### Agenda

<table>
<thead>
<tr>
<th>Time</th>
<th>Session</th>
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<tbody>
<tr>
<td>8:00 - 8:30 a.m.</td>
<td>Registration and Coffee</td>
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| 8:30 - 9:30 a.m.| **Session 1 - Welcome, Introduction, and Updates to Washington marijuana laws**  
|                 | Speakers: Joshua Ashby & Christopher Larsen, Ashby Law Group  
|                 | • Transportation Licenses  
|                 | • Out-of-State Financing  
|                 | • Merging of Medical Marijuana into Recreational |
| 9:30 - 10:15 a.m.| **Session 2 - Federal Marijuana Law and Policy Developments**  
|                 | Speaker: Sam Grosz, The Law Office of Samuel Grosz  
|                 | • DEA decision not to reschedule  
|                 | • Presidential Election  
|                 | • State legalization efforts  
|                 | • Border Crossing Issues |
| 10:15 - 10:30 a.m. | Break                                      |
| 10:30 - 11:00 a.m.| **Session 3 - Intellectual Property**  
|                 | Speaker: Neil Juneja, Gleam Law  
|                 | • Trademark (State and Federal)  
|                 | • Trade Secrets  
|                 | • Branding/Merchandising/Advertising |
| 11:00 - 12:00 p.m.| **Session 4 - Business Development**  
|                 | Speaker: Christine Masse, Miller Nash Graham & Dunn  
|                 | • Valuation  
|                 | • Investment/Finance  
|                 | • Use of Holding Companies |
| 12:00 - 1:00 p.m. | Lunch on your own                           |
1:00 - 2:00 p.m.  **Session 5 - Taxes and IRC §280E**  
Speaker: Dani Espinda, CPA, CGMA, ACT Resources PLLC  
- Cost of Goods Sold (COGS)  
- Form 8300  
- Local taxation

2:00 - 3:00 p.m.  **Session 6 - Rapid Fire Session – Specific Marijuana Concerns**  
- **Employment**: Compensation, Hiring, and Firing — Speaker: Rochelle Nelson, Fisher Phillips  
- **Land Use & Zoning**: Moratoriums; Nonconforming Use; Business Licensing; Landlord/Tenant issues — Speaker: Sean Badgley, C3 Law Group  
- **Banking**: Local Options; Issues with National Banks — Speaker: Eric Camm, Apex Law Group

3:00 - 3:15 p.m. Break

3:15 - 4:00 p.m.  **Session 7 - Litigation**  
Speaker: Ryan Espegard, Gordon Thomas Honeywell  
- Fate of early marijuana litigants  
- Issues and procedure for municipal & administrative appeals and related litigation  
- Business and real property disputes

4:00 - 5:00 p.m.  **Session 8 - Ethics**  
Speaker: Joshua Ashby, Ashby Law Group  
- Advising marijuana clients  
- Potential for conflict
Faculty Biographies

Program Chairs

Joshua Ashby, Ashby Law Group
Joshua began working with his first startup in 1997 and has successfully assisted many more start-up and established companies since then. He has experience negotiating manufacture and wholesale agreements from Europe to South America, and previously lived in East Asia. Joshua graduated summa cum laude from Embry-Riddle Aeronautical University and worked for a U.S. Congressman before going to law school. Joshua earned his J.D. from Seattle University School of Law, where he studied administrative, regulatory, tax, business, and international law. As an attorney, Joshua's practice focuses on business strategy and corporate planning.

Christopher Larsen, Ashby Law Group
Chris joined Ashby Law Group PLLC in 2014. His practice primarily focuses on representing businesses in highly regulated industries with their transactional, regulatory, and compliance needs. He has extensive experience facilitating transactions and communicating the needs of his clients to state administrative agencies. Chris also has worked closely with local county governments and advocated for his clients on various land use issues.

Chris is a Washington native and earned his J.D. from Seattle University School of Law, where he studied corporate governance and intellectual property law. As the Editor in Chief of the Seattle Journal of Environmental Law, he led the publication through final accreditation and established its Westlaw presence. Before joining Ashby Law, Chris assisted Pacific NW companies with business planning, compliance, and investigation in highly regulated industries, such as unlawful detainers, process service, and government permitting.

