Uniformity Up In Smoke: How the Controlled Substances Act Treats Similarly Situated Debtors Differently

Abstract

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Cannabis-related debtors have been continuously prevented from accessing relief in bankruptcy. The Controlled Substances Act functions as the key culprit preventing these debtors from achieving plan confirmation. With the widespread legalization of cannabis among the states, the disparate treatment of cannabis-related debtors breaches the uniformity requirement of the Constitution's Bankruptcy Clause. Until bankruptcy courts recognize that cannabis-related debtors are similarly situated to other debtors, however, cannabis-related debtors should seek ways to diversify their income so that, if filing a petition for bankruptcy becomes necessary, there exist sufficient non-cannabis related income to fund a reorganization plan and receive a discharge.

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I. INTRODUCTION

Cannabis-related debtors (hereinafter, CRDs[2]) have been prevented from accessing the full benefits that bankruptcy has to offer with little exception.[3] This preclusion is rooted in the Controlled Substances Act (CSA) and cannabis's status as a Schedule I substance.[4] Put simply, due to the plant's status in federal law, it is a crime to "knowingly open, lease, rent, use, or maintain any place, whether permanently or temporarily, for the purpose of manufacturing, distributing, or using" cannabis.[5] The U.S. Trustee, and sometimes creditors, refer to the CRDs' apparent violations of the CSA as a factual basis for their arguments to bankruptcy courts to reject plan confirmation for CRDs.

The common theme for CRDs that have been prevented from achieving plan confirmation is a complete lack of non-cannabis related income to fund a reorganization plan. Income based solely on proceeds derived from cannabis-related operations has been the common thread in Chapter 7,[6] Chapter 11,[7] and Chapter 13[8] cases for CRDs that have had their cases thrown out of bankruptcy.

This article will also explore two recent bankruptcy cases involving CRDs. The first case, currently within the jurisdiction of the Western District of Michigan's Bankruptcy Court analyzes the U.S. Trustee's and the debtor's competing arguments with respect to confirmation of a plan funded entirely by proceeds derived from cannabis operations. The second case explores what CRDs may face outside of bankruptcy.

One of the purposes of this article is to introduce a new argument in favor of allowing CRDs access to plan confirmation. The Constitution's Bankruptcy Clause requires that "laws on the subject of bankruptcies" be uniform.[9] Although the CSA is not a bankruptcy law, the Act's disparate and objective effects on similarly situated debtors has now become alarmingly significant due to the widespread legalization and regulation of cannabis on the

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[2] Throughout this article, CRDs refer to debtors engaged in operations directly within and ancillary to the cannabis industry. Therefore, CRD can refer to an entity that operates a dispensary, cultivation, or cannabis production facility. CRD may also refer to an entity that derives revenue from another company directly engaged in operations within the cannabis industry. For example, both the entity that leases warehouse space to another entity which cultivates cannabis are both considered CRDs for purposes of this article.

[3] *See infra* Section IV.A.

[4] *See infra* note 17.

[5] *Infra* note 30.

[6] *See Arenas v. U.S. Trustee (In re Arenas)*, 535 B.R. 845 (B.A.P. 10th Cir. 2015); *IN re Medpoint Mgmt., LLC*, 528 B.R. 178 (Bankr. D. Ariz. 2015); *Northbay Wellness Group, Inc. v. Beyries*, 789 F.3d 956 (9th Cir. 2015).

[7] *See In re Rent-Rite Super Kegs W. Ltd.*, 484 B.R. 799 (Bankr. D. Colo. 2012); *In re Arm Ventures, LLC*, 564 B.R. 77 (Bankr. S.D. Fla. 2017); *In re Way to Grow, Inc.*, 597 B.R. 111 (Bankr. D. Colo. 2018).

[8] *See In re McGinnis*, 453 B.R. 770 (Bankr. D. Or. 2011); *In re Johnson*, 532 B.R. 53 (Bankr. W.D. Mich. 2015); *Olson v. Van Meter (In re Olson)*, 2018 WL 989263 (B.A.P. 9th Cir. Feb. 5, 2018).

[9] U.S. Const. art. I, § 8, cl. 4.

state level. As of 2022, approximately 428,000 jobs are supported by the cannabis industry in the United States.[10] If Congress legalizes cannabis federally, this jobs figure could be as high as 1.75 million.[11] Even without federal legalization, the number of Americans relying on the cannabis industry for economic well-being is too large to continue CRD's pariah-like treatment within Bankruptcy. The continued denial of CRDs' access to bankruptcy relief becomes increasingly absurd as cannabis entities become accepted as legitimate businesses subject to state regulation. This article argues that under the Bankruptcy Clause's uniformity requirement, CRD's continued preclusion from plan confirmation pursuant to the CSA cannot stand.

