No. 20-56265

IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

FRANCINE SHULMAN, IRON ANGEL, LLC, AND 3F, INC.,
Plaintiffs-Appellants,

v.

TODD KAPLAN, MEDICAL INVESTOR HOLDINGS LLC, DBA VERTICAL COMPANIES, CHARLES HOUGHTON, MATT KAPLAN, DREW MILBURN, COURTNEY DORNE, SMOKE WALLIN, ROBERT SCOTT KAPLAN, AKA ROBERT SCOTT, ELYSE KAPLAN, JEFF SILVER, IRON ANGEL II, LLC, NCAMBA9, INC., AND VERTICAL WELLNESS, INC.,
Defendants-Appellees.

On Appeal from the United States District Court
for the Central District of California
No. 2:19-cv-05413-AB-FFM
Honorable André Birotte Jr.

OPENING BRIEF FOR PLAINTIFFS-APPELLANTS

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CORPORATE DISCLOSURE STATEMENT

Pursuant to Federal Rule of Appellate Procedure 26.1, Plaintiffs-Appellants Iron Angel, LLC and 3F, Inc. hereby state, by and through counsel, that each of them has no parent corporation, and no publicly held corporation owns 10% of more of Iron Angel, LLC's stock or 3F, Inc.'s stock.

Dated: December 15, 2021

Respectfully submitted,

/s/ Cheryl Cauley

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JURISDICTIONAL STATEMENT

The United States District Court for the Central District of California had subject matter jurisdiction over the claims arising under the Racketeer Influenced and Corrupt Organizations Act ("RICO") and the Lanham Act pursuant to 28 U.S.C. § 1331. The district court had supplemental jurisdiction over the claims arising under California state law pursuant to 28 U.S.C. § 1367.

On October 29, 2020, the district court entered a final judgment dismissing Plaintiffs' Complaint. ER 3. Plaintiffs timely filed a notice of appeal on November 30, 2020.[1] ER 158. This Court has jurisdiction under 28 U.S.C. § 1291.

ISSUE PRESENTED

Whether the district court erred in concluding that Plaintiffs cannot state a RICO claim for damages due to their connection to the cannabis industry.

INTRODUCTION

In our federal system, the States function as "laboratories" of democracy. *See, e.g.*, *Arizona State Legislature v. Arizona Indep. Redistricting Comm'n*, 576 U.S. 787, 817 (2015) ("This Court has 'long recognized the role of the States as laboratories for devising solutions to difficult legal problems.'") (citation omitted); *United States v. Lopez*, 514 U.S. 549, 581 (1995) (Kennedy, J., concurring) ("[T]he

[1] Because 30 days after entry of the judgment fell on Saturday, November 28, 2020, the period to file a notice of appeal ran until Monday, November 30, 2020. *See* Federal Rule of Appellate Procedure 26(a)(1)(C).

States may perform their role as laboratories for experimentation to devise various solutions where the best solution is far from clear."); *New State Ice Co. v. Liebmann*, 285 U.S. 262, 311 (1932) (Brandeis, J., dissenting) ("It is one of the happy incidents of the federal system that a single courageous state may, if its citizens choose, serve as a laboratory; and try novel social and economic experiments without risk to the rest of the country."). Over the last decade, a number of states have chosen to experiment with the legalization of cannabis. Eighteen states now allow adult recreational use, and 36 allow for medicinal use. This wave of experimentation has given rise to a multibillion-dollar industry that employs over 300,000 workers and will soon equal the size of the craft beer industry. Amid this changing legal landscape, Ms. Francine Shulman, a successful and well-respected elderly California farmer, saw an opportunity. She acquired new land, expanded her farming operations, and began to cultivate cannabis in an operation licensed by California law. While she had the vision, Ms. Shulman lacked the capital and resources to further expand on her ambitious business plan.

Like Ms. Shulman, Defendants also saw an opportunity. Aware of Ms. Shulman's assets and her vulnerabilities, Defendants decided they too could strike it rich by following their tried-and-true scheme: 1) trick Ms. Shulman into entering a business partnership by promising capital, expertise, and resources they would never provide; 2) use that relationship to secure additional partnerships; and 3) cash out

without abiding by their contractual obligations and leave Ms. Shulman in financial despair. Defendants have made it their habit to employ this fraudulent scheme and decided to make Ms. Shulman their next victim. Defendants succeeded, leaving Ms. Shulman, her property, and her business severely damaged. After Defendants left her in financial ruin, Ms. Shulman filed suit in federal court, bringing RICO claims to hold Defendants to account for their pattern of racketeering activity.

Despite Ms. Shulman's numerous injuries at the hands of Defendants' wrongful conduct, the district court refused to allow Ms. Shulman any redress. It held that it could not provide a remedy for actions related to a business that is illegal under federal law (though legal under California law), and that affording any relief in these circumstances would require the court to contravene the Controlled Substances Act ("CSA"). Such a course of action was, in the court's view, contrary to public policy. In doing so, the district court rejected the consensus of numerous courts that allowing Ms. Shulman to state a claim for damages in these circumstances does not violate the CSA. In addition, it severely disrupted the policy formulated by Congress and the executive branch in this contentious area: noninterference with cannabis activities conducted in compliance with state law. The district court's holding threatens the stability of one of the nation's fastest growing industries and makes numerous businesses and employees invisible to federal law.

Accordingly, the district court erred in finding that that Plaintiffs cannot state a RICO claim for damages due to their connection to the cannabis industry and dismissing Plaintiffs' Complaint, and this Court should reverse the district court's decision.

STATEMENT OF THE CASE

I. Ms. Shulman, a successful farmer for over 20 years, grows a cannabis cultivation business.

In 1996, Ms. Francine Shulman purchased Apple Creek Ranch, a 50-acre apple orchard in the Santa Rita Hills of Santa Barbara County, California and began what eventually flourished into a prosperous farming business. ER 15–16 ¶ 2. Mastering organic farming practices, Ms. Shulman's business grew rapidly as she expanded the orchard to numerous apple varieties and unique organic fruits and vegetables. *Id*. She became well-known in the agricultural community for her comprehensive farming knowledge and ability to grow unusual and challenging varieties of fruits and vegetables, and the local community held her in high regard not only for her business success but also her kindness and generosity to the surrounding area. ER 16 ¶¶ 3–4.

In March 2014, Ms. Shulman identified a 1,100-acre property in Lompoc, California, ideal for multiple uses, including cannabis cultivation. ER 16–17 ¶ 5, 31–32 ¶ 56. She arranged to lease the property and ultimately purchased it in December 2014 with the goal of cultivating both produce and medical cannabis and

ultimately building a wellness retreat. *Id*. Nicknaming the property "Iron Angel" after her motorcycle, Ms. Shulman invested in critical infrastructure, such as a well, irrigation, power, and roads, to farm organic produce and cannabis. ER 16–17 ¶ 5. In August 2014, she moved onto the property and began cultivating organic produce, and, pursuant to the Compassionate Use Act of 1996, medical cannabis. ER 31–32 ¶ 56. To comply with its legal requirements, Ms. Shulman formed and joined collectives, including 3F, Inc. and acquired state licenses for her cultivation operations. *Id*. At all times, Ms. Shulman and her collectives complied with all local and state laws and regulations regarding cannabis cultivation. ER 16–17 ¶ 5, 32 ¶ 57.

As Ms. Shulman developed her cannabis cultivation skills at Iron Angel Ranch, favorable changes in the law dramatically increased the value of her business. ER 17 ¶ 6, 32–33 ¶ 58. The County of Santa Barbara passed regulations in January 2016 favoring local farmers like Ms. Shulman who had existing medical cannabis cultivation, and in November 2016, California voters approved Proposition 64, the Adult Use of Marijuana Act, permitting the sale of cannabis for recreational use. *Id*. These changes created the opportunity for farmers like Ms. Shulman to transform modest cannabis grows into large-scale cannabis cultivation, manufacturing, and processing operations. *Id*.

Recognizing the growth potential for her cannabis operations, Ms. Shulman looked to acquire additional properties. ER 17–18 ¶ 7, 33–35 ¶ 59–63. By July 2017, she had leased an additional property in Lompoc, which became known as "Sisters," that had five-times the cultivable acreage of Iron Angel. ER 17–18 ¶ 7, 33 ¶ 59. Ms. Shulman then turned her attention to a piece of property in Buellton known as "Wellsprings," which contained 10-times the cultivable acreage of Iron Angel and could thus support a large-scale commercial cannabis operation. ER 17–18 ¶ 7, 34 ¶ 61. Due to her strong relationship with the owners of Wellsprings, Ms. Shulman succeeded in executing a purchase agreement due to close on January 15, 2018, as well as a lease that would allow her to both immediately begin farming operations and move into an existing residence on the property. ER 34–35 ¶¶ 62–63.

