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Northeast Bankruptcy Conference and Consumer Forum

From Green to Red: What Insolvency Professionals Need to Know About Cannabis

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Introduction to the Cannabis Industry

May 2022



Cannabis Business Consulting

Strategy – Compliance – Operations

1 Legal Cannabis in the United States



The legal cannabis market offers numerous opportunities with a high number of consumers and players

Market Highlights

- **Legalization**
 - **39 states** have legalized cannabis in some form:
 - 19 states have legalized **recreational** (also known as adult-use) cannabis
- **Market Landscape**
 - The legal cannabis industry in the United States grew **30%** in 2021
 - Legal recreational and medical cannabis sales (**\$27B**) outsold Starbucks' North American sales (**\$20.5B**) in 2021
- **Unique Players**
 - Food and beverage manufacturers such as **Heineken, Molson Coors,** and **Nestlé** have become investors in the US legal cannabis market
 - Products from these players include THC-infused beers & seltzers and CBD-infused liquid drops and gels

\$37.9B market value
by 2024 in North America

\$27B US consumer spend
estimated in 2021

\$10.9B flower sales
estimated in 2021 in the United States

\$19.9M equity investment
average in 2021 for cannabis companies

Sources: Visual Capitalist, TechCrunch, New Cannabis Ventures, BDSA, MJBizDaily

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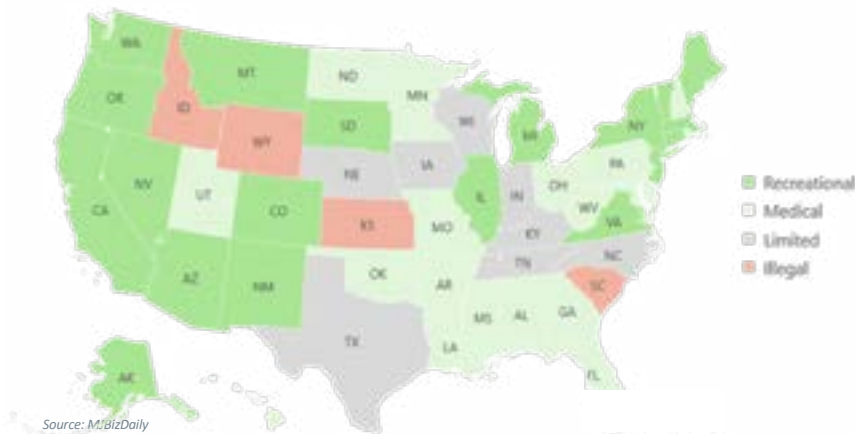
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2 Cannabis Legalization in the United States



States in the South and Midwest are lagging behind, but the momentum towards legalizing adult-use cannabis persists into 2022

Cannabis Legalization in Each U.S. State



Comments

- The Northeast and West Coast, both regions with large numbers of liberal voters, have the highest concentration of fully legal states
- In the Northeast, New Jersey, New York, and Connecticut have either already launched or are planning to launch an adult-use market in 2022
- Momentum is growing and more states are likely to legalize adult-use cannabis in 2022, such as Rhode Island and Delaware

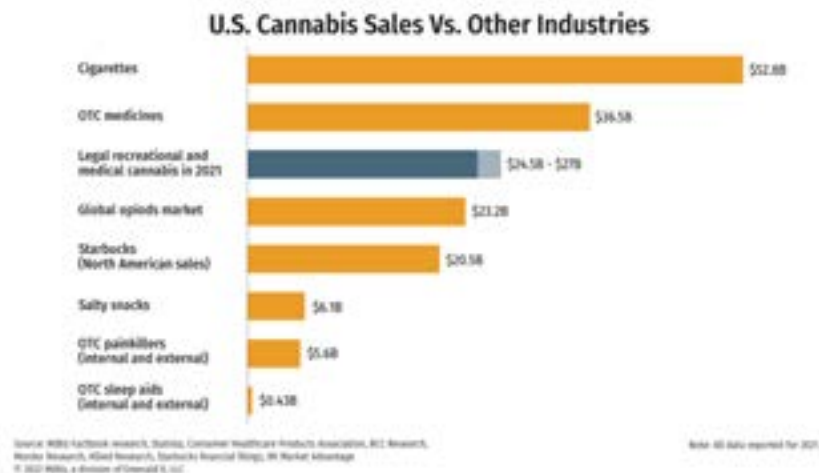
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3 US Cannabis Sales vs. Other Industries



The legal cannabis market in the US is growing quickly and has surpassed several other industries



