

Cannabis Business Blog

Strategic Planning for Businesses, Part 2

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Last month, in the first half of this two-part series on strategic planning, we reviewed the important fact that the growth, processing, distribution, retail sale and use of marijuana, while legal under state law, remains illegal as a controlled substance under federal law. The Aug. 29, 2013 Cole memo is guidance from the federal government which provides that the federal government will not enforce the marijuana laws in Washington so long as the state does an adequate job of preventing the marijuana industry from being abused in the state of Washington.

The Cole memo is guidance which could be amended or withdrawn at any time either in whole or part. The impact would lead to criminal prosecution and severe economic hardship.

So what do we recommend for the I-502 business participant?

As mentioned at the end of the last month's article, we recommend that the I-502 business person utilize a strategic asset ownership plan of limited liability companies (LLCs) and trusts to isolate the risk inherent with the I-502 business from the other assets of the business participant.

Structuring with LLCs: The I-502 business should be owned by an LLC (Washington state law appears to require that the business be owned by an LLC formed under Washington law. See WAC 314.55.020(7)). If the I-502 business person has several I-502 related businesses each business should be operated within its own LLC. The reason for this is to isolate the liabilities associated with each I-502 business within its own separate LLC. We further recommend that the I-502 business person have a second LLC hold the ownership in the I-502 business entity (the operating entity).

The ownership LLC provides a second layer of protection by having both the ownership and operation of the I-502 business in LLCs.

Under Washington law, assuming the investors of the LLC properly operate the LLC and treat it as a separate, independent legal entity, the liabilities associated with the operation of the I-502 business should remain within the LLC and not "bleed" over into the other assets of the I-502 business person. (In the event the federal government reversed the prosecuting of violators of

the Controlled Substance Act as it relates to Washington residents, there is no assurance this structure would protect the I-502 business person from criminal liability if found personally liable for violating the federal Controlled Substance Act.)

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Warning Regarding Federal Law: The possession, distribution, and manufacturing of marijuana is illegal under federal law, regardless of state law which may, in some jurisdictions, decriminalize such activity under certain circumstances. Penalties for violating federal drug laws are very serious. For example, a conviction on a charge of conspiracy to sell drugs carries a mandatory minimum prison term of five years for a first offense and, depending on the quantity of marijuana involved, the fine for such a conviction could be as high as \$10 million. In addition, the federal government may seize, and seek the civil forfeiture of, the real or personal property used to facilitate the sale of marijuana as well as the money or other proceeds from the sale. Although the U.S. Department of Justice (DOJ) recently rescinded its guidance regarding prioritization of criminal prosecutions of individuals and entities operating in compliance with effective state regulatory systems, DOJ left in place long standing guidance to federal prosecutors regarding how to exercise this discretion. Individuals and companies are cautioned to consult with experienced attorneys regarding their exposure to potential criminal prosecution before establishing business operations in reliance upon the passage of state laws which may decriminalize such activity. Federal authority to prosecute violations of federal law as crimes or through seizures and forfeiture actions is not diminished by state law. Indeed, due to the federal government's jurisdiction over interstate commerce, when businesses provide services to marijuana producers, processors or distributors located in multiple states, they potentially face a higher level of scrutiny from federal authorities than do their customers with local operations.