II. Seeking to grow this business, Ms. Shulman enters a business relationship with Defendants.

Around this time, Ms. Shulman recognized that for her business to achieve its full potential, she needed a business partner with capital to invest in her business and with industry experience and knowledge to guide the business through a changing and complex regulatory landscape for cannabis operations in California. ER 18–19 ¶ 9, 34–35 ¶ 64. In June 2017, Ms. Shulman was introduced to Todd Kaplan—the founder and CEO of Medical Investor Holdings LLC dba Vertical Companies ("Vertical")—and Defendants. ER 19 ¶ 10, 24 ¶ 23, 34–35 ¶ 64. Defendants told

Ms. Shulman that Vertical was a financially stable company and that it had existing indoor cultivation, large-scale manufacturing, many brand partners, and dispensaries. ER 36 ¶ 65. Defendants touted that Vertical had significant experience in the cannabis industry and had legal counsel with local regulatory expertise. *Id*. Ms. Shulman met several times with Kaplan and other Defendants to discuss a business partnership, and Defendants again offered their expertise in the cannabis industry and interest in partnering with Ms. Shulman. ER 36–39 ¶¶ 66–73.

However, none of it was true. ER 39 ¶ 73. An admitted felon who had been indicted for health care fraud, conspiracy to commit money laundering, illegal kickbacks, and attempts to evade taxes, Kaplan had found his next victim. ER 19 ¶ 11. Kaplan and Defendants have forced their way into the California cannabis industry by subjecting numerous victims to a similar fraudulent scheme: misrepresent Defendants' acumen and skill in the cannabis industry, enter into business partnerships with the victims, refuse to abide by the contractual terms, try to take over the victims' business for themselves, and then walk away leaving the victims in shambles. ER 78–81 ¶¶ 164–68. Defendants would pitch themselves to potential brand affiliates or investors as an established, experienced, sophisticated, and successful cannabis organization, secure a business relationship, fail to abide by those terms, and then use the partnership with that brand affiliate to lure in another victim. ER 81–83 ¶¶ 169–73. And Defendants would use the existing relationships

to deceive investors into providing them capital while Defendants had no plans to provide a return to those investors. ER 82–83 ¶ 173. Ultimately, Defendants' deceptive scheme appears to be 1) deceive business owners, brand affiliates, and investors into entering business partnerships, 2) use those relationships to secure additional partnerships with other victims, and 3) cash out without ever living up to their contractual obligations and leave the victims in ruin. *Id*. Numerous separate victims of this scheme are now known, and they are named in the Complaint. ER 78 ¶ 164

Defendants employed this very scheme against Ms. Shulman. Recognizing the key attributes that were important to Ms. Shulman in selecting a business partner—financing, operations, distribution, branding, manufacturing, and regulatory expertise—Kaplan misrepresented his and his company's experience in the cannabis business and misrepresented the financial status of his company and his ability to fund a cannabis operation. ER 39 ¶ 73. Kaplan falsely asserted that Defendants had extensive experience in cannabis cultivation and production in California. *Id.* He misrepresented that they were experts in cannabis operations. *Id*. He falsely claimed expertise in cannabis laws and regulations in California and misled Ms. Shulman into believing that Defendants could expertly guide the business through regulatory and licensing procedures. *Id.* With regard to available capital to invest in the business, Kaplan assured Ms. Shulman that she would never

have to worry about the finances. *Id.* He stated that he had numerous investors lining up to provide cash and that he had substantial personal resources that were also available to the business, but this was all a lie. *Id*.

Based on these lies, Ms. Shulman and Kaplan developed a general business plan. ER 39–40 ¶ 74. Vertical would pay all operational expenses and manage day-to-day operations in exchange for the use of Ms. Shulman's farmland, a share of crops existing at the time of the partnership (with a defined split), contacts, and the ability to cultivate through Ms. Shulman's legal nonconforming use licenses. *Id*. Kaplan claimed the parties would work "together" to obtain additional county and state licenses (under the new regulations), launch brands based on Ms. Shulman's Iron Angel name, and manage the overall business operations. *Id.* Vertical and Ms. Shulman were to share net profits from Iron Angel and Sisters equally, and Kaplan also included a provision that gave him an option to purchase a 42.5% "tenant in common interest" in Iron Angel. *Id*.

Ultimately, the parties entered into a Reciprocal Membership and Cultivation Agreement ("Cultivation Agreement"). ER 42–43 ¶ 78. Kaplan signed on behalf of an entity that he formed and for which he acted as CEO, NCAMBA9; however, Kaplan, Vertical, and other Defendants worked collectively as the intended beneficiaries. *Id*. The Cultivation Agreement authorized NCAMBA9 to use a management company to manage operations, and NCAMBA9 immediately turned

management over to Vertical and Kaplan. *Id*.

Although the Cultivation Agreement applied only to Iron Angel and Sisters, Kaplan and Vertical convinced Ms. Shulman to extend their partnership to Wellsprings, where she alone had the sole contractual rights to both lease and farm the property, and eventually buy it. ER 46 ¶ 88. This Wellsprings Agreement, entered into on July 21, 2017, called for the same operational and financial terms as the Cultivation Agreement—Vertical was responsible for managing cannabis operations, and profits would be split 50/50. *Id*.

Upon signing of the Cultivation Agreement, it soon became clear that Kaplan and Defendants had defrauded Ms. Shulman. ER 44–45 ¶ 85. Kaplan and Defendants lacked the necessary resources to even begin operations on Iron Angel and Sisters—despite pledging to cover all operational expenses, Defendants failed to do so, forcing Ms. Shulman to spend the remainder of her life savings paying for necessary operational expenses, including cultivation supplies, insurance, equipment rentals, irrigation supplies, agricultural labor costs, and lease payments at Sisters. *Id*. Nor were Defendants prepared to operate the business as they had promised to do, lacking the experience necessary to manage operations and failing to provide enough or qualified personnel to do so. ER 45 ¶ 86, 50–51 ¶ 97.

III. Defendants implement numerous fraudulent schemes to the detriment of Ms. Shulman, her property, and her business.

Having lured Ms. Shulman into a business relationship, Defendants turned their efforts not to managing the business operations but to developing a scheme to defraud Ms. Shulman of her business and property interests. ER 46–47 ¶ 90. While appearing to work with Ms. Shulman to develop and close on the acquisition of Wellsprings, Defendants planned to strip Ms. Shulman of her rights in Wellsprings and allow Defendants to assume control of Wellsprings and its cannabis operations for themselves. *Id*. Defendants would sabotage the closing of the acquisition of Wellsprings so that they could acquire the property for themselves. ER 47–53 ¶¶ 90–102. Ultimately, Defendants successfully obstructed the closing of the acquisition but failed to acquire the property for themselves. ER 51 ¶ 98, ER 52–53 ¶ 101–02. Nevertheless, Defendants' actions still deprived Ms. Shulman of ownership of a property that would have substantially increased her business and the profits expected to be generated from that property in the future. ER 52–53 ¶ 102.

Defendants next devised a plan to steal Iron Angel from Ms. Shulman and take for their enterprise all the profits from cannabis cultivation on the property. ER 54 ¶ 105. Defendants misrepresented to Ms. Shulman that for state licensing purposes, she needed to sign an agreement leasing Iron Angel to a limited liability corporation for which Kaplan was the sole manager. ER 54–55 ¶¶ 106–07. Defendants assured Ms. Shulman that the lease was a formality; its terms would not

be followed; and the parties would operate under the Cultivation Agreement. ER 55 ¶ 107. However, state regulations did not require the lease, and Defendants intended to use it a basis to claim exclusive possession of Iron Angel, oust Ms. Shulman from Iron Angel, and take 100% of its profits should she terminate the Cultivation Agreement. ER 56–57 ¶¶ 108–12.

Defendants also defrauded Ms. Shulman out of her operator licenses. The enactment of the Adult Use of Marijuana Act altered the state and local regulatory and permitting regime for cannabis production. ER 57–58 ¶ 113. Because Ms. Shulman was an existing cultivator of medical cannabis, Santa Barbara County ordinance permitted her to continue cultivation while awaiting the approval of a state license to operate under the new Adult Use of Marijuana Act. *Id.* This gave her a unique advantage and made her an attractive target to Kaplan and Defendants. In December 2017, Ms. Shulman took advantage of this unique opportunity, initiating the process of obtaining licenses to operate Iron Angel, Sisters, and Wellsprings as commercial cannabis sites. ER 58 ¶ 114. After obtaining some licenses, Ms. Shulman looked to Defendants to assist with navigating state and county licensing requirements, but instead of helping her obtain the additional licenses, Defendants submitted false affidavits claiming that they had continuously operated the properties to obtain temporary licenses for themselves only. ER 58–59 ¶ 115. As a result of Defendants' failure to include Ms. Shulman in the permit applications, Ms.