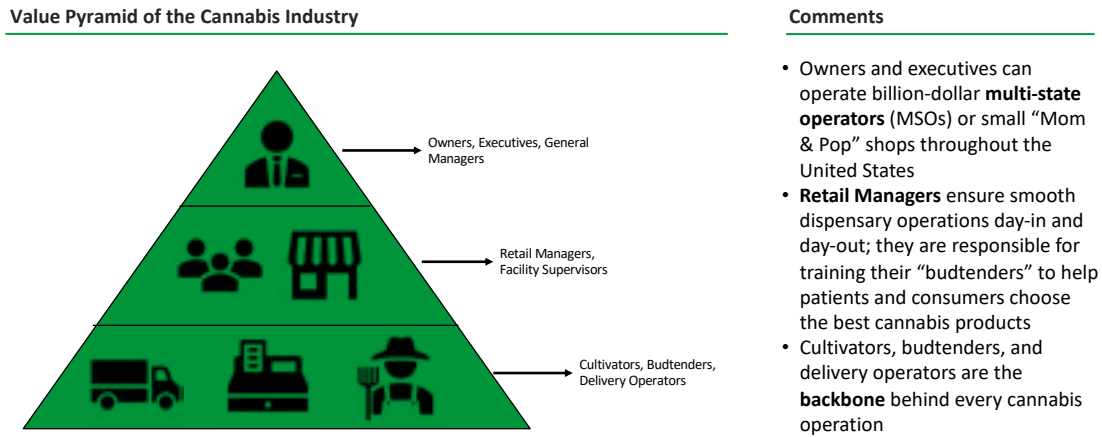
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4 The Value Pyramid of the Cannabis Industry



Along with the supply chain, the cannabis industry's value pyramid provides its own unique value in getting products to the end consumer



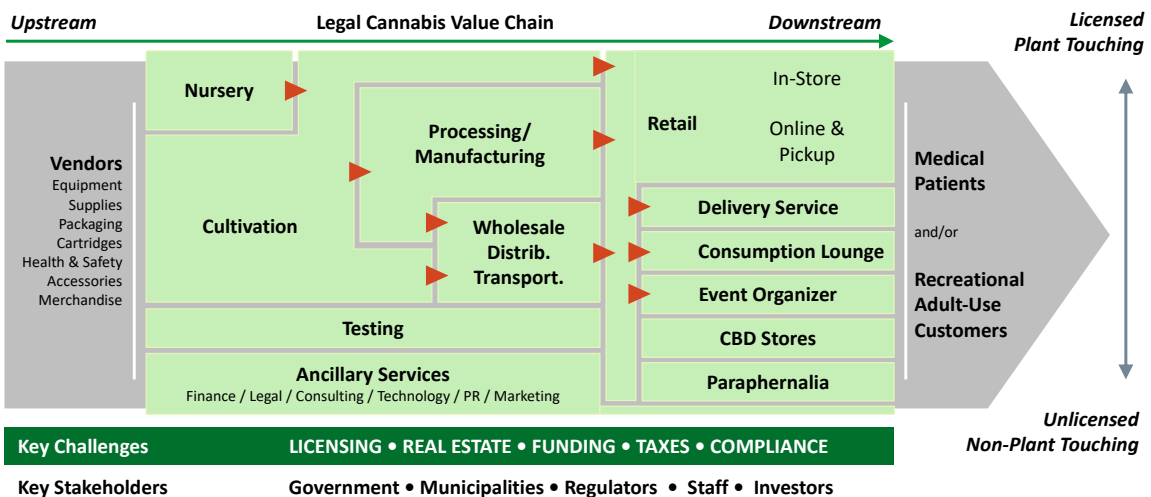
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5 The Legal Cannabis Value Chain



There are multiple opportunities across the value chain beyond the more typical avenues of cultivation and retail



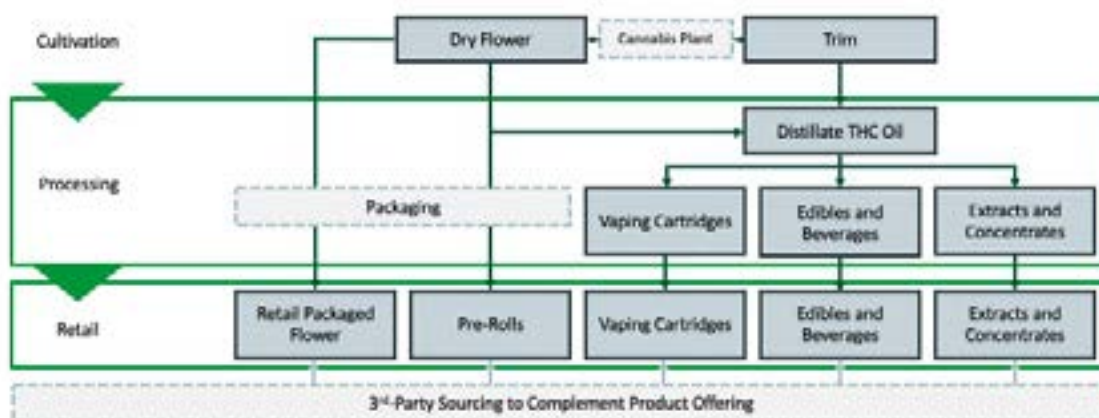
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6 Cannabis Product Flow



Cannabis flower can be used for a wide variety of products after cultivation, such as vapes, edibles, and concentrates



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7 The Science Behind Cannabis - The Cannabis Plant



The cannabis plant has several different parts, each with their own unique purpose



Source: Leafly

The Cannabis Plant

- Trichomes – rich in cannabinoids and terpenes; most often used in concentrates and extracts
- Node - Connect new stem offshoots and take the shape of a branch, a leaf, or bud; points where the plant's younger branches split from the main stem
- Stem – transports water and nutrients to the plant from the roots
- Fan Leaves – While an important part of the plant's photosynthesis, these leaves are removed during harvest
- Pistil – the primary part of female cannabis' plants reproductive system
- Cola – Several small clusters of flowers at the end of the stem; the more there, the better the plant's quality
- Calyx – In the flowering stage, the calyx is the first part formed; provides the plant with stability