Presenters

Sean Badgley, C3 Law Group
Sean Badgley is an attorney working exclusively with Washington's emerging cannabis industry. A Colorado native, Sean holds an undergraduate degree in business economics from the University of Colorado. Sean graduated from Seattle University's School of Law and fell in love with the Pacific Northwest along the way. Since his admission the Washington Bar, Sean has repeatedly and successfully represented clients against the Washington Liquor and Cannabis Board. When Sean is not fighting government overreach in the field of recreational cannabis, Sean works on I-502 compliant corporate governance and is a successful litigator.

Eric Camm, Apex Law Group
Eric is an experienced attorney with a broad array of corporate governance, commercial transaction, and dispute resolution experience. He focuses his practice working with early stage to medium size businesses, identifying corporate governance and other liability issues before they arise.

Eric has acted as general counsel to numerous closely held private companies, non-profit corporations, and small cap public companies. His experience includes corporate governance, formation, public disclosure requirements, creditor/debtor issues, employment matters, nonprofit and foundation issues,
and IP protection. He has drafted numerous contracts, employment agreements, license agreements, merger agreements, commercial leases, promissory notes, debt restructuring instruments, settlement agreements, and public filings for his clients. Eric has also assisted public and private clients, including port districts, private companies, individuals, investment LLCs and startup ventures with dispute resolution, utilizing negotiation, alternate dispute resolutions such as arbitration and mediation and of course, civil litigation.

**Ryan Espegard, Gordon Thomas Honeywell**

Ryan joined GTH in 2012, where his primary areas of practice now include litigation, administrative regulations, and land use law. Ryan’s litigation experience spans a broad range of legal issues, but is frequently focused on products liability, land use, real estate, and business disputes. He is also breaking ground in the emerging area of cannabis business and regulation law, advising his clients as they develop some of the first legal marijuana businesses in the country. Ryan moved to the Northwest to attend Seattle University School of Law in 2006 after growing up in the Midwest and obtaining a bachelor’s degree in economics at the University of Wisconsin-Madison.

**Dani Espinda (CPA), Rhodes & Associates**

Dani is a principal at ACT Resources, PLLC and Tax Manager and Cannabis Business Consultant at Rhodes & Associates, PLLC in Federal Way with 16 years public accounting experience. She is a graduate of Central Washington University with a Bachelor of Science degree in Accounting and has been a licensed CPA since 2002. Dani specializes in tax compliance and planning for individuals, partnerships, corporations, estates and trusts as well as financial accounting and reporting and QuickBooks consulting. She has experience in various industries including manufacturing, real estate, personal services and construction but her primary focus these days is medical and recreational cannabis tax and business consulting for clients in multiple states. Dani has presented to the WSCPA, WAATP, MJBA, Cannabis Women’s Alliance and CannaCon 2016 in WA and AK as well as conducted several marijuana business and tax workshops for her clients in the industry.

**Samuel Grosz, The Law Office of Samuel Grosz**

Samuel Grosz is an attorney practicing in West Linn, Oregon where he focuses on general business law and tax issues facing cannabis businesses. He was an advisor to the supporters of Measure 91, which legalized recreational marijuana in Oregon. After its passage, he worked with the Oregon Liquor Control Commission to create administrative rules for Measure 91. He has lobbied for the marijuana industry at both the state and federal level.

Mr. Grosz holds an LL.M. in Taxation from Georgetown University and earned his law degree cum laude from Seattle University. He holds a B.A. from Portland State University in finance and marketing with a minor in Russian language. Also, he earned a Graduate Certificate in Real Estate Development from Portland State University. Mr. Grosz volunteers his time at Legal Aid Services of Oregon by assisting low-income taxpayers. He serves on the Oregon State Bar’s Tax Section, Laws Committee and on the Multnomah Bar Association’s Young Lawyers CLE Committee. He is an avid sailor and enjoys traveling abroad.

**Neil Juneja, Gleam Law**

Neil Juneja is the founder of Gleam Law, a cannabis-focused law firm with offices in Seattle, Washington and Portland, Oregon and is a licensed patent attorney. The majority of his practice focuses on trademark protection of cannabis brands in state and federal law. In addition, Neil has written numerous article on cannabis law and intellectual property as well as spoken at many events including in the
National Mall in Washington DC and at the Seattle Hempfest. Some of Gleam Law's notable clients include the first Seattle recreational marijuana retailer, several world-famous musicians branding cannabis products, and many publicly traded companies working in the cannabis industry. Neil has also been in Newsweek, Time Magazine, and on several documentaries for his work in the cannabis legal industry.

