

Date of Hearing: August 14, 2019

ASSEMBLY COMMITTEE ON APPROPRIATIONS  
Lorena Gonzalez, Chair  
SB 51 (Hertzberg) – As Amended June 13, 2019

Policy Committee:	Banking and Finance	Vote:	10 - 0
	Business and Professions		18 - 0

Urgency: Yes      State Mandated Local Program: Yes      Reimbursable: No

**SUMMARY:**

This bill enacts the Cannabis Limited Charter Banking and Credit Union Law to allow for the licensure and supervision of cannabis limited charter banks and credit unions authorized to offer limited depository services to cannabis businesses. Specifically, this bill:

- 1) Authorizes the Department of Business Oversight (DBO) to license a cannabis depository institution (CDI) and authorizes a CDI to accept deposits and issue an account holder special purpose checks that may be used only for specified purposes.
- 2) Authorizes state and local agencies to accept special purposes checks and specifies that no private or public entity is required to accept special purpose checks.
- 3) Requires a CDI to obtain and maintain private insurance for itself and its assets and authorizes a CDI to enter into an agreement with other CDIs to form a banking network.
- 4) Creates the Cannabis Limited Charter Bank and Credit Union Advisory Board (Board), comprised of the California State Treasurer, the California State Controller and the chief of the Bureau of Cannabis Control, and requires DBO to submit to the board a report of annual enforcement activities. The Board must evaluate these reports and public comments and make recommendations to the Legislature and the Governor on recommended actions.

**FISCAL EFFECT:**

- 1) Ongoing costs to DBO in the range of \$2 million each year to adopt emergency regulations, process applications, conduct examinations and enforce the provisions of the bill. These cost estimates rely on optimistic assumptions that enough banks participate in the proposed closed loop system to make it viable. Costs would be lower to the extent the system never becomes operational, though DBO would still incur initial costs of developing regulations and program development. (Financial Institutions Fund, Credit Union Fund)
- 2) Unknown, but likely modest costs for the Treasurer, Controller, and the chief of the Bureau of Cannabis Control to participate in the Board and develop recommendations to the Legislature.

**COMMENTS:**

- 1) **Background and purpose.** Federal law prevents cannabis businesses from accessing financial services provided by banks and credit unions, including basic checking accounts

and electronic payment services that nearly all business rely on to facilitate transactions with their customers. As a result, most cannabis businesses in California lack basic banking services. According to a survey conducted by the California Growers Association in 2017, more than two-thirds of its membership is unbanked, with cultivators having the lowest level of access along the supply chain. Unbanked cannabis businesses are forced to transact primarily in cash, which presents public safety challenges and makes it difficult for state and local agencies collect taxes and enforce state laws.

- 2) **The proposed banking solution.** SB 51 proposes a “closed-loop” banking system that allows cannabis businesses, state and local agencies, and other vendors to accept checks. CDIs would be authorized to provide limited services, including the acceptance of deposits and the issuance and redemption of special purpose checks. These checks may be used only to pay fees and taxes to state and local government agencies, pay rent, pay vendors located in California for expenses related to goods and services associated with the cannabis business, and purchase bonds or similar debt instruments issued by state or certain local agencies. These checks may not be used in any other capacity and balances may not be transferred to other banks outside the system.
- 3) **Will it work?** SB 51’s proposed closed-loop banking solution may offer a partial and temporary cash management solution until a more viable federal solution emerges. If enough CDIs become operational, there are narrow cases where this new network of institutions could help cannabis businesses manage their cash. Given the practical challenges these businesses face in completing even the most mundane business activities, even a partial and temporary solution could be worth pursuing.

However, this committee must also balance the significant state costs of starting this new banking system with the distinct possibility that not enough CDIs will become operational to create a viable system. Like with last year’s bill (SB 930 (Hertzberg), which was held on this committee’s Suspense File), there are significant obstacles toward successful implementation of this bill. They include:

- a) **Insurance.** This bill requires CDIs to obtain private insurance, a requirement that will be difficult to comply with and will add significant costs to participating CDIs. Typically, deposits at traditional banks and credit unions are insured by federal agencies with risk pooled across institutions and backed by the federal government. In contrast, a private entity willing to insure a CDI will likely charge high premiums given the risk associated with cannabis banking.
- b) **Federal law.** SB 51 does not guarantee that CDIs will be protected from federal law enforcement. As the Assembly Banking and Finance Committee analysis notes, one unfortunate side effect of this bill could be the concentration of cannabis business assets into one or several easily identifiable institutions, making them an easier target of federal law enforcement action.
- c) **Costs for banking customers.** A CDI’s revenue will primarily come from fees charged to customers for services. Because CDIs may offer only limited services and will have high operational costs and insurance premiums, customers are likely to be charged very high fees.