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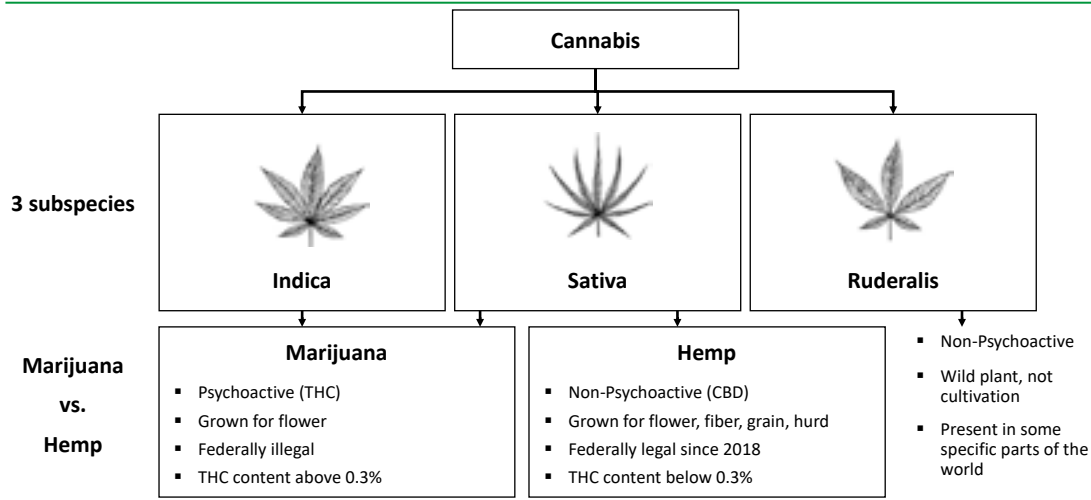
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The Science Behind Cannabis – Marijuana and Hemp



Cannabis can be divided into 3 subspecies. Marijuana is psychoactive, while hemp is not.



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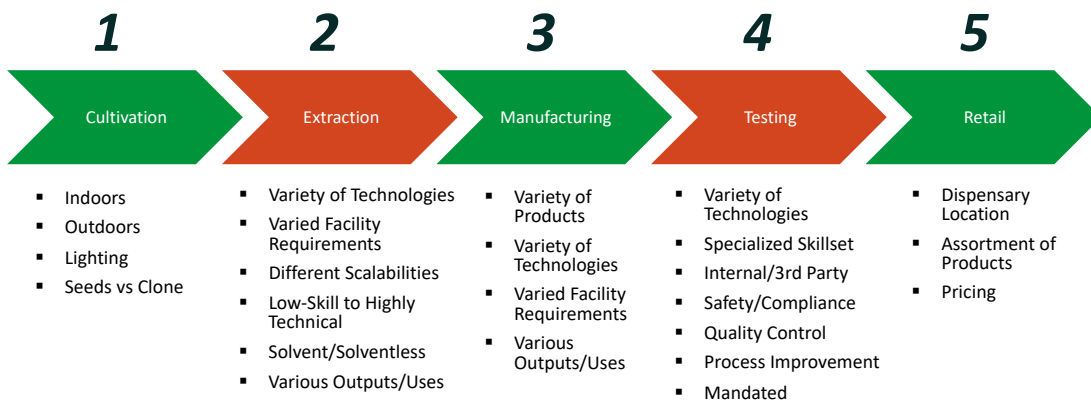
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The Legal Cannabis Supply Chain



The supply chain plays a significant role in the development of cannabis products and ultimately getting to the end user



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From our offices in Portland, Boston, and San Francisco, we help clients nationwide navigate the complex and evolving challenges of starting and operating a cannabis business.

Our management team includes seasoned business leaders with experience within and outside of the cannabis industry. Together, we provide the knowledge and resources you need to reach your business goals and stay in compliance with state laws.

Whether you're just getting started and need help with your application, SOP documents, financial modeling, etc., or you're looking to elevate the efficiency of your existing business with the help of an outsourced professional who knows the industry, we're here to help.



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History and Business Cases

NORTHEAST BANKRUPTCY CONFERENCE & CONSUMER FORUM
JULY, 2022

Historically Dismissed

- ▶ As the cases that follow indicate, cannabis-related bankruptcy cases have historically been dismissed (even if company filing for chapter 11 is/was not directly involved in the cannabis industry)

In re Rent-Rite Super Kegs

- ▶ 484 B.R. 799 (Bankr. D. Colo. 2012)
- ▶ Creditor moved to dismiss chapter 11 case filed by Colorado debtor (a warehouse owner) that derived roughly 25% of its revenues from leasing warehouse space to tenants who, to debtor's knowledge, were engaged in business of growing marijuana, arguing that the case should be dismissed (i) under the "clean hands doctrine" and / or (ii) for being filed in bad faith
- ▶ The bankruptcy court dismissed the case, finding it could dismiss on grounds that the debtor had both unclean hands and the case was filed in bad faith

In Re Rent-Rite Super Kegs (Con't)