Christine Masse, Miller Nash Graham & Dunn
Christine M. Masse, a partner, is the leader of Miller Nash Graham & Dunn's government and regulatory affairs practice group and specializes in representing businesses in highly regulated industries with their transactional, regulatory, and public policy needs. Chris also leads the firm's tribal team, providing counsel to various Northwest Native American tribes and organizations on gaming, regulatory, real property, construction, financing, tax, liquor, marijuana, and economic development issues. Chris maintains a practice before the Washington State Gambling Commission relating to licensing issues and the approval and ongoing regulatory oversight of casino properties and before the Washington State Liquor and Cannabis Board on liquor and marijuana matters. She is a registered lobbyist in Washington State and has successfully lobbied for the passage of legislation in various areas. Before joining the firm, Chris was a judicial extern for the Honorable Thomas S. Zilly, U.S. District Court, Seattle, Washington, and clerked for the Department of Justice, U.S. Attorney, in Springfield, Illinois. Chris received her law degree, with honors, from the University of Washington School of Law. She earned her bachelor's degree in business administration, magna cum laude, at the University of Illinois.

Rochelle Nelson, Fisher Phillips
Rochelle Nelson is an attorney in Fisher Phillips’ Seattle office. Her practice covers all aspects of employment law, including wage and hour, employee drug-testing, and disability accommodations. Rochelle and her colleagues counsel cannabis retailers, growers, and other supporting industries with operations in California, Colorado, Oregon, and Washington on both state and federal employment law issues. She has presented on employment related topics for cannabis businesses and enjoys assisting emerging operations master the basics of employment laws to avoid litigation.
4th Annual NW Marijuana Law Conference

Washington Marijuana Industry at a Glance

• Initiative 502 passed in 2012 (55.7% approval)

• RCW 69.50 (Uniform Controlled Substances Act)
  • Washington State Liquor and Cannabis Board to adopt and establish rules

• RCW 69.51A (Medical Cannabis)

• Chapter 314-55 WAC (Marijuana Licenses, Application, Requirements, and Reporting)

• Liquor and Cannabis Board Policies (e.g., single producer license)
Marijuana Licenses

- **Producer**: grow, harvest, trim, dry, cure, and package into lots for *wholesale to producer or processor licensees*

- **Processor**: process, dry, cure, package, and label usable marijuana, concentrates, and infused products for *wholesale to processors and retailers*

- **Retailer**: sell usable marijuana, concentrates, infused products, and paraphernalia at *retail to consumers 21 years of age and older*

Marijuana Licenses (Continued)

- **Transportation (2016)**: physically transport or deliver marijuana, concentrates, and infused products between licensed marijuana businesses

- **Research (2016)**: produce, process, and possess marijuana for limited research purposes
License Qualifications

• 6 month WA residency

• Financial and Criminal Investigation

• 21 years of age

• Current on all tax obligations to WA DOR and other state agencies

• 1 Producer and 3 processor licenses OR 3 retail licenses

Who is a True Party of Interest?

• Owners and Spouses
  • Piercing the veil through to all individuals—including multilevel ownership structures

• Rights to Profits
  • Entity/Person who is in receipt of or has a right to receive a percentage of profits

• Exercise of Control
  • Entity/Person who exercises control over the licensed business in exchange for money or expertise
Who is not a True Party of Interest

• Landlords receiving reasonable payment for rent on a fixed basis under a bona fide lease
  • Landlord cannot exercise control over business or participate in management
• Employees who receive a bonus if:
  • Employee was on a fixed wage or salary and bonus is not more than 25% of employee’s pre-bonus annual compensation
  • Bonus is based on a written incentive/bonus program that is not out of the ordinary for the services rendered
• Person/Entity contracting with applicant to sell the property, unless contract holder exercises control over or participates in management of licensed business

Additional Regulations

• Location
• Traceability
• Security
• Extraction
• Packaging/Labeling
• Product Compliance
• Advertising
• Signage/Notices
• Pesticide/Fertilizer Use
• Quality Assurance Testing
• Sampling
• Waste Destruction and Disposal
• Transportation
• Recordkeeping
Marijuana Producer License

