remain in the underground economy and not become transparent, regulated, tax-paying businesses, as California voters intended.

Faced with these concerns, late last year I directed the staff of the State Treasurer's Office to carry out research and develop recommendations on strategies to address the cannabis banking conundrum. As the state's banker, I felt an obligation to fulfill the wishes of the voters when they passed Proposition 64 in November 2016.

Since then, I created a panel of 18 stakeholders—the Cannabis Banking Working Group—made up of representatives from the cannabis industry, financial institutions, and government tax collection, law enforcement, and regulatory agencies. The Working Group held six public meetings around the state and heard from nearly 50 expert panelists. Working Group members and their designated representative took time from busy schedules and worked diligently to consider ways to deal with the cannabis banking problem. The people of California owe them a great debt of thanks.

Based on the Working Group's findings, my office believes the best way to approach the cannabis banking problem is to think in terms of a series of steps, each of which involves greater access to banking services. The starting point is the current situation, in which the cannabis industry operates predominantly in cash, with only sporadic banking access. The end point is federal legalization of cannabis or, if that is not achievable, legislation shielding financial institutions that serve the cannabis industry. To progress along this continuum, we recommend the following actions: (1) the implementation of safer, more effective, and scalable ways to handle the payment of taxes and fees in cash that minimize the risks to stakeholders; (2) the State of California and local governments should develop a data portal of compliance and regulatory data and make it available to financial institutions that bank cannabis businesses; (3) a feasibility study of a public bank or other state-backed financial institution that provides banking services to the cannabis industry should be conducted; and (4) a multistate consortium of state government representatives and other stakeholders should be established to pursue changes to federal law to remove the barriers to cannabis banking.

In the end, it became apparent that a definitive solution to the cannabis banking quandary will remain elusive until the federal government removes cannabis from its official list of dangerous drugs or Congress approves safe harbor legislation protecting financial institutions that serve cannabis businesses from federal penalties.

The Working Group also heard from numerous vendors selling products and services that claim to provide cannabis businesses banking access. It is important to remember that contrary to what some solution providers have represented, there is no durable, failsafe solution to the banking problem until federal law is changed, and neither the Working Group nor the State Treasurer's Office endorses any particular product or service. Vendors should be selected with care, and the Appendix to this report suggests questions to ask vendors before hiring them.

California has exercised national leadership in areas ranging from enhancing civil rights to protecting the environment. The arrival of legal adult recreational cannabis offers another opportunity for our state to set an example. I am convinced we can find ways to expand cannabis industry banking access and make Proposition 64 a success.

Sincerely,

A handwritten signature in black ink, appearing to read "John Chiang". The signature is stylized and written in a cursive-like font.

JOHN CHIANG
California State Treasurer