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many public accounting firms, but there are unique challenges and risks in...

Isaac M. O'Bannon • Oct. 19, 2017

How Accounting Firms Can Serve Marijuana Businesses

By Stanley Sterna, JD and Joseph Wolfe

More than 25 states allow the sale of marijuana for medicinal use; eight states permit the sale for recreational use. This activity has created new business opportunities for many public accounting firms, but there are unique challenges and risks in serving these clients.

Providing services to clients engaged in a business that is legal under state law but illegal under federal law has raised concerns among CPA firms regarding professional liability risks and compliance with professional standards, laws and board of accountancy regulations. Under federal law, marijuana remains illegal under the Controlled Substances Act. This exposes firms that service marijuana businesses to charges of aiding and abetting or conspiracy to violate this law, as well as criminal prosecution and civil claims alleging violation of federal racketeering laws.

Many banks refuse to provide services to these businesses due to concerns about application of both the Controlled Substance Act and anti-money laundering laws. As a result, marijuana businesses handle large amounts of cash, highlighting the need to address internal controls and the risk of theft and fraud. Additionally, the application of federal and state tax laws to income tax reporting by marijuana businesses is complex, requiring a heightened focus on compliance by both CPAs and their clients.

Quality control procedures will be of heightened importance for any accountant

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checks of its employees and if any adverse findings will affect their ability to effectively render services. When entering into an engagement, CPA firms should obtain a representation letter from the business principals expressly stating that they fully understand and intend to comply with all state laws applicable to their business. Engagement letters should clearly define the scope of the services to be rendered, and require client management to acknowledge that it is their responsibility to maintain all tax and accounting records as needed to respond to inquiries, investigations or audits initiated by regulators and criminal or tax authorities. Additionally, all communications with the client should be documented in writing.

A related concern raised by many CPAs is how professional liability insurance coverage applies to claims that may arise from servicing these clients. Insurance coverage cannot be determined prospectively by the firm's insurer, agent or broker. However, understanding how coverage applies can ease the process of evaluating and mitigating the risks of servicing this growing industry.

Professional liability insurance policies include a definition of "professional services", which generally is broadly drafted to cover services performed by accounting firms. The majority of services CPA firms are likely to render for marijuana businesses are no different from those performed for other client industries.

Many policies also provide coverage for the costs associated with responding to a disciplinary or regulatory investigation. While coverage varies, these policy provisions are designed to provide coverage for the legal costs of responding to a complaint filed against the CPA firm or its employees by licensing boards or regulators. Professional liability policies generally do not, however, provide insurance coverage for the legal costs of responding to a criminal investigation or

defending criminal charges filed against the firm or individuals. Policy exclusions

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and conditions, as well as applicable laws, regulations and professional standards.

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Professional Liability Claims and Lawsuits:

Insurance coverage generally will apply, just as it would to services rendered for clients in other industries. However, in light of the fact that marijuana businesses remain illegal under federal law, claims may include allegations that the firm or individuals employed by the firm engaged in dishonest, fraudulent or criminal acts. Coverage is typically excluded if this occurred, but the relevant policy exclusions contain important exceptions. These usually indicate that the exclusion does not apply unless there is a final judgment by a court finding that the insured party is guilty of the allegation.

Fines, Penalties, Sanctions and Forfeitures:

Policies generally exclude coverage for these exposures. This includes penalties imposed on the CPA firm or individuals by licensing, taxing, regulatory and other legal authorities. Individuals or firms that come under investigation by any of these authorities should promptly place their professional liability insurer on notice of these matters. While there likely will be no insurance coverage for these exposures, there may be insurance coverage for the costs to hire legal counsel to defend the firm or individual, subject to other limitations contained in the policy.

Criminal Investigations and Criminal Legal Actions:

The costs to defend these matters generally are excluded from coverage. Once a firm

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review the AICPA white paper, *An Issue Brief on State Marijuana Laws and the CPA Profession*, which addresses relevant legal, regulatory, and risk mitigation concerns, and is updated yearly.^[1]

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^[1]
<https://www.aicpa.org/Advocacy/State/DownloadableDocuments/MarijuanaCPAsIss>

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