- Statewide Canopy TBD, but University of Washington and Law Policy Project (CLPP) determined 10M ft² of canopy is sufficient for Washington’s marijuana market (medical and recreational)
  - 12M+ sq. ft. licensed to date with additional producers still being licensed
- Three Categories:
  - Tier 1 – Less than two thousand ft²
  - Tier 2 – Two thousand ft² to ten thousand ft²
  - Tier 3 – Ten thousand ft² to thirty thousand ft²
- WSLCB reserves right to reduce all licensee’s production by the same percentage (e.g., prior 30% cap)

Marijuana Processor License

- WSLCB must approve all labeling and packaging for all marijuana-infused products
  - Licensee can request administrative hearing if denied
- Solid Infused Edibles:
  - Childproof individually packaged servings
  - Label must display number of servings in package
  - Homogenized
  - “This Product Contains Marijuana”
- Liquid Infused Edibles
  - Must include measuring device if multiple servings
  - Label must display number of servings in package
  - Homogenized
  - “This Product Contains Marijuana”
Marijuana Processor License (Continued)

- Marijuana-infused products must not:
  - Require cooking or baking; or
  - Be especially appealing to children
- Food items that may not be infused with marijuana to be sold at retails include: fruit/vegetable juices, butters, pumpkin/custard or egg containing pies, dairy products, and dried/cured meats
- Recipes for all marijuana-infused meant for oral ingestion must be kept on file at the licensed premises and made available to the WSLCB for inspection
- Department of Health and Department of Agriculture inspection of food processing facilities

Marijuana Retailer License

- Allowed to sell only usable marijuana, marijuana concentrates, marijuana-infused products, and marijuana paraphernalia
- No internet sales or delivery of product to customers
- Sale of marijuana products must not be below acquisition cost
- Allowed four months of average inventory on hand at any given time
Marijuana Retailer License (Continued)

• Allowed to transport product to other locations operated by licensee or to return product to processor

• May accept returns of open products with original packaging

• No consumption of marijuana or open containers permitted at retail outlet—exception for sample jar with mesh screen
  • Employees must not sample products on-site

• May dispose of marijuana product after providing 72 hours notice to WSLCB (2016)

Advertising

• Marijuana advertising and labels must not contain a statement or illustration that is:
  • False or misleading;
  • Promotes over consumption;
  • Represents the use of marijuana has curative or therapeutic effects; or
  • Is especially appealing to children

• No marijuana licensee shall place or cause to be placed an advertisement for marijuana in any form or through any medium:
  • Within 1,000 feet of a school, playground, recreation center or facility, child care center, public park, library, or game arcade not restricted to persons over 21;
  • On or in public transit or public transit shelter; or
  • On or in publicly owned or operated property
Advertising (Continued)

• Promotional Activity is heavily regulated:
  • No giveaways, coupons, or distribution of branded or unbranded merchandise

• Advertising Warnings:
  • “This product has intoxicating effects and may be habit forming.”;
  • “Marijuana can impair concentration, coordination, and judgment. Do not operate a vehicle or machinery under the influence of this drug.”;
  • “There may be health risks associated with consumption of this product.”;
  • “For use only by adults twenty-one and older. Keep out of the reach of children.”

Prohibited Practices

• Conditional Sales (bundling)
• Agreements between “industry member” or retailer resulting in undue influence
  • Industry Member means a licensed marijuana producer, marijuana processor, marijuana retailer, their authorized representatives, and any affiliates, subsidiaries, officers, partners, financiers, agents, employees, and representatives of any industry member.
• No marijuana producer or processor shall advance and no marijuana licensee shall receive money or moneys’ worth under an agreement written or unwritten or by means of any other business practice or arrangement such as:
  • Gifts, discounts, loans of money, premiums, rebates, free product of any kind, treats or services of any nature
2016 Updates: Out-of-State Financing

• What is a Financier?

• Removal of residency requirement for “Financier”

• Big Marijuana?

“Financier”
means any person or entity, other than a banking institution, that has made or will make an investment in the licensed business. A financier can be a person or entity that provides money as a gift, loans money to the applicant/business and expects to be paid back the amount of the loan with or without interest, or expects any percentage of the profits from the business in exchange for a loan or expertise.