- ▶ The court held debtor had "unclean hands" because it engaged in conduct that constituted a violation of federal criminal law and then sought equitable relief of the Bankruptcy Code. (Found dismissal was appropriate whether the Court applied the unclean hands as "cause" or as separate grounds for dismissal)
- ▶ The court held the plan was also unconfirmable for lack of good faith under §1129(a)(3) because a portion of the debtor's income was derived from an illegal activity

In re Medpoint Management, LLC

- ▶ 528 B.R. 178 (Bankr. D. Ariz. 2015)
- ▶ Medpoint Management, LLC ("Medpoint") was a dispensary-management entity. Medpoint's only source of revenue at the time of the petition was licensing fees from IP (specifically, the "Bloom" name and trademark) which Medpoint licensed to a dispensary and under which marijuana was sold. Medpoint also had limited other assets (lawsuit against former client dispensary and 100% interest in former dispensary manager)

In re Medpoint Management, LLC (Con't)

- ▶ Creditors, comprised of consultants and lenders of Medpoint, filed an involuntary chapter 7 petition against Medpoint. Medpoint filed a Motion to Dismiss or for Abstention, arguing that (i) a bankruptcy trustee could not lawfully administer a bankruptcy estate's marijuana-related assets without violating the CSA, which constituted cause for dismissal under §707(a) and (ii) creditors' hands were unclean due to their involvement in a medical marijuana enterprise

In re Medpoint Management, LLC (Con't)

- ▶ The court granted Medpoint's motion and dismissed the petition holding that: (i) granting the petition would result in chapter 7 trustee necessarily violating federal law, and the dual risks of forfeiture of Medpoint's assets and a trustee's inevitable violation of the CSA in administration of the estate constituted cause to dismiss, (ii) creditors had unclean hands in that they knowingly assisted with and profited from marijuana-related business and so they could not now seek relief from the bankruptcy court
- ▶ However, the Court held the creditors did *not* file petition in bad faith (“[n]ot every failed reason for filing an involuntary petition amounts to ‘bad faith.’”)

In re CWNevada LLC

- ▶ 602 B.R. 717 (Bankr. D. Nev. 2019)
- ▶ Decision dismissing cannabis cultivator and dispensary case filed after receivership commenced but acknowledging that CBD business may no longer be prohibited from using Chapter 11 after enactment of Farm Improvements Action of 2018 (Farm Bill)
- ▶ Creditor filed dismissal motion, which numerous other parties joined, seeking dismissal of the Chapter 11 case based on Section 305(a)(1), or Section 1112(b)

In re CW Nevada (Con't)

- ▶ Court noted that in chapter 7, 11, and 13 cases, the common thread was that cases were not automatically dismissed for mere involvement of marijuana related assets, and in chapter 11 and 13 cases, bankruptcy courts consider whether a debtor could propose a feasible plan that did not rely on income received through a violation of the CSA
- ▶ Court noted further that "there may be cases where Chapter 11 relief is appropriate for an individual or a non-individual entity directly engaged in a marijuana-related business
- ▶ Ultimately dismissed the case pursuant to §305(a)(1) for unrelated reasons

Garvin v. Cook Invs. NW, SPNWY, LLC

- ▶ 922 F.3d 1031 (9th Cir. 2019)
- ▶ One debtor (which derived revenues from leasing commercial real estate) leased premises to a company that used the property to grow marijuana
- ▶ UST's initial motion to dismiss for cause under §1112(b) denied because bankruptcy court determined debtors could possibly "propose a plan that does not rely on the income from the marijuana operation lease"

Garvin (Con't)

- ▶ Debtors' subsequently filed plan called for rejection of the marijuana-related lease and the plan was structured so that obligations would be paid without revenue from marijuana operations
- ▶ UST objected to confirmation on basis of section 1129(a)(3) because it was proposed by means forbidden by law (but not on lack of good faith). Bankruptcy court rejected UST argument and confirmed plan. District court affirmed.

Garvin (Con't)

- ▶ On appeal, the Trustee challenged the bankruptcy court's refusal to dismiss under §1112(b) for "gross mismanagement of the estate," but Ninth Circuit concluded argument was waived because not raised before bankruptcy court
- ▶ The Ninth Circuit, engaging in a textual analysis focusing on the language in the plain text of 1129(a)(3) which notes the plan has "not been proposed" by any means forbidden by law, upheld confirmation, concluding plain text of 1129(a)(3) directs bankruptcy court to "police the means of a reorganization plan's *proposal*, not its substantive provisions."

Garvin (Con't)

- ▶ In making this ruling, the Court disagreed with other courts, including the *Rent-Rite* court, which have held that dismissal was appropriate for bad faith where a significant portion of the debtors' income was derived from an illegal activity
- ▶ “[F]ocus is [] on the plan proponent's actions specifically related to the plan proposal process, rather than whatever actions might occur pursuant to the plan itself or the proponent's behavior during the bankruptcy case more generally.”

In re Basrah Custom Design, Inc.

- ▶ 600 B.R. 368 (Bankr. E.D. Mich. 2019)
- ▶ The debtor was listed as landlord, as agent of the owner, on a lease of property to a medical marijuana dispensary (“MJCC”). MJCC sued debtor and owner, among others, to enforce its right to purchase the land pursuant to the lease terms in state court. When the state court found for MJCC, the debtor filed its bankruptcy case
- ▶ The UST objected and filed a motion to dismiss the bankruptcy case for “cause” under §1112(b), alleging that the debtor pursued the bankruptcy case with unclean hands to enable its owner to profit from a marijuana business.

