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## PERSPECTIVE

# Ninth Circuit bars cannabis companies from pursuing RICO claims

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Doing business in California's legal cannabis industry remains a risky endeavor. The majority of the industry is still unlicensed, tax rates at the state and local levels are high (notwithstanding a recent reprieve from California's cultivation tax), and there are not enough licenses to meet geographic demand throughout the state. Outside financing remains difficult to secure for equipment, tenant improvements, account receivables and working capital because, under the federal Controlled Substances Act (CSA), cannabis remains a Schedule I narcotic.

To complicate things further, federal courts continue to struggle with the conflicts between federal and state laws regulating cannabis, including whether and when to let cannabis producers enforce their rights. In a recent decision, the Ninth Circuit took up whether a cannabis business victimized by fraud could assert a civil claim under the federal Racketeer Influenced and Corrupt Organizations (RICO) statute. While the court rejected such a claim, it left the door open to others that could be equally powerful.

In *Shulman v. Kaplan*, Case No. 20-56265 (Jan. 18, 2023), Francine



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Shulman, a California cannabis entrepreneur looking to expand her business, entered into a partnership with Todd Kaplan. She later claimed that Kaplan – who allegedly had a criminal record and a history of taking over small businesses through fraud – tried to do the same to Shulman's business, ultimately causing it to collapse. In response, she sued Kaplan in federal court, raising a RICO claim, among others.

The trial court dismissed the RICO claim, and the Ninth Circuit affirmed. As the Ninth Circuit ex-

plained, a plaintiff only has standing under RICO if her “business or property” was harmed by the defendant's illegal actions in violation of the RICO statute. But because use, cultivation, distribution, and sale of cannabis remain illegal under federal law, the court held that Congress did not intend “business or property” to include a cannabis-production company. Thus, Shulman – and anyone else operating a cannabis business – could not sue under RICO even if they were indeed the victim of fraud or other racketeering.

While the decision eliminated one potential tool for cannabis companies to protect themselves against predatory and unethical business practices, it was not a complete loss for the industry. The Ninth Circuit found that Shulman *could* have standing under Article III of the Constitution to sue in federal court for other claims relating to her cannabis business. For Article III standing, a plaintiff must show that the defendant caused her injury to a property interest that is recognized under state law –

in this case, that of California. Because California law does recognize cannabis-related property interests, cannabis company owners like Shulman can potentially sue in federal court for harm to their businesses (though not under RICO).

Even the inability to bring RICO claims may not be a major limitation for the cannabis industry, at least in California. Under the California Supreme Court's 2022 decision in *Siry Investment v. Farkahndepour*, California Penal Code Section 496(c) allows a business owner or partner who is harmed through fraud by her part-

ners or business associates to recover treble damages and attorney fees – the same remedies available under RICO. Many other states have their own versions of RICO. A cannabis industry plaintiff could assert such claims in fraud cases without running into the restrictions the Ninth Circuit imposed in *Shulman*.

While federal law continues to complicate cannabis businesses' legal status, they still have many tools to protect themselves from unscrupulous counterparts and other bad actors. When disputes arise, an understanding of those evolving options remains crucial.

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