Shulman now faces a number of permitting problems, and her ability to cultivate cannabis is threatened. ER 59 ¶ 117.

From the moment the agreements were entered, Defendants had no intention of abiding by the Cultivation Agreement and Wellsprings Agreement. ER 60 ¶ 118. Defendants failed to cover operational expenses, routinely sold product to affiliates at below market prices, and never paid Ms. Shulman for her share of any product harvested. ER 60–65 ¶¶ 118–31. After repeated requests from Ms. Shulman, Kaplan finally agreed to meet with Ms. Shulman to discuss their financial arrangement. ER 65–66 ¶¶ 132–34. Kaplan proposed a new contractual relationship that bore no resemblance to the parties' original agreements. ER 66–67 ¶¶ 134–35. Ms. Shulman rejected these efforts to bully her into forfeiting her contractual rights and continued to try to resolve Defendants' contractual breaches. ER 67–69 ¶¶ 136–39. Defendants stalled in responding to Ms. Shulman so that they could continue to harvest and sell cannabis for their own benefit and make it appear to investors that they were the owners and operators. ER 68 ¶ 136, 69 ¶ 139. The parties' business relationship eventually ended when Ms. Shulman terminated the Cultivation Agreement on February 25, 2019, and when the parties were evicted on March 12, 2019, from Wellsprings due to the failure to close on the acquisition of the property. ER 69–71 ¶¶ 140–43.

After the loss of Wellsprings, Ms. Shulman returned to her permanent residence on Iron Angel to continue her cannabis operation on her property without Kaplan and Defendants. ER 71 ¶ 144. Defendants then used the phony lease signed by Ms. Shulman to obtain a court order ousting Ms. Shulman from her home and taking Iron Angel's operations for themselves. ER 71–72 ¶¶ 144–46. The court granted Defendants the right to enter Iron Angel on certain terms and to operate the cannabis business exclusively. ER 73 ¶ 147. When entering Iron Angel, Defendants routinely intimidated and harassed Ms. Shulman. ER 73 ¶¶ 147–48. Defendants' management of the cannabis business caused it substantial chaos and harm, leading to multiple regulatory violations, damage to the fields and plants, and diminished prospects of successful harvests in future years. ER 73–74 ¶¶ 149–51. Defendants eventually abandoned Iron Angel, leaving Ms. Shulman a business in shambles. ER 74 ¶ 151.

IV. Consistent with a pattern of defrauding innocent targets, Defendants caused Ms. Shulman and her business to suffer numerous harms.

Defendants' repeated misrepresentations throughout the California cannabis industry have victimized not only Ms. Shulman but many other parties. ER 78 ¶ 164. At least five other individuals have been made victims of a scheme similar to the one faced by Plaintiffs, and Defendants' conduct evidences a clear pattern of fraud, misrepresentation, and deception. Defendants' use of this scheme against Ms. Shulman resulted in substantial harm, taking a variety of forms, to Plaintiffs. ER 75

¶ 154. Defendants failed to pay any amounts due for the cultivation of cannabis on Iron Angel, Sisters, and Wellsprings, and their mismanagement, operational failures, and repeated contractual breaches deprived Plaintiffs of the profits they otherwise could have attained from cultivating the three properties. ER 75–76 ¶¶ 155–58. Defendants caused other financial harm, including failure to reimburse Ms. Shulman for operational expenses she incurred; damages to Ms. Shulman's property on Iron Angel; and damages in light of Defendants' malicious prosecution of their claim that the phony lease displaced the Cultivation Agreement. ER 76–77 ¶ 159. Defendants' conduct also deprived Ms. Shulman of her ownership interest in Wellsprings, excluded her from her operator licensing, and harmed the Iron Angel brand. ER 59 ¶ 117, 76 ¶ 160–61. And Defendants inflicted great emotional distress on Ms. Shulman. ER 77–78 ¶¶ 162–63.

V. Plaintiffs file suit, and the district court dismisses the Complaint.

On June 20, 2019, Plaintiffs Francine Shulman, Iron Angel, LLC, and 3F, Inc. initiated this action against Defendants Todd Kaplan, Medical Investor Holdings LLC, dba Vertical Companies, Matt Kaplan, Drew Milburn, Courtney Dorne, Smoke Wallin, Robert Scott Kaplan, aka Robert Scott, Elyse Kaplan, Jeff Silver, Iron Angel II, LLC, NCAMBA9, Inc., Vertical Wellness, Inc. (collectively, "MIH Defendants"), and Charles Houghton. ER 173, D.Ct. 1. Plaintiffs asserted 25 claims arising under federal and California state law against Defendants, including the

claims at issue here for violations of RICO.[2] ER 83–139 ¶¶ 174–456; 18 U.S.C. §§ 1962(c)-(d), 1964(c).

On January 28, 2020, the district court granted a motion by Defendants to compel arbitration and stayed the action in its entirety. ER 178, D.Ct. 58. After the arbitrator concluded that Defendants had waived their right to arbitrate, the arbitration was dismissed on July 9, 2020, and the district court subsequently vacated the stay on July 13, 2020. ER 179, D.Cts. 62–63. After the stay was lifted, Defendants moved to dismiss the Complaint pursuant to Federal Rule of Civil Procedure 12(b)(6).[3] ER 179, D.Cts. 66, 67. As to the RICO claims, Defendants argued that Plaintiffs could not state a claim for damages based on activity that is illegal under federal law and that Plaintiffs had failed to plead essential elements of their RICO claims. D.Ct. 66-1 at 10–17. On October 29, 2020, the district court granted Defendants' motion to dismiss.[4] ER 180, D.Ct. 73. It concluded that because any remedy for Plaintiffs' RICO claims would violate federal law, specifically the CSA, Plaintiffs' injuries to their cannabis business were not redressable under RICO, and Plaintiffs therefore lacked standing to seek relief in

[2] Plaintiffs do not challenge the dismissal of their Lanham Act claims.

[3] The MIH Defendants filed a motion to dismiss, and Houghton filed a separate motion to dismiss and notice of joinder in the MIH Defendants' motion. ER 179, D.Cts. 66–67.

[4] The district court granted the MIH Defendants' motion and denied as moot Houghton's motion. ER 8.

federal court. ER 5–6. The court reached the same conclusion as to the other federal claims, denied leave to amend because Plaintiffs could not plead additional facts to overcome the illegality of their business activities. On the basis of the dismissal of these federal claims, the court declined to exercise supplemental jurisdiction over the state law claims and dismissed Plaintiffs' Complaint in its entirety. ER 7–8. Plaintiffs timely appealed. ER 158.

SUMMARY OF ARGUMENT

To enforce RICO's prohibition against racketeering activity, Congress authorized victims of racketeering to bring private suits and recover treble damages. This private right of action provides a remedy for those harmed by racketeering and creates a comprehensive system of private enforcement. To ensure that RICO serves its twin aims, the Supreme Court has repeatedly instructed courts to read the statute's terms broadly and to avoid reading limitations into RICO. This Court has regularly heeded the Supreme Court's admonitions, but the district court paid no attention to them. Instead, the court crafted an implied exception to RICO's reach that lacks any basis in the statutory text. In addition, the district court failed to consider RICO's deterrent effect on racketeering activity.

More crucially, the district court's chief concern—that affording Plaintiffs a damages remedy under RICO would force it to contravene the CSA's prohibition on the cultivation of marijuana—finds little support in the caselaw. The few cases to

address this question reject the district court's reasoning. Courts repeatedly hold that a plaintiff's connection to the cannabis industry neither deprives them of remedies afforded by federal law, nor immunizes a defendant's wrongful conduct. In fact, the only circuit to address this question has concluded that permitting a remedy in these instances does not violate the CSA. In addition, federal courts regularly enforce contracts that concern the cannabis industry. These courts have generally held that ordering payment does not require a defendant to possess, cultivate, or distribute cannabis or otherwise violate the CSA, and thus, a remedy may be afforded to the plaintiff. This Court has recognized that when a contract may be enforced without requiring illegal conduct, then the court should do so.