To be sure, bankruptcy courts have not shied have from considering cases of past and possibly ongoing violations of non-bankruptcy laws. In one example, a bankruptcy court oversaw a voluntary Chapter 11, which was later converted to Chapter 7, that involved a debtor in possession of leaking containers that held toxic substances.[12] Another bankruptcy case that received Chapter 11 plan confirmation involved extensive environmental harm and criminal liability for the debtor's officers.[13]

This article will first discuss the Controlled Substances Act and its objective effects on CRDs and similarly situated debtors. Next, the argument that the disparate treatment of CRDs cannot continue in light of the Constitution's uniformity requirement will be presented followed by supporting Supreme Court caselaw. The article will conclude with an analysis of two recent bankruptcy cases involving CRDs.

II. Drug Control Meets Bankruptcy

This section will introduce the Controlled Substances Act including the competing recommendations made by President Richard Nixon's own commission on drug abuse. Section II.B. will first address why CRDs should be considered similarly situated to other debtors. Next, the section will discuss the objective effects of the Controlled Substances Act on CRDs including the Act's disparate treatment between CRDs and similarly situated debtors.

A. The Controlled Substances Act

Before President Richard Nixon declared drug abuse "public enemy number one,"[14] Congress was successful in passing the most extensive drug law of the twentieth century, the Comprehensive Drug Abuse Prevention and

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[10] *See* Bruce Barcott, Beau Whitney, Max Savage Levenson, and Chris Kudialis, *Jobs Report 2022* at 2, Leafly (2022) (stating that the authors found 428,059 full-time equivalent jobs supported by legal cannabis as of January 2022.").
[11] *See id.* at 7.
[12] *See Midlantic Nat'l Bank v. New Jersey Dept. of Envt'l Prot.,* 474 U.S. 494 (1986).
[13] *See In re Freedom Industries, Inc.,* Case No. 14-bk-20017 (Bankr. S.D. W.Va. Jan. 17, 2014).
[14] Richard Nixon Foundation, *President Nixon Declares Drug Abuse "Public Enemy Number One,"* YouTube (April 29, 2016), https://www.youtube.com/watch?v=y8TGLLQlD9M.

Control Act of 1970.[15] Congress enacted the Controlled Substances Act (CSA) as Title II of the Drug Abuse Prevention and Control Act and placed all substances that were already regulated under existing federal laws into one of five schedules.[16] The Supreme Court has described the CSA as "a lengthy and detailed statute creating a comprehensive framework for regulating the production, distribution, and possession of five classes of 'controlled substances.'"[17]

The Attorney General is tasked with scheduling a substance based on its potential for abuse, risk to public health, and risk of psychological or physiological dependence, among other factors.[18] "Marihuana" was found to be such a threat to public health, so highly addictive, and without any medically accepted use that the plant was deemed a Schedule I substance,[19] on par with heroin.[20] "When a substance is placed on Schedule I, it represents a legislative judgment that '[t]he drug … has a high potential for abuse; ... no currently accepted medical use in treatment in the United States; [and] ... [t]here is a lack of accepted safety for use of the drug or other substance under medical supervision.'"[21]

Classifying cannabis as a Schedule I controlled substance was contrary to the recommendation of President Nixon's National Commission on Marihuana and Drug Abuse. Raymond P. Shafer, the chairman of the commission, had actually recommended the decriminalization of cannabis in small amounts:

> "[T]he criminal law is too harsh a tool to apply to personal possession even in the effort to discourage use. It implies an overwhelming indictment of the behavior which we believe is not appropriate. The actual and potential harm of use of the drug is not great enough to justify intrusion by the criminal law into private behavior, a step which our society takes only with the greatest reluctance."[22]

The authors of the report also cautioned against the "legal oversimplification" of marijuana policy.[23] Our society may have already crossed the line into legal oversimplification, however, because the effects of

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[15] Pub. L. 91-513 (1970).
[16] *Id.*
[17] *Gonzales v. Raich*, 545 U.S. 1 at 24 (2005).
[18] *See* 21 U.S.C. § 811.
[19] *See* 21 U.S.C. § 812(c)(10).
[20] *See* 21 U.S.C. § 812(b)(10).
[21] 21 U.S.C. § 812(b)(1).
[22] *Marihuana: A Signal of Misunderstanding: First Report of the National Commission on Marihuana and Drug Abuse* at 140 (1972) (hereinafter, the "Shafer Report").
[23] *Id.* at 26 ("Perhaps the major impediment to rational decision-making is the tendency to think only in terms of the legal system in general and of the criminal justice system in particular. This thinking is understandable, given the history of marihuana's involvement with the criminal law. Nonetheless, the law does not exist in a social vacuum, and legal alternatives can be evaluated only with reference to the values and policies which they are designed to implement and the social context in which they are designed to operate.").

marijuana's criminalization have spilled into several areas of law, including bankruptcy.