True Party of Interest – Profits
Any entity or person who is in receipt of, or has the right to receive, a percentage of the gross or net profit from the licensed business during any full or partial calendar or fiscal year.
2016 Updates: Medical Marijuana

- State-Run Patient Database
  - Voluntary, but required to receive recognition card and benefits
- Authorization + Recognition Card
  - Purchase 3x legal limit of non-medical customer
  - Access to products with higher THC concentration (30% vs. 10%)
  - Sales tax exempt
  - Home grow 6-15 plants at residence
  - Arrest protection—no longer a mere affirmative defense
  - Participate in Cooperative
- Authorization Only
  - Possession equal to recreational limits
  - Home grow 4 plants at residence

2016 Updates: Medical Marijuana

- Medical Marijuana Endorsement
  - Mandatory for all retail shops selling medical-grade marijuana
  - One employee on-site during all hours of operation trained to educate patients, enter patients into the database, and issue recognition cards.
  - Trained Employees are NOT medical providers—they may only assist and educate patients—they cannot provide medical advice, diagnose conditions, change current treatments, or open and use actual products when demonstrating how to use.
  - Medically endorsed stores must keep enough medical-grade product on hand to cover patient demand
- Increased Testing and Labeling requirements from Dept. of Health
  - General Use Compliant, High CBD, High THC
2016 Updates: Cooperatives

- Registration with WSLCB required
- Each patient must be authorized and hold a recognition card
- Patients must be 21+ years of age, can participate in only one cooperative, and may not grow plants elsewhere.
- Patients must provide assistance in growing plants—monetary contributions not sufficient
- Cooperatives may purchase plants from licensed producers
- No marijuana product of any kind may be provided to any person who is not a member of the cooperative

2016 Updates: Cooperatives

- Plants must only be grown in the cooperative, which must be the domicile of one member, obscured from public view, and only one cooperative per tax parcel
- Cooperative may not locate:
  - Within one mile of a marijuana retailer; or
  - In those areas already prohibited for licensed marijuana businesses
- Cooperatives may grow up to the amount allowed for each patient (no more than 60 plants in a cooperative and 72 ounces)
- Patients no longer participating must notify WSLCB within 15 days and new patient may not join until 60 days have passed
2016 Updates: WSLCB Response to MMJ

- New Retail Applications
  - Priority language and new applications accepted
  - Removal of state-wide cap on retail stores—increased cap per jurisdiction
  - Removal of requirement that a licensee could not exceed 33% of allowed licenses in any jurisdiction

- Statewide Plant Canopy
  - Removal of emergency rule setting state-wide canopy set at 8.5 million
  - New cap to be imposed at a later date but UW study suggests 10 million

- Additional Processor Licenses
  - Existing producer only licensees allowed to submit application to add marijuana processor license

2016 Updates: Producer License

- 2015 Washington State Cannabis Patient Protection Act (SSB 5052) required assessment of production needs to MMJ patients.

- 10M ft² sufficient and 12M+ ft² licensed to date (May 2016)

- 2nd and 3rd Producer licenses withdrawn and refunds issued

- Business assumptions for existing licensed producers
2016 Updates: Transportation License

- New Transportation License allows licensed common carrier to physically transport marijuana product between licensed marijuana businesses in WA
- Same qualification requirements for True Parties of Interest
- Prohibited from carrying or using a firearm
- Same transportation requirements, except allowed to use any assigned vehicle
  - Permitted to use any vehicle assigned for the purposes of transporting marijuana
  - Limited to vehicles under 10,000 lbs. GVW due to federal oversight

2016 Updates: Research License

- New Research License allows licensee to produce, process, and possess marijuana for limited research purposes
  - WSLCB’s Scientific Reviewer will review description of intended research project for compliance and provide continued review of any reports made by licensees
- Research licensee may only sell grown marijuana product to other research licensees
- Research licensees may contract with UW and WSU
2016 Updates: Marijuana Recalls

- Product Recalls:
  - Exempt market withdrawals (e.g., aesthetic or packaging)
  - Licensee-initiated recalls
  - WSLCB investigation initiated recalls
  - Board-directed recall
- Recall Plan (required for all licensees)
  - Designation of recall coordinator; procedures for identifying and isolating recalled product on-hand; procedures to retrieve and destroy product in the market; communication plan to notify those affected by recall

2016 Updates: Other rule changes

- Local Ordinances allowed to reduce 1,000’ buffer requirement
  - Not applicable to elementary and secondary schools, and playgrounds

- Pesticide Action Levels established
  - Previous zero tolerance action level “not workable”

- Electronic payment of marijuana excise tax now accepted
Any Questions?