The district court wrongly concluded that permitting Plaintiffs to recover damages under their RICO claim would be contrary to public policy. The district court erroneously characterized Plaintiffs' activities as unequivocally illegal under federal law. Plaintiffs' activities comply with state law, and since 2009, federal policy regarding enforcement of the CSA has turned the CSA's marijuana prohibitions into a nominal bar on such conduct. Instead, the federal government has adopted a more nuanced approach, declining to interfere with cannabis activities conducted in compliance with state law. This federal policy derives not only from the executive branch's enforcement decisions and priorities but also Congress's regular appropriations riders restricting the Department of Justice's ability to

prosecute marijuana-related offenses. Contrary to the district court's conclusion, federal policy has rejected unequivocal enforcement of the CSA. Next, the district court failed to articulate how providing Plaintiffs a remedy under RICO would be contrary to this policy of noninterference with state-authorized cannabis activities. Courts should hesitate to disrupt the policy decisions and balance struck by the political branches in this contentious area. The court also failed to explain how permitting wrongful and illegal acts affecting interstate commerce to go unpunished is at all consistent with federal policy and RICO's purposes.

Lastly, the district court's holding produces alarming consequences that chills one of the hallmarks of our federal system: the ability of states to act as "laboratories" for democratic experiments. According to the district court, those engaged in the cannabis industry—or any other activity legalized first by states—lose the protections afforded by federal laws and may never be able to recover damages in federal court. As more states legalize cannabis sale and use, the industry has grown and will continue to grow dramatically, and affirmance of the district court's decision could devastate the industry and its workers.

Accordingly, this Court should reverse the district court's order dismissing Plaintiffs' Complaint.

STANDARD OF REVIEW

This Court reviews *de novo* a district court's dismissal for failure to state a claim under Federal Rule of Civil Procedure 12(b)(6). *Abcarian v. Levine*, 972 F.3d 1019, 1022 (9th Cir. 2020). Well-pleaded factual allegations in the complaint are taken as true and construed in the light most favorable to the non-moving party. *Id*.

ARGUMENT

I. The district court erred in holding that Plaintiffs cannot state a RICO claim for damages due to their connection to the cannabis industry.

The district court erroneously held that because Plaintiffs engage in the cultivation of cannabis, they cannot state a RICO claim for damages. The district court offered little support for this conclusion. Indeed, it not only clashes with RICO's broad remedial purposes and scheme of private enforcement but also lacks a sound legal basis. Providing a remedy to Plaintiffs would not require the contravention of any federal law, nor would doing so be contrary to public policy. Congress and the executive branch have repeatedly endorsed a permissive policy toward cannabis activities in compliance with state and local law, and a failure to follow that policy here will lead to troubling consequences.

A. The district court offered no support for its conclusion that any remedy in this case would contravene federal law.

The district court first observed that "Plaintiffs [sic] damages under RICO are inextricably intertwined with their cannabis cultivation—any relief would remedy Plaintiffs' lost profits from the sale, production, and distribution of cannabis." ER

5. It further reasoned, without any citation to authority, that "any potential remedy in this case would contravene federal law under the CSA" because "[a] court order requiring monetary payment to Plaintiffs for the loss of profits or injury to a business that produces and markets cannabis would, in essence (1) provide a remedy for actions that are unequivocally illegal under federal law; and (2) necessitate that a federal court contravene a federal statute (the CSA) in order to provide relief under a federal statute (RICO)." *Id*. According to the district court, "this approach [is] contrary to public policy." *Id*. Because remedying Plaintiffs' injuries would result in an "illegal mandate," the district court concluded that "Plaintiffs' injuries to their cannabis business are not redressable under RICO," and thus, Plaintiffs lack standing to seek relief. ER 6.

The district court offered little analysis to support this broad and novel ruling, and when it did, the court's reasoning was utterly conclusory. The court stated that any potential remedy would contravene federal law and require a federal court to violate the CSA but offered no explanation for that conclusion. Similarly, the district court failed to explain why or how such a remedy in this case would be contrary to public policy. And the district court addressed the most directly on point case, *Siva Enterprises v. Ott*, No. 2:18-cv-06881-CAS-GJSx, 2018 WL 6844714 (C.D. Cal. Nov. 5, 2018), in only two sentences. When faced with a question of law that has received little analysis in the federal courts, the district court offered scant and

conclusory analysis that leaves this Court and future courts to guess as to the reasoning and scope of the decision.

B. Congress intended and the Supreme Court has instructed that RICO must be interpreted broadly to effectuate its remedial purposes and scheme of private enforcement.

Enacted in 1970 as Title IX of the Organized Crime Control Act, Pub. L. No. 91-452, § 901, 84 Stat. 922 (1970) (codified at 18 U.S.C. §§ 1961-1968), RICO provides for both criminal and civil liability for those engaging in "racketeering activity," broadly defined as certain specified acts chargeable under state or federal law. *Sedima, S.P.R.L. v. Imrex Co., Inc.*, 473 U.S. 479, 481–82 (1985) (citing 18 U.S.C. § 1961(1)). Specifically, RICO "outlaws the use of income derived from a 'pattern of racketeering activity' to acquire an interest in or establish an enterprise engaged in or affecting interstate commerce; the acquisition or maintenance of any interest in an enterprise 'through' a pattern of racketeering activity; conducting or participating in the conduct of an enterprise through a pattern of racketeering activity; and conspiring to violate any of these provisions." *Id*. at 482–83 (quoting 18 U.S.C. § 1962).[5]

[5] Before the district court, Defendants raised additional arguments for dismissal of Plaintiffs' RICO claims that the district court did not address in its order. *See* D.Ct. 66-1 at 10–17. Should this Court agree with Plaintiffs that the district court erred in its reasoning, this Court should not consider these alternative arguments. *See Golden Gate Hotel Ass'n v. City & Cnty. of San Francisco*, 18 F.3d 1482, 1487 (9th Cir. 1994) ("As a general rule, 'a federal appellate court does not consider an issue not passed upon below.'") (quoting *Singleton v. Wulff*, 428 U.S. 106, 120 (1976)).

1. RICO's private right of action not only remedies those harmed by racketeering activity but also deters future racketeering activity.

In crafting RICO, "Congress provided criminal penalties of imprisonment, fines, and forfeiture for violation of these provisions," and "[i]n addition, it set out a far-reaching civil enforcement scheme" allowing those harmed by RICO violations to bring private suits. *Sedima*, 473 U.S. at 483 (citing 18 U.S.C. §§ 1963 and 1964). Specifically, "[a]ny person injured in his business or property by reason of a violation" of 18 U.S.C. § 1962 may sue to recover treble damages. 18 U.S.C. § 1964(c).

The Supreme Court has repeatedly instructed lower courts that they "should not read the statutory terms of RICO narrowly." *Odom v. Microsoft Corp.*, 486 F.3d 541, 547 (9th Cir. 2007). Instead, "'RICO is to be read broadly,'" and "[a]s Congress admonished and as the Court repeated in *Sedima*, RICO should 'be liberally construed to effectuate its remedial purposes.'" *Id*. (quoting *Sedima*, 473 U.S. at 498); *see also* Pub. L. No. 91-452, § 904(a), 84 Stat. at 947 (same). Thus, RICO's private right of action permitting the recovery of treble damages serves a twin purpose: provide a remedy for those harmed by racketeering activity and create a comprehensive system of private enforcement.

2. The Supreme Court and this Court have repeatedly rejected a narrow approach toward RICO.

This Court observed in *Odom* that since RICO's enactment, "[t]here has been some judicial resistance to RICO, manifested in narrow readings of its provisions by lower federal courts." 486 F.3d at 545. In response, the Supreme Court has regularly "corrected these narrow readings," imploring lower courts to read the statute broadly and to refuse to read such limitations into RICO. *Id*. at 545–47 (discussing *United States v. Turkette*, 452 U.S. 576 (1981); *Sedima*, 473 U.S. 479; *Nat'l Org. for Women, Inc. v. Scheidler*, 510 U.S. 249 (1994); and *Cedric Kushner Promotions, Ltd. v. King*, 533 U.S. 158 (2001)). In *Turkette*, the Supreme Court reprimanded the lower court because it "clearly departed from and limited the statutory language" in a way that failed to give RICO its full effect as "both preventive and remedial." 452 U.S. at 581, 593. In *Sedima*, the Court explained that RICO's text mandated a "less restrictive reading" than the one offered by the court of appeals to fully effectuate its remedial purpose. 473 U.S. at 497–98. In *National Organization for Women*, the Court rejected a limitation adopted by the court of appeals because Congress had not imposed any such requirement in either RICO's definitional section or operative language. 510 U.S. at 260–61. And in *Cedric Kushner Promotions*, the Court rejected another narrow construction that the text of the statute did not require. 533 U.S. at 163. This Court has heeded the Supreme Court's repeated admonitions,

rejecting narrow constructions of RICO's statutory terms and instead construing them liberally to effectuate its remedial purposes. *Odom*, 486 F.3d at 547.