In re Basrah Custom Design (Con't)

- ▶ The Court dismissed the bankruptcy case, finding that the debtor had unclean hands and there was cause to dismiss pursuant to §1112(b)(1)
- ▶ The Court also held the debtor was collaterally estopped from denying that it wanted to continue to operate an illegal marijuana business due to a prior state court finding that the debtor intended to continue operating the business

In re Basrah Custom Design (Con't)

- ▶ Court distinguishes *Garvin* as being out of circuit and notes that it refused to decide the 1112(b) dismissal issue:
- ▶ “The decision of the Ninth Circuit Court of Appeals in *Garvin* is not binding on this Court, and, with respect, this Court does not necessarily agree with the *Garvin* court's holding about § 1129(a)(3). And, respectfully, one might reasonably question whether the *Garvin* court should have refused to decide the §1112(b) dismissal issue. That refusal, on waiver grounds, arguably is questionable, because it allowed the affirmance, by a federal court, of the confirmation of a Chapter 11 plan under which a debtor would continue to violate federal criminal law under the CSA.”

In re Way to Grow, Inc.

- ▶ 610 B.R. 338 (D. Colo. 2019)
- ▶ Another post-*Garvin* decision where District Court affirmed the dismissal of a seller of equipment, products and other material utilized in the manufacture of cannabis. In their first day motions debtors stated that future business expansion plan is tied to the growing cannabis industry which is heavily reliant on hydroponic gardening, but added that they do not own or do business with cannabis

In re Way to Grow, Inc. (Con't)

- ▶ Creditor filed motion to dismiss because the debtors' aided and abetted in violation of the CSA and dismissal was warranted pursuant to §1129(a)(3) because the plan was not proposed in good faith, given the debtors' tainted revenues and assets at risk of forfeiture
- ▶ The bankruptcy court found that the debtors could not sever ties with marijuana industry and remain in operation and therefore determined debtors were likely in violation of the CSA and dismissed the case on that basis, finding the violation to be cause under §1112(b)

In re Way to Grow, Inc. (Con't)

- ▶ The District Court affirmed and found that a Chapter 11 debtor cannot propose a good-faith reorganization plan that relies on knowingly profiting from the marijuana industry; which is cause for dismissal under §1112(b)
- ▶ District court further questioned the narrow interpretation given to 1129(a)(3) by the *Garvin* court

In re Way to Grow, Inc. (Con't)

- ▶ States that *Garvin* misreads the dismissal in *Rent-Rite* pursuant to 1129(a)(3) as being based upon the “and not by any means forbidden by law” language, when in reality the basis was good faith:
- ▶ “[I]t is frankly inconceivable that Congress could have ever intended that federal judicial officials could, in the course of adjudicating disputes under the Bankruptcy Code, approve a reorganization plan that relies on violations of federal criminal law.”

Individual and Consumer Cases

NORTHEAST BANKRUPTCY CONFERENCE & CONSUMER FORUM

JULY, 2022

Generally Not Permitted

- ▶ As the following cases demonstrate, marijuana-related consumer bankruptcy cases fare no better than business cases
- ▶ That being said, as with *Garvin*, the BAP in *In re Olson* signaled that perhaps not all marijuana-related bankruptcy cases should be dismissed, depending on the specific factual circumstances and findings at play

In re McGinnis

- ▶ 453 B.R. 770 (Bankr. D. Or. 2011)
- ▶ Chapter 13 debtor proposed a plan funded by, inter alia, medical marijuana growing operations. Debtor also owned an LLC which collected rents from other growers
- ▶ Court held that absent the growing operations, which violated the CSA and could not be relied upon, the Court could not find that the plan is reasonably certain to produce sufficient income to fund the plan and denied confirmation
- ▶ Court held that if the debtor proposed an amended chapter 13 plan that did not rely on income streams that violate the CSA, the court would confirm the plan

In re Arenas

- ▶ 535 B.R. 845 (Bankr. B.A.P. 10th Cir. 2015)
- ▶ The debtors jointly owned a commercial building in Denver that consisted of two units, which were used to grow and sell marijuana by the debtors (the second unit was leased to a dispensary). Most of the debtors' income stemmed from rental income of the units and the debtors' marijuana business. Their nonexempt assets were 25 marijuana plants and the building
- ▶ The debtors filed a Chapter 7 petition that they later attempted to convert to Chapter 13. UST asked that the case be dismissed, alleging that it would be impossible for a chapter 7 trustee to administer the assets without violating federal law.

In re Arenas (Con't)

- ▶ The bankruptcy court denied the debtors' motion to convert their Chapter 7 case to Chapter 13, and concluded that the debtors could not receive Chapter 7 relief because engaging in federal criminal conduct demonstrated a lack of good faith that would bar confirmation of their Chapter 13 plan and was cause to dismiss their Chapter 7 case, too
- ▶ On appeal, this BAP, reviewing the order for abuse of discretion, (reviewing findings of fact for clear error and conclusions of law *de novo*), affirmed.