B. THE CSA'S EFFECTS ON BANKRUPTCY LAW

The continued criminalization of cannabis cultivation, sale, and use is no longer in line with society's values and expectations.[24] Although the high-water mark for the War on Drugs was on June 17, 1971, when President Nixon declared his war on drugs, federal law has continually been resistant to seeing cannabis as anything less than a menacing public scourge.

Since 1978, when New Mexico enacted the first medical marijuana law, states have slowly legalized cannabis's medicinal and recreational use.[25] As of August 2022, nineteen states and the District of Columbia have passed laws that allow personal possession and consumption of cannabis by adults.[26] Each and every one of the states and Washington D.C. have a robust program that regulates the planting, harvesting, testing, processing, packaging, and sale of cannabis.[27] These robust regulatory programs allow entrepreneurs and investors to operate medical and recreational dispensaries provided they follow the strict guidelines of the state in which they do business. For example, the approximately one-hundred medical and recreational dispensaries that operate in Nevada must comply with the strict regulations of the Nevada Cannabis Compliance Board or risk losing their license.[28]

Although each dispensary, cultivation facility, and laboratory must comply with their respective state's strict regulatory requirements each operation is still a "business." Like all businesses, each dispensary and facility must pay employees, transact with vendors, buy or lease property, and undertake other regular operations. All businesses are susceptible to failure due to insufficient cashflow, limited borrowing, or being overleveraged. When unfortunate conditions befall an organization, a company may decide to file for Chapter 11 bankruptcy so it can reorganize its obligations, discharge debt, and continue operating with a fresh start.

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[24] *Id.* at 27 ("Where society is ambivalent about its attitude toward the behavior and other institutions are not committed to its discouragement, the law cannot be said to be working, even though many people may not engage in the behavior because it is against the law.")

[25] *See* Alice O'Leary-Randall, *Today Is the 40th Anniversary of America's First Medical Marijuana Law*, CANNABISNOW (February 21, 1978) https://cannabisnow.com/lynn-pierson-first-medical-marijuana-law/.

[26] *See States/Territories with Legalized Marijuana*, NORML, https://norml.org/laws/legalization/ (last visited Aug. 14, 2022).

[27] Otherwise known as "Seed to Sale." *See Seed to Sale 101*, GrowFlow, https://www.growflow.com/en/seed-to-sale-101 (last visited Aug. 14, 2022).

[28] *See* Licensed Nevada Cannabis Stores/Dispensaries, Cannabis Compliance Board – State of Nevada, https://ccb.nv.gov/list-of-licensees/ (last visited Aug. 14, 2022).

CRDs, however, have not been allowed the luxury of accessing bankruptcy relief, including Chapter 11 reorganization.[29] Because cannabis is a Schedule I drug,[30] it is unlawful for any entity to:

> "knowingly open, lease, rent, use, or maintain any place, whether permanently or temporarily, for the purpose of manufacturing, distributing, or using any controlled substance,"[31] or to
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> "control any place, whether permanently or temporarily, either as an owner, lessee, agent, employee, occupant, or mortgagee, and knowingly and intentionally rent, lease, profit from, or make available for use, with or without compensation, the place for the purpose of unlawfully manufacturing, storing, distributing, or using a controlled substance."[32]

These provisions of the CSA have kept honest but unfortunate CRDs from accessing much needed bankruptcy relief. As will be discussed in this article, the U.S. Trustee, as a component of the Department of Justice, consistently takes the position that CRDs cannot benefit from the protections and mechanisms of the Bankruptcy Code because a plan funded by income derived from cannabis operations does not comply with 11 U.S.C. § 1129(a)(3).[33]

The CSA's influence on the Bankruptcy Code has led to dissimilar treatment of similarly situated debtors. This disparate treatment has led to CRDs being characterized as "the boogeyman of bankruptcy jurisprudence."[34] Non-CRDs and CRDs that operate in states where the plant is legalized and regulated are similarly situated. For example, a retail clothing store and a liquor store are both are licensed to do business in their state. The latter business must merely comply with more regulatory requirements than the former business. The same can by said about an entity operating legally within the cannabis industry.