However, the district court did not follow these oft-repeated instructions. Instead, it speculated, without any legal support, that "it seems implausible that RICO—a federal statute—was designed to provide redress for engaging in activities that are illegal under federal law." ER 6. But RICO clearly states that "*[a]ny* person injured in his business or property by reason of a violation of" 18 U.S.C. § 1962 may bring an action to recover treble damages. 18 U.S.C. § 1964 (emphasis added). RICO defines "person" to include "any individual or entity capable of holding a legal or beneficial interest in property," *see id.* § 1961(3), and this Court considers whether the plaintiff's "alleged business or property interest is cognizable under state law." *Newcal Indus., Inc. v. Ikon Office Sol.*, 513 F.3d 1038, 1055 (9th Cir. 2008). The district court's implied exception to RICO's reach lacks any basis in the statutory text.

In addition, the district court focused on only the remedial nature of RICO without considering its deterrent effect. RICO not only offers a remedy for those injured by racketeering activity but also creates a "far-reaching civil enforcement scheme." *Sedima*, 473 U.S. at 483. The district court did not pay any attention to how RICO's system of private enforcement should inform whether Plaintiffs may seek a remedy here. A refusal to allow a person injured by racketeering activity to

seek treble damages undercuts RICO's deterrent effect. Because the district court neglected to consider the preventive function of RICO's private enforcement scheme, the district court did not adequately analyze the legality of the remedy, public policy considerations, or the practical effects of the court's holding.

C. The district court would not have to contravene the CSA to provide Plaintiffs relief under RICO.

The district court rested its holding on the unfounded conclusion that affording Plaintiffs a damages remedy under RICO would require the court to violate federal law, specifically contravene the CSA and its prohibition on the cultivation of marijuana. However, the courts that have addressed this question and similar ones have permitted plaintiffs involved with the cannabis industry to bring claims for damages in federal court.

1. The few cases to address this question reject the district court's holding.

Few courts have addressed the question of whether a plaintiff with a connection to a state-authorized cannabis industry can state a claim for damages in federal court. But those who have done so have answered in the affirmative. In *Siva Enterprises v. Ott*, No. 218CV06881CASGJSX, 2018 WL 6844714 (C.D. Cal. Nov. 5, 2018), the court held that a business connected to the recreational cannabis industry could pursue federal claims against former officers and employees who had financially harmed the business. There, the plaintiff company Siva "provide[d] a

range of business solutions and operational services for the cannabis industry nationwide," and, over time, generated "valuable, confidential, proprietary and trade secret information not generally known to the public." *Id*. at *2 (cleaned up). The company and its CEO alleged that the defendants misappropriated the company's proprietary business information to start a competing cannabis business and steal Siva's clients. *Id*. at *2–3. The defendants raised a similar argument to the ones that Defendants raise here: "both of plaintiffs' federal claims involve the facilitation of the 'trafficking' of recreational marijuana—activity which is proscribed by the Controlled Substances Act ('CSA'), 21 U.S.C. §§ 801 *et seq.*, and therefore cannot give rise to a legally cognizable injury for purposes of Article III standing." *Id*. at *5.

The court rejected the defendants' argument. The plaintiffs had alleged a cognizable injury—misappropriation of proprietary business information and misuse of plaintiffs' identity and reputation—and it made no difference that the plaintiffs may have engaged in an enterprise illegal under federal law. *Id*. The court held that there was no conflict between the plaintiffs' claims and the CSA as the "plaintiffs [were] not seeking a remedy that would compel either party to violate the Controlled Substances Act." *Id*. A contrary holding would result in immunizing the defendants' unlawful actions from federal law simply because the plaintiffs were engaged in an illegal enterprise. *Id*.

While the court in *Siva* did observe that "the dispute in this case does not involve the actual production or sale of cannabis" but "concerns the actions of defendants in allegedly misappropriating plaintiffs' confidential business information and passing themselves off as Siva to take Siva's clients," *id*, the district court should not have dismissed *Siva*'s otherwise on-point holding on this basis, ER 6. First, the *Siva* court rested its holding on the fact that the *remedy requested* by the plaintiffs did not compel a violation of the CSA; that the dispute in *Siva* did not involve actual production or sale of cannabis was an additional, not required, reason to permit the plaintiffs' claims. Second, the *Siva* court did not draw a principled distinction between proprietary business information regarding cannabis sales and creation of cannabis products—nor could it, since both gain their value through an active cannabis enterprise. If a court may legally remedy harm to the former, which directly concerns the cultivation and sale of cannabis, it logically follows that the court should be able to legally remedy harm to the latter. *See Tarr v. USF Reddaway, Inc.*, No. 3:15-CV-02243-PK, 2018 WL 659859, at *3 (D. Or. Feb. 1, 2018) (plaintiff in a personal injury case could seek lost profit damages derived from the plaintiff's cannabis growing business); *see also id*. (defendant failed to cite "any authority that prohibits a claim of damages by an injured party in a personal-injury action in federal court when those damages are based on losses arising from a cannabis operation that is lawful under state law"). Third and lastly, the dispute in *Siva* and the dispute in

the present case concern cannabis in similar fashions. Cannabis may animate the circumstances under which this dispute arises, but at its core, the dispute concerns Defendants' pattern of racketeering activity that caused harm to Plaintiffs' business and property. The district court should have followed *Siva* and permitted Plaintiffs' RICO claims to stand.

The Tenth Circuit's decision in *Kenney v. Helix TCS, Inc.*, 939 F.3d 1106 (10th Cir. 2019), *cert. denied*, 141 S. Ct. 241 (2020), closely aligns with *Siva*'s reasoning. In *Kenney*, the plaintiff—a security guard for a business providing security, inventory control, and compliance services to the marijuana industry—brought an action under the Fair Labor Standards Act ("FLSA") against his employer. *Id*. at 1108. The Tenth Circuit rejected the employer's argument that the FLSA did not apply to workers like the plaintiff since Colorado's recreational marijuana industry is in violation of the CSA. *Id*. Because "[t]he FLSA is a remedial scheme for the benefit of all workers," applying the FLSA to the plaintiff did not conflict with the statute's purposes, nor did those purposes conflict with the CSA. *Id*. at 1111. Additionally, "case law has repeatedly confirmed that employers are not excused from complying with federal laws just because their business practices are federally prohibited." *Id*. at 1112. Because "the FLSA is focused on regulating the activity of businesses, in part on behalf of the individual workers' wellbeing,

rather than regulating the legality of individual workers' activities," the statute applied with equal force "in this novel context of the marijuana industry." *Id*.

Both *Kenney* and *Siva* relied on *Greenwood v. Green Leaf Lab LLC*, No. 3:17-CV-00415-PK, 2017 WL 3391671 (D. Or. July 13, 2017), *report and recommendation adopted*, No. 3:17-CV-00415-PK, 2017 WL 3391647 (D. Or. Aug. 7, 2017), which also rejected a defendant's argument that the case's proximity to the cannabis industry left the plaintiff without a remedy. With facts nearly identical to *Kenney*, the plaintiff—a courier transporting marijuana samples for a marijuana-testing facility—brought an action under the FLSA against his employer. *Id*. at *1. The court began with the premise that "the FLSA is a remedial statute to be construed liberally in favor of employees; exemptions are narrowly construed against employers," *id*. at *2 (citation and internal quotation marks omitted), and concluded "that any possible violations of the Controlled Substances Act are not relevant to whether the FLSA's protections apply to Plaintiff," *id*. at *2–3. In the court's view, "just because an employer is violating one federal law, does not give it licence [sic] to violate another." *Id*. at *3 (citation and internal quotation marks omitted).

Siva, *Kenney*, and *Greenwood* demonstrate the errors in the district court's holding. First and foremost, these cases clearly show that the cannabis industry is not invisible to federal law, and federal civil laws do not become inapplicable simply because a claim involves the cannabis industry. Instead, the analysis turns on the

facts and circumstances of the case, and courts must consider both the need to compensate the victim and to deter the wrongdoer. *Siva* underscores that providing a remedy to a cannabis business harmed by the wrongful acts of another does not violate the CSA, and federal courts may entertain such damages claims. *Kenney* and *Greenwood* instruct that a defendant cannot escape liability under federal law for wrongful acts simply because the underlying business transaction may not comport with federal law. As the courts observed in *Kenney* and *Greenwood*, the court must focus on the purposes animating the statute forming the basis of the plaintiff's claim. Like the FLSA, "RICO should 'be liberally construed to effectuate its remedial purposes.'" *Odom,* 486 F.3d at 547 (quoting *Sedima*, 473 U.S. at 498). In sum, a court cannot deny a remedy to a plaintiff—nor permit those who commit wrongful acts to escape liability and accountability—simply because of a connection to the cannabis industry.

