



Putting Marijuana Businesses to the QALICB Test

OWEN GRAY, CPA, NOVOGRADAC & COMPANY LLP



Question: Can marijuana businesses be qualified low-income community businesses (QALICBs)?

Answer: Despite the fact that the U.S. Drug Enforcement Administration classifies marijuana as a Schedule I drug—those with no currently accepted medical use and a high potential for abuse—25 states and the District of Columbia currently permit medical marijuana businesses to legally operate in their states/district. Four states (Alaska, Colorado, Oregon and Washington) currently permit various forms of recreational marijuana use. Nine states have November ballot measures to increase access to marijuana. ArchView Market Research recently estimated total U.S. sales from legal marijuana will reach \$6.7 billion in 2016. Marijuana businesses vary from farmers who cultivate marijuana crops to companies who produce edible/infusion marijuana products to medical marijuana dispensaries, to name just a few examples.

Internal Revenue Code Section (IRC §) 45D and related regulations do not contain a specific prohibition against marijuana businesses. To be a qualified active low-income community business

(QALICB) a partnership or corporation must meet the following tests:

1. gross-income requirement;
2. use of tangible property;
3. service performed;
4. collectibles;
5. non-qualified financial property.

The first three tests are all geographic-based determinations (e.g., where services are performed). The next two tests are percentage of assets tests.

IRC §45 does contain a prohibition against certain businesses being QALICBs. The statute specifically prohibits private or commercial golf courses; country clubs; massage parlors; hot tub facilities; sun tan facilities; race tracks or other facilities used for gambling or any store the principal business of which is sale of alcoholic beverages for consumption off premises. Additionally a business that consists predominantly of the development or holding of intangibles for sale or license is prohibited from being a QALICB. As such these limitations would not prohibit marijuana businesses.

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There is one additional prohibition contained in IRC §45D to be considered and that is the prohibition against farming. A trade or business the principal activity of which is farming cannot be a QALICB. For this purpose farming is defined as

1. cultivating the soil or raising or harvesting any agricultural or horticultural commodity on a farm or
2. handling, drying, packing, grading or storing on a farm any agricultural or horticultural commodity in its unmanufactured state but only if the owner, tenant or operator regularly produces more than one-half of the commodity so treated.

These provisions apply to farming businesses with more than \$500,000 of owned or leased assets used in the business. As such, this provision has the potential to prevent businesses that grow/cultivate marijuana crops from being QALICBs.

While certain marijuana businesses appear eligible to be QALICBs, there are other considerations, in addition to numerous underwriting considerations, that a community development entity (CDE) would need to evaluate before making a loan to or investment in such an entity. A CDE would be advised to consult with the Community Development Financial Institutions (CDFI) Fund to determine if the CDFI Fund views this as permissible under the NMTC allocation agreement. Would the CDFI Fund view this type of activity as

inconsistent with the allocatee's NMTC allocation application unless it was specifically mentioned in the application? Would the CDFI Fund view this as a type of activity inconsistent with the purposes of IRC Section 45D?

Likewise, a CDE would need to discuss this with its potential NMTC investor. Most NMTC investors are banks that are subject to the federal Bank Secrecy Act, which requires banks to watch for anti-money laundering law violations in its customer accounts. Banks are required to file reports with the Financial Crimes Enforcement Network (FinCen), a Treasury Department agency for suspicious activity. Many banks believe they may be viewed as committing money laundering by accepting a marijuana business related deposits under the anti-money laundering laws. While the Justice Department and FinCen has issued guidance on how banks may avoid running afoul of the Bank Secrecy Act, the guidance is merely guidance and doesn't change the existing federal laws. As such most major banks will not provide banking to marijuana related businesses.

So while technically a marijuana related business may qualify as a QALICB, a CDE would be strongly encouraged to consult with its legal and tax advisors, along with the CDFI Fund and its investor before deciding to finance a marijuana-related business. ❖

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