To be sure, the CSA is not bankruptcy law – the CSA is statutory law promulgated under Congress' commerce power to establish a cohesive legal framework to regulate certain drugs that are, in the Attorney General's eyes, deemed to pose a risk of abuse and dependence.[35] Due to the fact that a number of states have legalized and regulated cannabis for both medicinal and

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[29] *Infra* note 93.
[30] *Supra* note 18.
[31] *See* 21 U.S.C. 856(a)(1).
[32] 21 U.S.C. 856(a)(2).
[33] 11 U.S.C § 1129 states that "[t]he court shall confirm a plan only if … the plan has been proposed in good faith and not by any means forbidden by law."
[34] *Infra* note 109 at 12, n.25.
[35] *Supra* note at 2 (2005) ("The regulation is squarely within Congress' commerce power because production of the commodity meant for home consumption … has a substantial effect on supply and demand in the national market for that commodity.") *see also*, Joanna R. Lampe, *The Controlled Substances Act (CSA): A Legal Overview for the 117th Congress* at 1, Congressional Research Service (February 5, 2021), R45948.

recreational purposes, the CSA objectively affects the relationship between debtors and creditors. The fact that cannabis-related debtors must comply with complex state regulations and exist in defiance of the CSA's mandates does not sufficiently distinguish them as a separate class of debtors that justifies disparate treatment within bankruptcy. Without the premise that cannabis-related debtors are sufficiently distinct relative to other debtors, the CSA cannot continue to act as a barrier to sensible and pragmatic relief.

III. A Legal Basis for Allowing MRBs Access to Bankruptcy Relief

Academics, professionals, politicians, and laypersons alike can, with a modicum of effort and a dash of social awareness, articulate public policy arguments for the federal legalization of cannabis. But for tangible change to be affected, supporters of cannabis legalization need to form sound legal arguments for their cause. The purpose of this section is to articulate a new strain of legal argument, supported by constitutional law, to allow CRDs access to bankruptcy relief. If we accept the proposition that CRDs are similarly situated to other debtors, then we must also demand that CRDs be treated uniformly.

A. Uniformity

The twin goals of bankruptcy are to ensure an equitable distribution of assets to creditors and a fresh start for the discharged debtor.[36] Notwithstanding the CSA, no cogent reason exists to bar CRDs that operate in a state which regulates cannabis from accessing bankruptcy relief. CRDs are just like any other debtor. As shown through the discussion of MEG in section III, cannabis-related debtors have employees, vendors, and taxes to pay similar to all debtors who file a Chapter 11 Petition. All other things being equal, the only real difference between a CRD and a non-CRD is the industry in which the CRD operates and where it derives its revenue. This assertion is especially true in the nineteen states and District of Columbia where cannabis is regulated.[37]

CRDs and their creditors would be better served if both the U.S. Trustee and bankruptcy courts treated CRDs like any other business that files for bankruptcy. CRDs are subject to the CSA in addition to their own state's regulations. The CSA's disparate objective effects on CRDs and similarly situated debtors flies in the face of both accepted bankruptcy doctrine and Constitutional law. If equal distribution and a fresh start are the twin pillars of

[36] *See In re Neff,* 824 F.3d 1181, 1187 (2016) ("At the core of the Bankruptcy Code are the twin goals of ensuring an equitable distribution of the debtor's assets to his creditors and giving the debtor a fresh start." (citing *Sherman v. SEC* (*In re Sherman*), 658 F.3d 1009, 1015 (9th Cir. 2011), abrogated on other grounds by *Bullock v. BankChampaign*, N.A., 569 U.S. 267 (2013).) (internal quotation marks omitted).

[37] The author emphasizes that debtors in states where cannabis is regulated are the only debtors this argument should apply to.

bankruptcy, then the CSA should not stand in the way of CRD's relief, especially when the Constitution supports those objectives.

Article I, Section 8, Clause 4 of the United States Constitution grants Congress the power "to establish … uniform Laws on the subject of Bankruptcies throughout the United States."[38] Given the Constitutional status of the term "uniform," this requirement supersedes an outdated law passed when this nation was in the grips of reefer madness.[39] When a federal law stands in the way of the Constitutionally required attribute of uniformity in bankruptcy law, the former should yield to the latter. By upholding the supremacy of the Constitution,[40] both the U.S. Trustee and bankruptcy courts will not only promote equitable distribution to creditors, but also a fresh start to a legal, regulated CRD. Viewed this way, the adjudicative and regulatory bodies must err on the side of the Constitution rather than the CSA.