Here, the district court sharply deviated from these cases. First, it reflexively denied relief to Plaintiffs due to their connection to the cannabis industry, but that alone cannot deprive Plaintiffs of a remedy. Next, it assumed, without analysis, that affording Plaintiffs a damages remedy would violate the CSA. And third, the court wholly failed to consider that its holding allowed Defendants to escape liability for their wrongful acts, which are plainly illegal under both federal and state law. Had the district court focused on RICO's purposes—providing a remedy for victims of

racketeering activity and deterring such wrongdoing—it would have concluded that, like the FLSA, RICO is concerned with regulating Defendants' conduct, not the legality of the victim's business, and no conflict arises between RICO and the CSA.

In sum, the district court failed to offer any principled basis for why the decisions of the courts that have addressed the question raised by this case should be disregarded. This Court should follow the reasoning of those courts and reverse the district court's judgment.[6]

2. Federal courts regularly enforce contracts that concern the cannabis industry.

As the above cases concern broad, remedial federal statutory schemes, their decisions allowing a plaintiff with a connection to the cannabis industry to state a claim for damages in federal court are directly instructive here. But this Court can also look to how district courts approach claims arising out of contracts relating to the sale and cultivation of cannabis. While the issue in Plaintiffs' appeal here is the dismissal of their RICO claims, federal courts are faced with a similar question of whether a plaintiff connected to the cannabis industry may seek a legal remedy for

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[6] *Grandpa Bud, LLC v. Chelan County Washington*, No. 2:19-CV-51-RMP, 2020 WL 2736984 (E.D. Wash. May 26, 2020), is wholly inapposite. There, the question was whether the plaintiff was "deprived of a constitutionally protected liberty or property interest" in connection with its federal due process claim under 42 U.S.C. § 1983. *Id*. at *3. The court reasoned that "there is no federal constitutional right to cultivate cannabis," and "[e]ven when cannabis production is a legitimate use of one's property at the state level, such use is not recognized as a protectable property interest under the U.S. Constitution." *Id*. at *4. That holding has no relevance here.

breach of contract. This Court has adopted a flexible approach toward assessing a contract's enforceability. Specifically, it has explained that "[n]uanced approaches to the illegal contract defense, taking into account such considerations as the avoidance of windfalls or forfeitures, deterrence of illegal conduct, and relative moral culpability, remain viable in federal court . . . [so] long as the relief ordered does not mandate illegal conduct." *Bassidji v. Goe*, 413 F.3d 928, 937–38 (9th Cir. 2005). Thus, courts should consider whether a remedy exists "that would not require a court to order a legal violation." *Id*. at 939. No such remedy existed in *Bassidji*; enforcement of the contract would have mandated illegal conduct, because requiring the defendant to pay the plaintiff would have furthered trade with an Iranian company and provided funds to the Iranian economy in contravention of an executive order issued by the President. *Id*. at 939. But if a legal remedy could have been crafted, then the contract could have been enforced. *Id.*

Heeding this call for flexibility, courts in this Circuit have enforced contracts concerning cannabis and rejected defendants' arguments that the subject matter of the contracts or any remedy is "illegal." This reasoning is best demonstrated by the district court's decision in *KUSH, Inc. v. Van Vranken*, No. 220CV649JCMDJA, 2020 WL 8371452 (D. Nev. June 19, 2020). In *KUSH*, both parties operated in the medicinal and recreational marijuana industry, and the defendant agreed to transfer to plaintiff a 60% membership interest in his business entity in return for the plaintiff

conveying stock in itself and its parent company to the defendant. *Id*. at *1. The plaintiff brought a breach of contract claim after the defendant failed to perform, and the defendant argued that their agreement was void since any remedy would require that the court enforce a contract for the operation of a cannabis-cultivation business in violation of the CSA. *Id.* at *4. Surveying the changing legal landscape for both medicinal and recreational marijuana, the court observed that "[b]ecause of state legalization of marijuana, federal courts have been using a more nuanced approach to determine whether to enforce marijuana-related contracts" and to assess arguments of illegality. *Id*. at *5. The court explained that practical realities necessitated such an approach:

> Moreover, as more states regulate and legalize marijuana, the number of marijuana-related contractual disputes will inevitably rise. Using Van Vranken's black-and-white approach in such cases would set a precedent that allows remorseful parties—who willfully entered into such contracts—to evade their contractual obligations by going to federal court and asserting the federal prohibition of marijuana. This would undermine the fundamental reason why people willfully enter into contracts: to hold each party accountable to their promises. Further, as the court in *Mann v. Gullickson* held, voiding marijuana-related contracts and allowing parties to shield themselves from their contractual obligations would potentially induce illicit conduct, namely rampant nonpayment for services rendered pursuant to a contract. *Mann*, 2016 WL 6473215, at *9.

Id. Accordingly, the court held that courts must "enforce 'illegal' contracts in order to avoid unjustly enriching a defendant or disproportionately penalizing a plaintiff." *Id*. The *KUSH* court's reasoning accords with this Court's flexible approach. And the court's concern with unjust enrichment and evasion of contractual obligations is

in harmony with RICO's purposes. If a court may enforce an "illegal" contract to prevent inequitable outcomes in the contract context, then certainly it can remedy harms to a cannabis business in the RICO context.

Mann v. Gullickson, No. 15-CV-03630-MEJ, 2016 WL 6473215 (N.D. Cal. Nov. 2, 2016), also illustrates a proper application of this Court's precedent. After the defendant breached an agreement to buy two cannabis businesses from the plaintiff, the plaintiff filed a breach of contract claim in federal court. *Id*. at *1. The court held that "ordering payment on the parties' contract would not mandate illegal conduct" because "[m]andating that payment does not require [the defendant] to possess, cultivate, or distribute marijuana, or to in any other way require her to violate the CSA." *Id*. at *7. In sum, the court "[found] no reason why the parties' agreement would not be enforceable." *Id*.; *see also Ginsburg v. ICC Holdings, LLC*, No. 3:16-CV-2311-D, 2017 WL 5467688, at *8 (N.D. Tex. Nov. 13, 2017) (enforcing contract relating to cannabis industry and permitting relief where "[o]btaining this relief does not require that [the defendant] manufacture, distribute, dispense, or possess marijuana.").

Like *KUSH* and *Mann*, *Green Earth Wellness Center, LLC v. Atain Specialty Insurance Co.*, 163 F. Supp. 3d 821 (D. Colo. 2016), provides a nuanced approach toward enforcement of contracts concerning cannabis cultivation. In that case, a medical marijuana business brought a breach of contract action against its insurance

carrier for the carrier's failure to compensate the business for marijuana plants destroyed in a fire. *Id*. at 823. The insurer argued that even if the policy did provide coverage, public policy would require that coverage be denied, *id*. at 832, but the court disagreed, concluding that ordering the insurer to comply with the contract and pay damages was not illegal under federal or state law, *id*. at 834–35.

As the nuanced approach of these cases illustrate, where a court can provide a remedy that does not require illegal conduct, the court should allow the plaintiff to seek damages for wrongdoing they may have suffered. As was the case in *Mann*, ordering Defendants to pay a remedy to Plaintiffs here would not require Defendants to engage in any illegal conduct. Requiring that Defendants compensate Plaintiffs for the harms to their property and business does not require Defendants to possess, cultivate, or distribute marijuana, or otherwise violate the CSA. Instead, the payment of treble damages by Defendants here under RICO serves the dual purpose of providing a remedy for the fraudulent scheme employed by Defendants *and* serving as a deterrent to future violators. For this reason, application of this caselaw to the RICO context is straightforward. These cases recognize both that the need to provide the plaintiff a remedy is heightened when the defendant is unjustly enriched to the plaintiff's detriment, and that the practical realities of state legalization of cannabis call for greater protection for businesses involved in the cannabis industry and less rigid application of bars on recovery based on the unique interplay of

cannabis law at the federal and state levels. RICO is designed to prevent the type of wrongful profit gained by Defendants to the harm of Plaintiffs (and many others) and protect these victims from racketeering. Allowing Plaintiffs a remedy fits seamlessly within this Court's flexible approach toward contract enforcement. Accordingly, the district court erred in holding that any remedy here would require contravention of the CSA.