In re Arenas (Con't)

- ▶ The BAP found: a finding of lack of good faith is entitled to highest level of deference, (ii) finding was based on the fact that the plan was likely not feasible due to, among other factors, the debtors' lack of income to fund the plan even with the rental income from the dispensary, and not just the fact that marijuana is involved and (iii) if debtors are incapable of proposing a confirmable plan, the plan is proposed in bad faith
- ▶ In addition, the BAP found the inability to lawfully administer the estate constituted cause for dismissal under §707(a)

In re Johnson

- ▶ 532 B.R. 53 (Bankr. W.D. Mich. 2015)
- ▶ Chapter 13 debtor derived almost half of his income from growing and selling marijuana and UST sought dismissal of the case
- ▶ Court found the debtor's business to be "patently incompatible with a bankruptcy proceeding" but ordered that the debtor may cease operating his marijuana business if he wanted to stay in bankruptcy

In re Olson

- ▶ 2018 WL 989263, **4-6 (B.A.P. 9th Cir. Feb. 5, 2018)
- ▶ Bankruptcy court dismissed case *sua sponte* concluding chapter 13 debtor was in violation of federal law for leasing property to, and collecting post-petition rent from, a cannabis company, which was operating legally under applicable California law. In dismissing, bankruptcy court was not persuaded by debtor's attempts to distance herself from the cannabis business, having ceased to take rent from the dispensary and moving to reject the lease

In re Olson (Con't)

- ▶ The BAP vacated dismissal and remanded for further findings on the specific criminal activity and the legal standard for dismissing the case under §1307(c). The BAP first noted the bankruptcy court did not make a finding of "cause" sufficient under the statute, i.e. that proceeds from an illegal business were needed to fund the plan, or that the trustee would need to administer funds from illegal activities
- ▶ BAP also focused on the specific "knowledge" requirement that the CSA imposed for prohibiting leasing space to a cannabis business, noting the debtor was nearly blind, elderly, residing in a nursing home and relying on others to operate her business

In re Olson (Con't)

- ▶ In ordering this case be remanded, the BAP signaled that perhaps not all cannabis-related companies are necessarily excluded from federal bankruptcy protection. Rather than adopting a rigid approach, the BAP indicated that in the Ninth Circuit, a court would need to make specific findings to justify dismissal.

In re Burton

- ▶ 610 B.R. 633 (B.A.P. 9th Cir. 2020)
- ▶ Dismissal of case affirmed where individual chapter 13 debtors owned the majority interest in an entity that cultivated and sold marijuana
- ▶ Debtors opposed UST on dismissal, because the entity was defunct and not being used to fund their plan. However, the entity was engaged in two state court lawsuits seeking recovery for breaches of contract related to its former business operations

In re Burton (Con't)

- ▶ BAP affirmed dismissal because recovery of assets would violate the CSA and because if recovery was successful, then Chapter 13 trustee would have to administer assets connected to illegal activity. The court was not persuaded by the debtors' argument that they were unlikely to recover any proceeds in the lawsuits

In re Malul

- ▶ 614 B.R. 699 (Bankr. D. Colo. 2020)
- ▶ Court vacated order to reopen Chapter 7 case, where claims tied to recovery of medical marijuana contract claims would need to be administered. Chapter 7 trustee sought to approve a settlement which would have provided the estate a lump sum made "with traceable funds that do not originate from a marijuana enterprise"
- ▶ UST objected to both the settlement and reopening the case, arguing that administration of the estate would require Chapter 7 trustee to engage in illegal activity by seeking "to recover the debtor's investment in a marijuana business from a related marijuana business or alter ego of the marijuana business"

In re Malul (Con't)

- ▶ Court noted of the marijuana-related bankruptcy landscape: "If the uncertainty of outcomes in marijuana-related bankruptcy cases were an opera, Congress, not the judiciary, would be the fat lady. ... The Court may enjoy the opera, but anxiously awaits the fat lady's song"
- ▶ Court held "mere possession of those rights and interests, and certainly her prosecution of litigation claims in furtherance of those rights and interests, constitute ongoing criminal violations of the CSA," and declined to reopen the case to administer the asset

In re Mayer

- ▶ 2022 Bankr. LEXIS 256 (Bankr. D. Ariz. Jan. 31, 2022)
- ▶ Chapter 13 debtor's sole source of income was from a corporation that manufactured and sold extraction presses to make organic concentrates "primarily" used to extract and process marijuana resin
- ▶ Court held that Debtor's only reliable assets which could support a feasible Chapter 13 plan are derived from ongoing CSA violation. Court further rejected Debtor's proposal to fund his plan from other non-CSA violative sources because Debtor could not show that these sources (another corporation and an expected inheritance) were viable

Concluding Thoughts

- ▶ While *Garvin* and *Olson* seem to indicate movement in the Ninth Circuit away from the stricter precedent refusing Title 11 relief to any debtor with ties to the cannabis industry, they have not had widespread impact outside of the Ninth Circuit
- ▶ Within the Ninth Circuit, there is no *per se* rule forbidding debtors with ties to the marijuana industry from utilizing Title 11. However, it seems unlikely that these opinions could be relied upon as an affirmative mechanism for a marijuana business (as opposed to a business that merely has ties to cannabis industry) that seeks to continue to operate its prepetition operations

Chapter 15 Slides

NORTHEAST BANKRUPTCY CONFERENCE & CONSUMER FORUM
JULY, 2022

What is Chapter 15?