In *Railway Labor Executives v. Gibbons*, the Supreme Court determined that a law passed by Congress, could not survive scrutiny under the Bankruptcy Clause because the law did not apply consistently to a defined class of debtors.[41] The law at issue established that the trustee of a regional railroad company must provide economic benefits of up to $75million to the railroad's employees who were not hired by other railroads.[42] These benefits were considered priority administrative expenses under the law.[43] The law altered the relationship of the railroad company's remaining creditors and would have resulted in them being paid little to nothing on their claims.[44] The Supreme Court struck down the law because it was not uniform as required by the Constitution and only applied to one railroad.[45]

Although the CSA is not a "law on the subject of bankruptcies" like the law at the center of *Gibbons*, the holding in *Gibbons* still speaks to the CSA because of the CSA's objective effects on a CRD and its creditors. Indeed, the "subject of bankruptcies is incapable of final definition" and encompasses the "subject of the relations between [a] debtor and his creditors, extending to his and their relief."[46] Cannabis's federal illegality affects the relationship between CRDs and their creditors by preventing the cannabis-related debtor from accessing bankruptcy relief. Without bankruptcy, creditors must race to the courthouse to help ensure they get the biggest slice of the pie. Before the widespread legalization and regulation of cannabis among the states, it could not be said that the CSA substantially altered the relationship between debtors and creditors in the cannabis industry. The plant's legalization in a significant number of states has altered the legal landscape since the passage of the CSA.

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[38] U.S. Const. art. I, § 8, cl. 4.
[39] Reefer Madness (G&H Productions 1936).
[40] *Marbury v. Madison*, 5 U.S.C. 137 (1803) (standing for the proposition, among others, that Congress can pass no law that is contrary to the Constitution.)
[41] *See Railway Labor Executives' Ass'n v. Gibbons,* 455 U.S. 457, 473 (1982).
[42] *Id.* at 461-62.
[43] *Id.* at 463.
[44] *See id.* at 467.
[45] *See supra* note 40.
[46] *Wright v. Union Central Life Ins. Co.*, 304 U. S. 502, 513–514 (1938).

The CSA no longer operates as a mere regulatory law promulgated under Congress's commerce power; it is a law that significantly impacts various areas of law, including bankruptcy.[47] The Constitution demands that significant impact to be uniform among similarly situated debtors. And because CRDs are similarly situated to all other licensed and regulated debtors within states, the CSA must not prevent CRDs from accessing relief and obtaining a fresh start. Continuing to prevent access to relief amounts to disparate treatment in direct violation of the Bankruptcy Clause.

In addition to granting CRDs a fresh start, access to bankruptcy relief for CRDs promotes the creditors' bargain.[48] Without bankruptcy, CRDs must resort to alternative equitable remedies such as receiverships – a topic that will be explored in section IV.C. through a practical example – or the CRD's creditors must enter into intercreditor agreements, among other workarounds.[49] Alternative remedies do not offer the same guarantees, protections, and predictability.[50] Moreover, the U.S. Trustee is hindering payment of unsecured claims by maintaining that the debtor's violation of the CSA does not comply with 11 U.S.C. § 1129(a)(3).

The Bankruptcy Clause's uniformity requirement will be met if a court allows a CRD to proceed through bankruptcy to plan consummation. The uniformity requirement is not upended, however, in cases where a CRD that operates in a state that has neither regulated nor decriminalized the plant is precluded from accessing bankruptcy relief. In the latter case, the CRD, operating illegally both under federal and state law, is sufficiently dissimilar from other debtors. The lack of a legal nexus under state law rejection of plan confirmation under 11 U.S.C. § 1129(a)(3). "General operation of the [bankruptcy] law is uniform although it may result in certain particulars differently in different states."[51]

The Bankruptcy Clause demands uniform treatment in bankruptcy between similarly situated debtors. It prevents similarly situated debtors from being subjected to disparate treatment, whether that treatment comes from Congress, the U.S. Trustee, or the courts. The CSA has been the focal point for treating similarly situated debtors differently, among other injustices. As will be discussed in section IV.B., Master Equity Group, LLC, a legal business in every sense of the term, is subject to disparate treatment relative to other similarly situated debtors solely because it earns revenue from cannabis-related operations. This incongruent treatment, consequent of the CSA, cannot be

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[47] For example, the CSA's impact on copyrights with respect to entities operating within the cannabis industry and copyrights – perhaps a subject of a future article by the author.

[48] *See* Thomas H. Jackson, *Bankruptcy, Non-Bankruptcy Entitlements, and the Creditor's Bargain*, 91 YALE L.J. 857, 860 (1982) (discussing that "[a] more profitable line of pursuit might be to view bankruptcy as a system designed to mirror the agreement one would expect the creditors to form among themselves were they able to negotiate such an agreement from an ex ante position.").

[49] *See also* Michael R. Handler, Ellen M. Snare, and Christina M. Markus, *Lending to Cannabis Companies: No Bankruptcy, No Problem?*, AM. BANKR. L.J. (July 14, 2022).

[50] *Id.* at 1.