Some district court decisions have denied relief where the plaintiffs sought to exercise equity rights or obtain equity interests in cannabis companies. These courts recognized that the mere presence of cannabis did not automatically bar recovery by the plaintiffs, but found that the specific circumstances prevented a legal remedy. Specifically, these courts were asked to grant an equity interest in a cannabis company or a right to its future profits. *See, e.g.*, *Sensoria, LLC v. Kaweske*, No. 20-CV-00942-MEH, 2021 WL 2823080, at *9 (D. Colo. July 7, 2021); *Sensoria, LLC v. Kaweske*, No. 20-CV-00942-MEH, 2021 WL 103020, at *6 (D. Colo. Jan. 12, 2021) (court's previous ruling on motion to dismiss); *Polk v. Gontmakher*, No. 2:18-CV-01434-RAJ, 2020 WL 2572536 (W.D. Wash. May 21, 2020); *Bart St. III v. ACC Enterprises, LLC*, No. 217CV00083GMNVCF, 2018 WL 4682318, at *5 (D. Nev. Sept. 27, 2018). These courts reasoned that granting such relief compelled future violations of the CSA. Whether these courts reached the right conclusion or not,

Plaintiffs' requested relief—a payment of damages for past wrongful conduct that unjustly enriched the Defendants—raises none of these concerns.

In sum, "even where contracts concern illegal objects, where it is possible for a court to enforce a contract in a way that does not require illegal conduct, the court is not barred from according such relief. However, if, as in *Bassidji*, the enforcement of a contract would require the court to order illegal conduct, such contracts are unenforceable." *Mann*, 2016 WL 6473215, at *7; *see also Ginsburg*, 2017 WL 5467688, at *8 ("In practice, however, federal courts have taken a more flexible approach to the question of enforceability.") (collecting cases). Here, cases similar to Plaintiffs' demonstrate that Plaintiffs can be afforded relief under RICO without requiring Defendants to violate the CSA, and thus, the district court wrongly refused to hear Plaintiffs' RICO claims.

While the caselaw in this area may be sparse, all relevant decisions point in the same direction: the district court erred in dismissing Plaintiffs' RICO claims, and its decision must be reversed.

D. Allowing Plaintiffs to recover damages under their RICO claim is not contrary to public policy.

The district court grounded its ruling in its view that because Plaintiffs' business activities are illegal under federal law, it would be contrary to public policy to afford Plaintiffs a remedy under RICO. However, the district court was wrong to

treat Plaintiffs' conduct as obviously illegal, and thus, affording Plaintiffs a remedy is not contrary to public policy.

1. The district court was wrong to characterize Plaintiffs' activities as "unequivocally illegal under federal law."

The district court viewed Plaintiffs' business activities as "unequivocally illegal under federal law." ER 5. At the outset, it is undisputed that Plaintiffs' activities complied with California state law. Since 1996, California has permitted various cannabis-related activities. Approved by California voters in 1996, California's Compassionate Use Act of 1996, Cal. Health & Safety Code § 11362.5, provides that state criminal charges involving marijuana, including possession and cultivation of marijuana, do not apply to a person using marijuana for medical purposes on a physician's recommendation. *Id*. § 11362.5(d). In 2004, the state legislature expanded these immunities through the Medical Marijuana Program, *id.* §§ 11362.7 *et seq.*, and in 2016, California voters approved Proposition 64, the Adult Use of Marijuana Act, permitting recreational use of cannabis and sale and cultivation of cannabis for recreational use. *See id*. §§ 11362.1 *et seq*. Thus, California law generally permits medicinal and recreational use of cannabis and sale and cultivation of cannabis for such uses.

However, what these laws permit, the CSA prohibits. *See United States v. McIntosh*, 833 F.3d 1163, 1176 (9th Cir. 2016). Under the CSA, marijuana is classified as a Schedule I substance. *See* 21 U.S.C. §§ 802(16), 812(c), Schedule I

at (c)(10) (defining "marihuana" and classifying as a Schedule I controlled substance"). In light of this classification, under the CSA, the manufacture, distribution, or possession of marijuana with intent to manufacture, distribute, or dispense is a criminal offense. *Id*. §§ 841(a)(1), (b)(1)(D); *see also id.* § 844(a) (criminalizing simple possession).

"Nevertheless, federal policy regarding enforcement of the CSA has been less than clear since 2009." *Mann*, 2016 WL 6473215, at *4. "[T]he nominal federal prohibition against possession of marijuana conceals a far more nuanced (and perhaps even erratic) expression of federal Policy." *Green Earth Wellness Ctr.*, 163 F. Supp. 3d at 832. Since 2009, the federal government has given "conflicting signals" regarding marijuana regulation and enforcement, *id*.at 832 & n.7 (collecting Department of Justice memoranda and briefing, federal statutes, and caselaw), leading to "a continued erosion of any clear and consistent federal public policy in this area," *id*. at 835; *see also id.* at 833 (emphasizing "the difference between the federal government's *de jure* and *de facto* public policies"). In sum, federal authorities have expressed "an ambivalence towards enforcement of the Controlled Substances Act in circumstances where a person or entity's possession and distribution of marijuana was consistent with well-regulated state law." *Id*. at 833.

Notably, this inconsistent federal policy toward marijuana regulation and enforcement comes from not just the executive branch's enforcement decisions and

priorities, but also Congress itself. In each budget cycle since fiscal year 2014, Congress has passed an appropriations rider barring the Department of Justice from using taxpayer funds to prevent states from implementing their own laws that authorize the use, distribution, possession, or cultivation of medical marijuana. Congressional Research Service, *State Marijuana Legalization and Federal Drug Law: A Brief Overview for Congress* (May 29, 2020), at 4, available at https://crsreports.congress.gov/product/pdf/LSB/LSB10482.

The first iteration of this rider, § 538 of the Consolidated and Further Continuing Appropriations Act of 2015, Pub. L. No. 113-235, 128 Stat. 2130 (2014), prohibits the Department of Justice from using any of the funds made available in the Act "to prevent [32 specified] States [, including California and the District of Columbia] from implementing their own State laws that authorize the use, distribution, possession, or cultivation of medical marijuana." *Id*. at 2217; *see United States of Am. v. Marin All. For Med. Marijuana*, 139 F. Supp. 3d 1039, 1043 (N.D. Cal. 2015) ("The plain reading of the text of Section 538 forbids the Department of Justice from enforcing this injunction against [a medical marijuana dispensary] to the extent that [the medical marijuana dispensary] operates in compliance with California law."). The following year, Congress included this same rider in § 542 of the Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, 129 Stat. 2242 (2015), expanding it to include additional states and Guam and Puerto

Rico and again prohibiting the Department of Justice from using funds made available by the Act "to prevent any of them from implementing their own laws that authorize the use, distribution, possession, or cultivation of medical marijuana." *Id*. at 2332–33; *see McIntosh*, 833 F.3d at 1177 ("[A]t a minimum, § 542 prohibits DOJ from spending funds from relevant appropriations acts for the prosecution of individuals who engaged in conduct permitted by the State Medical Marijuana Laws and who fully complied with such laws."); *see also id*. at 1177–78 ("In sum, the ordinary meaning of § 542 prohibits the Department of Justice from preventing the implementation of the Medical Marijuana States' laws or sets of rules and only those rules that authorize medical marijuana use.").

This appropriations rider continues to be enacted each year, even as recently as this past year. Congressional Research Service, *State Marijuana Legalization and Federal Drug Law: A Brief Overview for Congress* (May 29, 2020), at 4, available at https://crsreports.congress.gov/product/pdf/LSB/LSB10482; *see also* Consolidated Appropriations Act, 2021, Pub. L. No. 116-260, § 531, 134 Stat. 1182, 1282–83 (2020). While the rider may not directly address state-legal activities involving recreational marijuana, it is clear that Congress, like federal authorities, has taken a passive approach toward treatment of cannabis activities that comply with state law. Like any other statute passed by both houses of Congress and signed by the President, the appropriations rider carries equal weight as and stands on equal

footing to the CSA. Moreover, enacted year after year since 2014, the rider offers the most recent insight into Congressional policy in this area. The district court's broad statement that Plaintiffs' activities are "unequivocally illegal under federal law" cannot be squared with the reality that federal authorities and Congress have undermined the CSA's cannabis prohibitions, particularly those complying with state law, and rejected a policy of unequivocal enforcement of the CSA.

2. Allowing Plaintiffs a remedy is consistent with public policy.

The district court concluded that allowing Plaintiffs a remedy under RICO would "be contrary to public policy." ER 5. The district court did not identify what public policy would be frustrated, hindered, or contravened, nor could it have. The policy of Congress and the executive branch is one of noninterference with state-sanctioned cannabis industries. For states that have legalized cannabis activities, federal policy is to avoid interference with these states' laws. *See, e.g.*, *KUSH*, 2020 WL 8371452, at *5 ("current public policy does not discourage marijuana companies from entering into contracts in states where marijuana is legal"); *Green Earth Wellness Ctr.*, 163 F. Supp. 3d at 832 (federal policy is "ambivalen[t] towards enforcement of the Controlled Substances Act in circumstances where a person or entity's possession and distribution of marijuana was consistent with well-regulated state law"). On this point, Congress and the executive branch are in harmony. The Department of Justice has set enforcement priorities, and Congress has restricted the

Department of Justice from using taxpayer funds to prosecute medical marijuana-related activities in states that have legalized such uses. Given that both political branches have reached a consensus on how the federal government should approach cannabis activities complying with state law, it only makes sense for the apolitical branch to follow the lead of Congress and the executive branch and avoid actively inhibiting cannabis use and cultivation that is conducted in compliance with state laws. Courts should hesitate to disrupt the balance struck by those branches that set the policy the judiciary follows. Allowing Plaintiffs to state RICO claims better aligns with federal policy in this area, and the district court's contrary ruling should be reversed.