- ▶ Chapter 15 of the Bankruptcy Code offers bankruptcy protection within the United States to debtors that are subject to an insolvency proceeding in another country, in order to provide comity with foreign courts and foreign bankruptcy proceedings

Is Chapter 15 Available for Cannabis Entities?

- ▶ As discussed previously, the typical challenge to a chapter 11 proceeding initiated by a cannabis company is to dismiss the chapter 11 because the plan is in "bad faith" or proposed by means forbidden by law, pursuant to § 1129(a)(3). In the chapter 15 context, a cannabis debtor may face similar challenges pursuant to the public policy exception, codified in § 1506.
- ▶ § 1506 states: "Nothing in this chapter prevents the court from refusing to take an action governed by this chapter if the action would be manifestly contrary to the public policy of the United States"

Is Chapter 15 Available for Cannabis Entities?

- ▶ Chapter 15 codifies the Model Law on Cross-Border Insolvency in substantially the same way it was written by the United Nations Commission on International Trade Law ("**UNCITRAL**"). The Guide to Enactment of the Model Law (the "**Guide**") published by UNCITRAL outlines the meaning and purpose of the provisions that are embodied in chapter 15.

Is Chapter 15 Available for Cannabis Entities?

- ▶ There, UNCITRAL explains “the purpose of the expression ‘manifestly,’ used also in many other international legal texts as a qualifier of the expression ‘public policy,’ is to emphasize that public policy exceptions should be interpreted restrictively and that [the public policy exception] is only intended to be invoked under exception circumstances concerning matters of fundamental importance for the enacting State.”
- ▶ The Guide provides that these fundamental policies would need to implicate some constitutional guarantees

Is Chapter 15 Available for Cannabis Entities?

- ▶ Indeed, the House Report accords with this interpretation, stating that § 1506 follows the Model Law exactly, and has been narrowly interpreted on a consistent basis in courts around the world. Additionally, the House Report specifically indicated the Guide “should be consulted for guidance as to the meaning and purpose of [chapter 15’s] provisions.” The House Report further notes that international usage of the word “manifestly” restricts the public policy exception to the most fundamental policies of the United States

Interpretation of § 1506

- ▶ “Fundamental policies” is not defined in the Code
- ▶ Courts have adhered to two principles in determining whether a fundamental policy is at risk:
 - ▶ “[d]eference to a foreign proceeding should not be afforded in a [c]hapter 15 proceeding where the procedural fairness of the foreign proceeding is in doubt or cannot be cured by the adoption of additional protections”; and
 - ▶ “[a]n action should not be taken in a [c]hapter 15 proceeding where such action would frustrate a U.S. court’s ability to administer the [c]hapter 15 proceeding and/or would impinge severely a U.S. constitutional or statutory right.” 480 B.R.

Cases Finding Violations of § 1506

- ▶ *In re Toft*, 453 B.R. 186, 198 (Bankr. S.D.N.Y. 2011)
- ▶ Insolvency administrator (trustee) of German debtor initiated a chapter 15 proceeding in order to gain access to debtor’s email accounts stored in the United States and for an order in effect granting him a wiretap on debtor’s future emails
- ▶ Prior to filing a motion with the Bankruptcy Court, the insolvency administrator sought and received German and English court (where debtor relocated) orders granting the above relief

In re Toft (Con't)

- ▶ The Bankruptcy Court noted that while comity is generally available for German and English proceedings, the Electronic Communications Privacy Act would require notice to the debtor for such acts, and the wiretap would be illegal under the Wiretap Act. As such, the Court found against the insolvency administrator, saying it was a "rare case" where § 1506 applies
- ▶ The Court noted that foreign procedures are not routinely imported into U.S. law and disclosure must be in accordance with U.S. practices and principles

In re Toft (Con't)

- ▶ The relief sought was denied for several reasons: (1) the relief is banned under U.S. law and would seemingly result in criminal liability under the Wiretap Act and Privacy Act for those who carried it the terms of any US court order; (2) it would directly compromise privacy rights subject to a comprehensive scheme of statutory protection available to aliens; (3) the statute at issue invoked the protections of the Fourth Amendment as well as the constitutions of many States. As such, such relief would "impinge severely a U.S. Constitutional or statutory right."

In re Gold & Honey, Ltd.

- ▶ 410 B.R. 357, 372–373 (Bankr. E.D.N.Y. 2009)
- ▶ In a series of chapter 15 cases, Petitioners were appointed as receivers in Israel for debtors who had already commenced a chapter 11 case. Despite being in violation of the automatic stay already issued by the U.S. Bankruptcy Court in the chapter 11, Petitioners argued the Israel proceeding should be recognized as a main foreign proceeding under chapter 15

In re Gold & Honey (Con't)

- ▶ The Court denied this request because the receivership proceedings in Israel violated both the automatic stay and the Court's orders reinforcing that stay. The Court invoked § 1506 because such recognition would reward and legitimize the petitioner's violation of the stay and orders regarding the stay

Cases Finding No Violation of § 1506

- ▶ *In re Metcalfe & Mansfield Alt. Inv.*, 421 B.R. 685, 697 (Bankr. S.D.N.Y. 2010)
- ▶ Debtors in a Canada Companies' Creditors Arrangement Act ("**CCAA**") proceeding sought chapter 15 recognition of very broad third-party non-debtor release and injunction
- ▶ The Bankruptcy Court requested briefing on whether recognition of these releases under chapter 15 would be proper, as such releases would not be available in the Second Circuit in a chapter 11 proceeding

In re Metcalfe & Mansfield Alt. Inv. (Con't)

- ▶ After recognizing the CCAA as the foreign main proceeding, the court noted "chapter 15 specifically contemplates that the court will exercise its direction consistent with principles of comity." "The key determination required by this Court is whether the procedures used in Canada meet our fundamental standards of fairness."
- ▶ Citing the House Report, the Court held the Canadian releases are entitled to comity because Canadian bankruptcy law provides procedural fairness. "The relief granted in the foreign proceeding and the relief available in a U.S. proceeding need not be identical."