[51] *Hanover Nat. Bank v. Moyses*, 186 U.S. 181, 190 (1902).

said to meet the Constitution's uniformity requirement. The CSA must yield to the Constitution.

The next section will discuss support for this argument from the Supreme Court case in the context of similarly situated debtors, albeit in different federal districts, that were subject to disparate treatment as a result of federal law.

B. *SEIGEL V. FITZGERALD*

Siegel v. Fitzgerald[52] supports the view that the CSA should yield to the Constitution in cases where the CRD operates in a state where cannabis is legalized. In *Siegel,* the Court examined whether a 2017 Act (Pub. L. 115–72, Div. B, 131 Stat. 1229) that increased fees in the U.S. Trustee program met the Constitution's uniformity requirement when the fee increase did not apply to six judicial districts in North Carolina and Alabama.[53] Those six districts are not within the U.S. Trustee program but are a part of the separate Administrator Program. The 2017 Act increased the maximum fee rate for Chapter 11 cases in the U.S. Trustee from $30,000 a quarter to $250,000 a quarter.[54] The fee increase did not take effect in the Administrator Program districts until October 1, 2018, but it took effect in the first quarter of 2018 for districts within the U.S. Trustee Program.[55] Moreover, the fee increase applied to both pending and newly filed cases in U.S. Trustee Program districts, while it only applied to newly filed cases in Administrator Program districts.[56]

The trustee overseeing the Circuit City Chapter 11 joint-liquidation plan, filed for relief against the Acting U.S. Trustee of his region in the Eastern District of Virginia because the trustee paid $576,142 more in fees for the first three quarters of 2018 than he would have without the 2017 Act over that same period.[57] The case came before the Supreme Court after the Fourth Circuit reversed the Bankruptcy Court's ruling that held that the fee increase violated the uniformity requirement.[58] The Fourth Circuit found that the 2017 Act did not violate the uniformity requirement because the requirement forbids only "arbitrary geographic differences" and because the fee increase applied only to the districts in the program that were running out of funds, the fee increase was not arbitrary.[59]

The Supreme Court reversed the Fourth Circuit and held that "the [Bankruptcy] Clause does not permit Congress to treat identical debtors

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[52] *See Siegel v. Fitzgerald*, 596 U.S. ____, 142 S. Ct. 1770 (2022).
[53] *Id.* at *4-*5.
[54] *See id.* at *4 (discussing Congress' enactment of Pub. L. 115–72, Div. B, 131 Stat. 1229) (hereinafter, 2017 Act).
[55] *See id.* at *4-*5.
[56] *Id.* at *5.
[57] *See id.* at *5-*6.
[58] *See id.* at *6.
[59] *Id.*

differently based on a … distinction that Congress itself created."[60] The Court noted that Congress was responsible for the separation of the U.S. Trustee Program and Administrator Districts and was therefore responsible for the budgetary shortfall.[61]

As demonstrated by the over half-a-million dollar fee increase in Circuit City's liquidation plan, the 2017 Act significantly changed the obligations between creditors and debtors because "increasing mandatory fees paid out of the debtor's estate decreases the funds available to payment to creditors."[62] Presumably, the 2017 Act would not have been an issue, but for the 2017 Act's unequal implementation in Administrator Program districts compared to U.S. Trustee Program districts. Given the fact that there is nothing "geographically distinct about Alabama or North Carolina that justified a different approach in those states," the fee increase failed to meet the uniformity requirement.[63]

Taking the same approach as the Court did in *Siegel*, we have already established in section II.B. that the CSA changes the relationship between debtors and creditors. If cannabis-related debtors cannot access the relief offered by the Bankruptcy Code, then the creditor's bargain is turned on its head.[64] For instance, creditors and debtors partially base the terms of their agreements, such as the interest rate and repayment period, on the probability of risk that the debtor will default. Bankruptcy acts as a "floor" for how much a creditor can recover from a debtor that has defaulted.[65] Creditors adjust the terms of their agreements with debtors based on the amount of risk that the creditor is willing to take based on what the creditor would recover if the debtor were to file bankruptcy.[66] The CSA, by prohibiting CRD's access to bankruptcy relief, objectively changes the relationship between CRDs and their creditors – creditors and debtors must significantly alter the terms of their agreements because the creditors' bargain is strangely absent from otherwise similar business arrangements.

Next, we have also showed that the CSA arbitrarily treats similarly situated debtors differently.[67] As discussed, no reasonable difference exists

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[60] *See id.* at *13 (stating "the Bankruptcy Clause affords Congress flexibility to 'fashion legislation to resolve geographically isolated problems,' but as precedent instructs, the Clause does not permit Congress to treat identical debtors differently based on an artificial funding distinction that Congress itself created.") (internal citation omitted).