Additionally, while the district court stated that its ruling accorded with public policy regarding cannabis cultivation, its holding clashes with other aspects of federal public policy, particularly the longstanding interest and purpose in punishing and deterring racketeering activity. As this Court has recognized, Congress intended RICO to serve a broad remedial purpose and elected to use private suits as an enforcement scheme. There is no support for the notion that while Congress intended to proscribe racketeering activity, it was content to allow such wrongful acts to flourish against victims that may be engaging in any of the numerous state-regulated cannabis industries. The district court's holding essentially licenses racketeering activity against victims that engage in activities that may be unlawful

at the federal level, but entirely legal at the state level, and fails to explain why allowing unquestionably wrongful acts to occur is consistent with federal public policy. It makes little sense that simply because the adjacent conduct may be illegal per the CSA (but not treated as such by Congress or the Department of Justice), public policy calls for allowing even more wrongful acts to be committed with impunity. The district court examined one narrow sliver of federal public policy; looking at the whole pie, public policy considerations call for allowing Plaintiffs a remedy under RICO.

In sum, allowing Plaintiffs a remedy under RICO preserves the policy decisions of the political branches and furthers RICO's aims. Denying them relief clashes with the priorities of Congress and the executive branch and wholly undermines the purposes of RICO. This Court should adopt the approach that reinforces the political branches' policy choices and reverse the district court's judgment.

E. The district court's holding produces alarming consequences.

The district court's holding causes those engaged in the cannabis industry to become invisible to the law—with industry victims losing the protections afforded by federal laws and industry perpetrators being given carte blanche to harm others. It also threatens the ability of states to serve as the laboratories that the Supreme

Court has frequently praised. According to the district court, those engaged in cannabis enterprises may never recover damages in federal court. For example:

- Consider a cannabis company that patents a cannabis farming and production technology. While a patent may issue for such an invention, the district court's holding would not permit the business to enforce the patent and recover damages, and the ruling would enable anyone to violate the patent rights of a cannabis business.
- Consider an employee at a cannabis company who is paid below minimum wage and brings an action under the FLSA. Recovery of lost wages would not be permitted by the district court because the damages would not only derive from an illegal enterprise but would also compensate someone engaging in that enterprise.
- Consider employees of a cannabis company which provides its workers a retirement plan. If the company fails to perform its fiduciary duties under the Employee Retirement Income Security Act of 1974 ("ERISA") or otherwise mismanages the employees' retirement investments, the district court's holding hinders the employees' ability to avail themselves of the protections offered by ERISA.
- Consider an employee of a cannabis company who suffers discrimination at work and seeks to bring a claim under Title VII of the

Civil Rights Act of 1964 against the employer. The district court's holding would leave the employee without a remedy and enable the employer to discriminate against its employees.

This loss of federal protection for the cannabis industry under a wide variety of otherwise uniform federal laws that regulate the activity, not the legality, of businesses will have a significant impact on states, the nationwide economy, and the people working in the industry. Eighteen states now allow adult recreational use, and 36 allow for medicinal use. *State Medical Cannabis Laws*, National Conference on State Legislatures (Nov. 29, 2021), https://www.ncsl.org/research/health/state-medical-marijuana-laws.aspx. Legal sales across the United States reached a record $17.5 billion, a 46% increase from 2019 that continued the industry's explosive growth year after year. Will Yakowicz, *U.S. Cannabis Sales Hit Record $17.5 Billion As Americans Consume More Marijuana Than Ever Before*, Forbes (Mar. 2, 2021, 3:43 PM), https://www.forbes.com/sites/willyakowicz/2021/03/03/us-cannabis-sales-hit-record-175-billion-as-americans-consume-more-marijuana-than-ever-before/?sh=14ae52ab2bcf. By 2026, the legal cannabis market is expected to reach $41 billion in annual sales, roughly the size of the craft beer industry. *Id*. As of 2021, the industry employs 321,000 full-time equivalent jobs. Bruce Barcott, Beau Whitney, & Janessa Bailey, *The US cannabis industry now supports 321,000 full-time jobs*, Leafly (Feb. 6, 2021),

https://www.leafly.com/news/industry/cannabis-jobs-report. The number of legal cannabis workers in the United States exceeds the number of electrical engineers, EMTs, and paramedics, and the United States now employs twice as many legal cannabis workers as dentists. *Id*. The industry gained 77,300 full-time jobs in 2020, a 32% increase despite a year marked by unemployment and recession. *Id*. The district court's decision threatens this rapidly growing industry, and this Court's affirmance could have devastating consequences for cannabis businesses—and the hundreds of thousands of workers operating them.

Not only does the district court's decision deprive those connected to the cannabis industry of legal protection, but it also creates a windfall for those engaging in wrongful acts. This case exemplifies those alarming consequences. Here, Defendants committed numerous wrongful acts and caused Plaintiffs (and many other innocent victims) severe and significant financial and proprietary harm. But according to the district court, Defendants are permitted to reap the gains of their wrongful acts. Ironically, in its desire to deter activities illegal under the CSA, the district court enables even more wrongful and illegal conduct by letting parties like Defendants evade liability—while themselves operating an even larger cannabis business.

The district court's decision lacks any legal support, undermines RICO's purposes, disrupts federal policy, and threatens significant harm to a growing industry. This Court must reverse the dismissal of Plaintiffs' RICO claims.

II. Even if the district court's holding were correct, some of the damages sought by Plaintiffs are not connected to cannabis cultivation.

Even if this Court were to agree with the district court that a plaintiff engaged in cultivating cannabis may not pursue damages to remedy an injury to that enterprise, only some of the damages sought by Plaintiffs are connected to cannabis cultivation. For those damages unconnected to cannabis cultivation, the district court's reasoning does not apply, and Plaintiffs should at least be able to state RICO claims relating to those harms. *See Bart St. III*, 2018 WL 4682318, at *6 (permitting plaintiff to state breach of contract claims for the terms of the contract that could be enforced without a violation of the CSA).

The harm suffered by Plaintiffs on account of Defendants' pattern of racketeering activity took many forms. ER 75 ¶ 154. Defendants' conduct caused harm to both Plaintiffs' business and property. Business harm included lost profits from the sale, production, and distribution of cannabis. ER 75–76 ¶¶ 155–58. But Plaintiffs' property harms were not so connected. Defendants also failed to reimburse Ms. Shulman for significant operational expenses she incurred (including through improvements to the land), damaged the Iron Angel Ranch, harmed the Iron

Angel brand, and deprived Ms. Shulman of her ownership interest in Wellsprings. ER 76–77 ¶¶ 159–61.

These harms do not implicate lost profits from cannabis sale, production, or distribution, but instead concern actual and real damage to property interests. They closely resemble the proprietary interests at issue in *Siva*. 2018 WL 6844714, at *5 (plaintiffs alleged that "defendants misappropriated plaintiffs' proprietary business information and misused plaintiffs' identity and reputation"). Here, Defendants' conduct caused out-of-pocket losses to Plaintiffs, and a loss in the value of Plaintiffs' property interests. Restoring that loss in value does not "provide a remedy for actions that are unequivocally illegal under federal law," nor does it "necessitate that a federal court contravene a federal statute." ER 5.

Indeed, the district court totally overlooked that not all of Plaintiffs' damages concern cannabis business harms. The court stated that "Plaintiffs seek damages for 'injury to their business,'" and "any relief would remedy Plaintiffs' lost profits from the sale, production, and distribution of cannabis." *Id*. But that is plainly wrong. Plaintiffs clearly claim injuries to their property, which the court never addressed. The court stated that "Plaintiffs' injuries to their cannabis business are not redressable under RICO" but failed to address Plaintiffs' injuries to their property interests. ER 6.

Thus, even if this Court agrees with the district court's reasoning, reversal is still warranted to allow Plaintiffs to pursue RICO claims as to their damages that do not implicate the sale, production, or distribution of cannabis.

CONCLUSION

For the foregoing reasons, Plaintiffs respectfully request that this Court reverse the district court's order finding that Plaintiffs cannot state a RICO claim for damages and dismissing Plaintiffs' Complaint.

Dated: December 15, 2021

Respectfully submitted,

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UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

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