In re Ephedra Prods. Liab. Litig.

- ▶ 349 B.R. 333, 335-337 (Bankr. S.D.N.Y. 2006)
- ▶ Canadian debtors requested chapter 15 recognition of Canadian orders requiring mandatory meditation of personal injury and wrongful death claims. Four claimants objected to the relief on the grounds that it deprived claimants of the right to a jury trial under U.S. law
- ▶ In interpreting “manifestly contrary to the public policy of the United States,” the Court looked to a similar issue for guidance: determining when to enforce “foreign judgments rendered on the basis of foreign proceedings that were plainly fair but that did not include some commonplace of American practice.”

In re Ephedra Prods. Liab. Litig. (Con’t)

- ▶ Looking to Supreme Court precedent, the Court highlighted comity should be granted if “[the foreign] proceedings are according to the course of a civilized jurisprudence. *i.e.*, fair and impartial.” (citing *Hilton v. Guyot*, 159 U.S. 113, 159 (1985))
- ▶ After citing to other legal systems which do not allow jury trials in similar contexts, the court held claimants were afforded a fair and impartial proceeding and nothing more was required by § 1506 or any other law

In re Ephedra Prods. Liab. Litig. (Con't)

- ▶ Notably, this result came after the debtor and other interested parties negotiated a claims resolution procedure which was subsequently approved by order of the Ontario court. The debtors then moved for that order to be recognized in the U.S. The U.S. Bankruptcy Court requested certain procedural changes to “assure greater clarity and procedural fairness,” which were thereafter approved by the Ontario court

In re Rede Energia S.A.

- ▶ Ad Hoc Group raised several objections to chapter 15 recognition of Brazilian debtors' plan
- ▶ After rejecting these objections for various reasons, the Court noted, “[w]here, as here, the proceedings in the foreign court progressed according to the course of a civilized jurisprudence and where the procedures followed in the foreign jurisdiction meet our fundamental standards of fairness, there is no violation of public policy.”

§ 1506 Violation Cases Are Distinguishable

- ▶ *In re Toft*, the petitioners functionally sought a wiretap in contravention to several privacy-related statutes
- ▶ The distinctions between the relief sought in *In re Toft* and a cannabis-related bankruptcy are twofold:
 - ▶ First, the relief sought in *In re Toft* would be contrary to statutory rights provided in the U.S., where the Fourth Amendment underpins those statutory rights.
 - ▶ Second, depending on the relief being sought, it is not necessarily the case that the relief requested by a cannabis or cannabis-related business in a chapter 15 proceeding (i.e., enforcement of the automatic stay) would require the Debtor or other parties to engage in criminal activity to implement such an order.

§ 1506 Violation Cases Are Distinguishable

- ▶ Likewise, in *In re Gold & Honey*, the court was concerned that the foreign court had instituted a receivership proceeding in contradiction of an ongoing U.S. court proceeding and in violation of the automatic stay. The case is fact-specific and could be categorized in part as the court's reaction to the Israel court's failure to recognize the US proceeding

Concluding Thoughts

- ▶ While Chapter 15 has not yet been successfully tested in the context of a cannabis-related recognition proceeding, there are meritorious arguments that chapter 15's public policy exception is not implicated in a cannabis or cannabis-related bankruptcy proceeding because the rights to be protected are not "fundamental"

Faculty

Hon. Bruce A. Harwood is Chief U.S. Bankruptcy Judge for the District of New Hampshire in Concord, appointed to the bench in March 2013. He also serves on the First Circuit's Bankruptcy Appellate Panel. Prior to his appointment to the bench, Judge Harwood chaired the Bankruptcy, Insolvency and Creditors' Rights Group at Sheehan Phinney Bass + Green in Manchester, N.H., representing business debtors, asset-purchasers, secured and unsecured creditors, creditors' committees, trustees in bankruptcy, and insurance and banking regulators in connection with the rehabilitation and liquidation of insolvent insurers and trust companies. He was a chapter 7 panel trustee in the District of New Hampshire and mediated disputes arising in debtor/creditor relations. Judge Harwood serves on ABI's Board of Directors on its Communication, Information and Technology Committee. He served as co-chair of ABI's Commercial Fraud Committee, as program co-chair of (and presently as judicial advisor to) ABI's Northeast Bankruptcy Conference; and as Northeast Regional Chair of the ABI Endowment Fund's Development Committee. He also served on ABI's Civility Task Force. Judge Harwood is a Fellow in the American College of Bankruptcy and was consistently recognized in the bankruptcy law section of *The Best Lawyers in America*, in *New England SuperLawyers* and by *Chambers USA*. He received his B.A. from Northwestern University and his J.D. from Washington University School of Law.

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