[61] *Id.* ("It is true that Congress' stated goal in raising fees in Trustee Program districts was to address this budgetary shortfall. That shortfall, however, existed only because Congress itself had arbitrarily separated the districts into two different systems with different cost funding mechanisms, requiring Trustee Program districts to fund the Program through user fees while enabling Administrator Program districts to draw on taxpayer funds by way of the Judiciary's general budget.")

[62] *Id* at *9.

[63] *See id* at *6.

[64] Jackson *supra* note 47.

[65] *See id.*

[66] *See id.*

[67] As emphasized in this article, this notion is only true in states that have legalized and regulated cannabis.

between CRDs and non-CRDs to justify disparate treatment. The CSA does not uniformly affect similarly situated debtors that are within the same state. As discussed in Section IV.B., the U.S. Trustee's position is that a CRD cannot achieve plan confirmation because its reorganization plan is funded by income derived from cannabis-related operations in violation of the CSA. On the other hand, a hypothetical debtor operating within the same state (i.e., a similarly situated debtor) with a reorganization plan that is not dependent upon cannabis-related income can achieve plan confirmation because it does not derive income from operations that violate 856(a)(1) and (2) of the CSA. Within the context of a state that has legalized and regulated cannabis, such disparate treatment is not uniform, arbitrary, and unconstitutional.

Siegal supports the argument that similarly situated debtors cannot be treated disparately under bankruptcy law. Like the dual U.S. Trustee and Administrator Programs in *Siegal*, the CSA creates a distinction between identical debtors that Congress itself manufactured.[68] Although the CSA is not a law "on the subject of Bankruptcies" to which the uniformity requirement would apply on its face, the objective effects of the CSA significantly alter the relationship between CRDs and their creditors and, at the same time, leave other similarly situated debtors unscathed and permitted to access bankruptcy relief. As more and more states legalize and regulate cannabis, the premise that CRDs are not similarly situated to non-CRDs, allowing the disparate treatment of the former, will become more difficult to justify.

IV. A Homogenous Income Stream Dooms A CRD's Bankruptcy Case

This section will address the common thread that a single income stream derived from operations that violate federal law is a reliable indicator that the CRD will not make it through to plan confirmation. Section IV.A. discusses a Ninth Circuit case in which the CRD was able to achieve plan confirmation by relying on non-cannabis related proceeds to fund its plan. A diversified income stream may be CRDs best path to successfully achieve plan confirmation until cannabis is federally decriminalized. The two sections that follow each focus on recent bankruptcy cases involving CRDs. The first case, involving Master Equity Group, LLC, is currently within bankruptcy as of August 2022. The U.S. Trustee overseeing the case, however, has objected to the CRD remaining in bankruptcy because its plan is funded exclusively by proceeds derived from federally illegal operations. The second case, *In re CWNevada*, involves a Nevada CRD's bankruptcy petition being dismissed for reasons other than its federally illegally income stream. The case is significant because it illustrates what CRD's face when they no longer have the protection that bankruptcy provides.

[68] *Supra* note 59.

A. *Garvin v. Cook Investments*

The CRD discussed in the following section maintains that the Ninth Circuit's ruling in *Cook Investments* provides a basis for the company's plan to be confirmed; however, a major difference exists between the CRD's plan of reorganization and the debtor's plan in *Cook Investments*: the CRD has no non-cannabis related income while the debtor in *Cook Investments* had a diversified income stream.

The debtor was comprised of five real estate holding companies that owned commercial real estate properties in Washington, a state that has legalized recreational use of cannabis since 2012.[69] One of its tenants, Green Haven, operated a cannabis production facility that "pumped out up to 300 pounds of bud a month."[70] After Cook defaulted on a bank loan, the company filed for Chapter 11 bankruptcy. The U.S. Trustee filed a motion to dismiss asserting that the Green Haven Lease constituted gross mismanagement under 11 U.S.C. § 1126(b).[71] The bankruptcy court, however, denied the motion.[72] The debtor later filed an amended plan that provided for it to continue as a going concern while repaying all of the creditors' claims in full.[73]

Under the amended plan, the bank's claim would be satisfied by having Cook's non-cannabis-related lessees paying their rents directly to the bank.[74] Cook was able to reject the Green Haven lease and structed the plan so that the rental proceeds from Green Haven (i.e., those directly attributable to cannabis operations) would be paid directly to Cook while non-cannabis-related proceeds would be used to satisfy the plan's monthly obligations.[75] The U.S. Trustee objected again, but this time the U.S. Trustee asserted that the plan violated 11 U.S.C. § 1129(a)(3) because, in its view, the amended plan was "proposed…by…means forbidden by law."[76]

The U.S. Trustee was referring to the CSA, specifically citing the section which makes it unlawful to "knowingly open, lease, rent, use, or

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[69] *Garvin v. Cook Investments NW, SPNWY, LLC*, 922 F.3d 1031, 1033 (2019).