Presented by:
Christopher Larsen
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Email: clarsen@ashbylawgroup.com
Federal Marijuana Law & Policy Development

November 4, 2016
4th Annual NW Marijuana Law Conference
Presenter: Samuel Grosz, Esq.

Outline

- DEA Decision not to Reschedule – *Any good news?*
- Presidential Election – *Does it really matter?*
- State Legalization Efforts – *Where are we?*
- Boarder Crossing – *Can I? Should I?*
What’s a schedule?
What’s the good news?

Rescheduling

What’s the DEA Schedule

- Controlled Substance Act (CSA), 21 USC §801 et seq.
  - Passed in 1970, establishing federal U.S. drug policy under which the manufacture, importation, possession, use and distribution of certain substances is regulated.
  - Implementing legislation for the Single Convention on Narcotic Drugs (more to come on this…)
  - Note – also has a schedule but different.

- The Schedule regulates “controlled substances” … “a drug or other substance, or immediate precursor, included in schedule I, II, III, IV, or V ….. The term does not include distilled spirits, wine, malt beverages, or tobacco….21 U.S.C. § 802(6)
Schedule I
21 USC §821

- Schedule I
  - (A) The drug or other substance has a high potential for abuse.
  - (B) The drug or other substance has no currently accepted medical use in treatment in the United States.
  - (C) There is a lack of accepted safety for use of the drug or other substance under medical supervision.

- No prescriptions may be written for Schedule I drugs.
- Examples: marijuana, heroin*, LSD, GHB, & ecstasy (MDMA).
  - *Heroin is merely morphine with a acetyl molecule attached allowing it to cross the blood-brain barrier quicker.

Schedule II
21 USC §821

- Schedule II
  - (A) The drug or other substance has a high potential for abuse.
  - (B) The drug or other substance has a currently accepted medical use in treatment in the United States or a currently accepted medical use with severe restrictions.
  - (C) Abuse of the drug or other substances may lead to severe psychological or physical dependence.

- Requires prescription
- Examples: cocaine, oxycodone, morphine, etc.
Schedule III
21 USC §821

- Schedule III
  - (A) The drug or other substance has a potential for abuse less than the drugs or other substances in schedules I and II.
  - (B) The drug or other substance has a currently accepted medical use in treatment in the United States.
  - (C) Abuse of the drug or other substance may lead to moderate or low physical dependence or high psychological dependence.

- Requires prescription

- Examples: Ketamine (Special K), 15mg > hydrocodone (Vicodin), codeine, etc.

Samuel Grosz, Esq. www.SamuelDavidLaw.com

Schedule IV
21 USC §821

- Schedule IV
  - (A) The drug or other substance has a low potential for abuse relative to the drugs or other substances in schedule III.
  - (B) The drug or other substance has a currently accepted medical use in treatment in the United States.
  - (C) Abuse of the drug or other substance may lead to limited physical dependence or psychological dependence relative to the drugs or other substances in schedule III.

- Requires prescription

- Examples: Xanax, Valium, Ambien, Tramadol, etc.

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Schedule V
21 USC §821

- Schedule V
  - (A) The drug or other substance has a **low potential for abuse relative to the drugs or other substances in schedule IV.**
  - (B) The drug or other substance **has a currently accepted medical use** in treatment in the United States.
  - (C) Abuse of the drug or other substance **may lead to limited physical dependence or psychological dependence** relative to the drugs or other substances in schedule IV.