[70] Cladia Yaw, *Mountain town's marijuana mishap was quite the stinker*, HeraldNet (Nov. 1, 2021) (The story of Green Haven's owner is remarkable: Vince Nguyen immigrated to Washington from Vietnam and broke into the medical marijuana industry after consenting to a blindfolded car ride to an undisclosed cannabis farm where he discovered his green thumb.) https://www.heraldnet.com/news/mountain-towns-marijuana-mishap-was-quite-the-stinker/.

[71] *Supra* note 68.

[72] *See id.* at 1033-34 (The bankruptcy court denied the motion without prejudice allowing the U.S. Trustee "to renew [the motion to dismiss] at plan confirmation." The Trustee, however, did not renew its motion to dismiss for gross mismanagement which "meant the bankruptcy court had no opportunity to consider whether the claimed gross mismanagement had been cured." The court seems to lament this and states that "[a]s a consequence, neither the bankruptcy court, nor the district court, nor this court could properly determine the applicability of the exception to dismissal for 'unusual circumstances.'" The Trustee apparently only wanted to litigate one issue at a time and saved that bullet in its chamber for another day.).

[73] *Id.*

[74] *Id.* at 1034.

[75] *Id.*

[76] *Id.*

maintain any place, whether permanently or temporarily, for the purpose of manufacturing, distributing, or using any controlled substance."[77] The U.S. Trustee maintained that, even though the amended plan made no explicit reference to the Green Haven lease, the reorganization plan was proposed by a means forbidden by law because Cook continued to receive rent payments from a cannabis-touching entity.[78] The Bankruptcy court nonetheless confirmed the amended plan.

The U.S. Trustee appealed the Bankruptcy Court's decision and the Ninth Circuit framed the issue as one of statutory interpretation. "Whether the Amended Plan was confirmable depends on whether § 1129(a)(3) forbids confirmation of a plan that is proposed in an unlawful manner as opposed to a plan with substantive provisions that depend on illegality."[79] The Ninth Circuit concluded that "§ 1129(a)(3) directs courts to look only to the proposal of a plan, not the terms of the plan."[80] The court ruled that bankruptcy judges are not to "gratuitously seek[] out possible illegalities in every plan,"[81] and concluded that because the plan was *proposed* in a lawful manner, "the Bankruptcy Court correctly concluded that it met the requirements of 11 U.S.C. § 1129(a)."[82]

In examining what actually occurred in this case, we find that the U.S. Trustee objected to a plan of reorganization that not only ensured the debtor continued as going concern, but also provided for the full repayment of all the debtor's obligations to its creditors. If that plan does not further the twin goals of the Bankruptcy Code, I don't know what does.[83] The U.S. Trustee, for its part, had to object to the debtor's plan of reorganization because the U.S. Trustee is a part of the Department of Justice, cannabis is a Schedule 1 drug within the Controlled Substances Act, and the amended plan *facilitated* illegal activity even though the plan made no mention of the Green Haven lease. Indeed, Green Haven, a cannabis-centric business, continued to pay the CRD, but those payments were outside the debtor's amended reorganization plan that was before the Bankruptcy Court. Both the Bankruptcy Court and the Ninth Circuit rejected the U.S. Trustee's reasoning because nothing in the proposal of the plan was unlawful.[84] If the Ninth Circuit sided with the U.S.

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[77] *Supra* note 30.
[78] *Supra* note 75 at 1035 ("Because it appears that Cook continues to receive rent payments from Green Haven, which provides at least indirect support for the Amended Plan, the Trustee asserts that it was "proposed … by … means forbidden by law.").
[79] *Id*
[80] *Id.*
[81] *See id.* at 1036 (citing *In re Food City, Inc.,* 110 B.R. 808, 812 (Bankr. W.D. Tex. 1990). (internal quotation marks omitted)
[82] *See id.* (citing *In re Gen. Dev. Corp.,* 135 B.R. 1002, 1007 (Bankr. S.D. Fla. 1991) ("Courts addressing the issue have uniformly held that Section 1129(a)(3) does not require that the contents of a plan comply in all respects with the provisions of all nonbankruptcy laws and regulations.") (internal quotation marks omitted).
[83] *See supra* note 35.
[84] Mark A. Salzberg, *Ninth Circuit Gives A Partial Green Light to Cannabis Company Bankruptcies*, The National Law Review (May 2, 2019)