- Requires prescription
- Examples: Robitussin (codeine – low dose)

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Reschedule v. De-schedule

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<tr>
<th>Reschedule</th>
<th>De-schedule</th>
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<tbody>
<tr>
<td>Require prescription</td>
<td>No prescription required</td>
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<tr>
<td>Dispensed via pharmacy or medical provider</td>
<td>Over-the-counter</td>
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<tr>
<td>Strict FDA oversight in production</td>
<td>Medical insurance coverage?</td>
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<tr>
<td>- Subject to FDA trials to bring to market</td>
<td>Less FDA oversight</td>
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<tr>
<td>Eligible for medical insurance coverage</td>
<td>Little if any effect to state marijuana laws</td>
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<tr>
<td>Large disruption to current state marijuana models</td>
<td>Allow access better access to FCC regulated media</td>
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<tr>
<td>Allow access better access to FCC regulated media</td>
<td>No 280E issue</td>
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<td>No 208E issue</td>
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Alternative

- Should the DEA create a new schedule for Marijuana?
  - Effectively legitimize and legalize state marijuana laws.

What happened in August?

- DEA was petitioned to consider rescheduling marijuana from Schedule I
  - Washington & Rhode Island Governors
    - Move to Schedule II
  - Private citizen
    - Move from Schedule I to ?

- Answer: NO
Why?

- DEA asserted that it could only be moved to Schedule II to comply with treaty obligations.
- Denial of Petition Factors, 21 USC §811(c)
  - The drug’s actual or relative potential for abuse;
  - The drug’s scientific evidence of its pharmacologic effect, if known;
  - The state of current scientific knowledge regarding the drug;
  - The drug’s history and current pattern of abuse;
  - The drug’s scope, duration, and significance of abuse;
  - The risk, if any, to public health;
  - The drug’s psychic or physiological dependence liability; and
  - Whether the drug is an immediate precursor of a controlled

Current Accepted Medical Use

- Factors:
  - The drug’s chemistry is known and reproducible;
  - There are adequate safety studies;
  - There are adequate and well-controlled studies proving efficacy;
  - The drug is accepted by qualified experts; and
  - The scientific evidence is widely available.

- DEA found NONE of the factors were met.
Research

- Last 2 years reg. researches increased from 161 to 354
- 90 researchers approved for CBD research on humans

The Good

- New policy statement to increase research on marijuana
- Streamline process to apply for research license
  - Unlikely for applicant to be able to participate in both state and federal research concurrently
- Note: Past illegal conduct will weigh heavily against an applicant
Presidential Election

Does it really matter?

Samuel Grosz, Esq. www.SamuelDavidLaw.com

Presidential Powers

- White House Policy Statements
  - “The Administration steadfastly opposes legalization of marijuana and other drugs because legalization would increase the availability and use of illicit drugs, and pose significant health and safety risks to all Americans, particularly young people.”
  - https://www.whitehouse.gov/ondcp/marijuanainfo
  - “As has been well documented, I smoked pot as a kid, and I view it as a bad habit and a vice, not very different from the cigarettes that I smoked as a young person up through a big chunk of my adult life. I don’t think it is more dangerous than alcohol.”
  - Obama http://www.newyorker.com/magazine/2014/01/27/going-the-distance-david-remnick

- Appointment Power, with the Senate
  - Attorney General, DOJ
  - Director of National Drug Control Policy “Drug Czar”
  - SCOTUS

Samuel Grosz, Esq. www.SamuelDavidLaw.com
Presidential Powers, cont.

- Non-enforcement
  - Cole Memo
- Re-scheduling 21 USC §811
  - Authority delegated to the Attorney General, working with the DEA and Secretary of HHS.
  - Decision must rely upon scientific evidence
  - 8 factor test
  - Adhere to treaties (The Single Convention)
- No easy route for President to legalize without congress.

Single Convention on Narcotic Drugs

- International treaty to prohibit production and supply of narcotic drugs and of drugs with similar effects except for specific purposes, such as medical treatment and research.
- Effective 1975, as of 2015 has 185 state parties, including U.S.
- Unclear whether criminalization of drug possession for personal use is required.
- Only covers the “flower”; not the leaves, Art. 1, s-para. 1(b), nor industrial hemp, Art. 28.
Single Convention, cont.

- Uruguay
  - Legalized marijuana in 2013
  - Condemned but no repercussions

- UNGASS – Special Session of Drugs, 2016
  - Punted the question of marijuana despite strong interest

- Remains an impediment to recreational marijuana

Trump

- “In terms of marijuana and legalization, I think that should be a state issue, state-by-state. … Marijuana is such a big thing. I think medical should happen — right? Don’t we agree? I think so. And then I really believe we should leave it up to the states.” Washington Post, October 29, 2015

- “I’d say [regulating marijuana] is bad. Medical marijuana is another thing, but I think it’s bad and I feel strongly about that. [Moderator: “What about the states’ right aspect of it?”] If they vote for it, they vote for it… But I think, medical marijuana, 100%.” C-SPAN, June 23, 2015

- “We’re losing badly the War on Drugs. You have to legalize drugs to win that war. You have to take the profit away from these drug czars.” Miami Herald, April 14, 1990
Clinton

- I think what the states are doing right now needs to be supported, and I absolutely support all the states that are moving toward medical marijuana, moving toward — absolutely — legalizing it for recreational use. What I’ve said is let’s take it off the what’s called Schedule I and put it on a lower schedule so that we can actually do research about it. There’s some great evidence about what marijuana can do for people who are in cancer treatment, who have other kind of chronic diseases, who are suffering from intense pain. There’s great, great anecdotal evidence but I want us to start doing the research. — Jimmy Kimmel Live, March 24, 2016

- “I think that states are the laboratories of democracy, and four states have already taken action to legalize, and it will be important that other states and the federal government take account of how that’s being done, what we learn from what they’re doing, I think that the states moving forward is appropriate and I think the federal government has to move to make this more available for research that they can then distribute to interested people across our country. I do think on the federal level we need to remove marijuana from the Schedule I of drugs, move it to Schedule II, which will permit it to be the basis for medical research because it’s important that we learn as much as possible. And since it was a Schedule I drug we haven’t done that research. A lot of experts in the field are telling me we’ve got to learn a lot more.” — WBZ NewsRadio, January 25, 2016

State Legalization Efforts

Where are we?
What’s on the ballots?
Where are we now? **Recreational**

- 4 states:
  - Alaska
  - Oregon
  - Washington
  - Colorado
- DC (not legal to buy).

Where are we now? **Medical**

- 25 states and DC with some form of legalization
- 174 million American live in states permitting some form of medical marijuana, over ½ the total population.
According to 2015 population estimates, marijuana reform results will affect roughly 82 million people, compared with the next most impactful initiative which is in healthcare and will affect 55 million people. (Approx. 25% of US population)

**Ballot - Medical**

- **Florida**
  - Amendment 2
  - Currently, low-THC non-smoked marijuana for patients
  - Allow for physicians to certify patients with some "other debilitating medical conditions of the same kind or class as or comparable to those enumerated."

- **Arkansas**
  - Two ballot measures – increases the chances of failure
  - Question 7 – Arkansas Supreme Court ruled (Oct. 27, 2016 – 2016 Ark. 359) 12,000 signatures invalid – so it won’t be on the ballot – but votes just not counted.
  - Question 6 – establish dispensaries and cultivation for patients with qualified medical conditions. Includes a tax provision.

- **North Dakota**
  - Initiated Statutory Measure 5 – requires patient cards certified by physicians for certain medical conditions.
  - Patients may petition to add to list of medical conditions.

- **(Montana)**
  - I-182 – Repeals Senate Bill 423 that limited dispensaries to 3 users and doctors to less than 25 patients per year
  - Effectively, restart the medical program enacted in 2004.
Ballot – Recreational

- **California**
  - Proposition 64 – 21 and over, create licensed on site-consumption, 6 plants home grow, 5 year prohibition on large scale grows, & 600 ft. from schools.
  - Taxes: $9.25 flower & $2.75 leaves per lbs. at cultivation, & 15% sales tax. Local taxes permitted.

- **Nevada**
  - Question 2 – 21 and over, 6 plants home grow, & 1,000 ft. from schools.
  - Taxes: 15% excise tax, annual license fees $3k - $30k
  - Quota for number of retail stores per county: Clark 80, most counties 2

- **Main**
  - Question 1 – 21 and over, 6 plants home grow, treated as agriculture product
  - Taxes: 10% sales tax

- **Massachusetts**
  - Question 4 – 21 and over, 6 plants home grow
  - Taxes: 3.75% excise tax & 2% local option.

---

Boarder Crossing

*Can I? Should I?*
Distribution
21 USC §841

• (a) Except as authorized by this subchapter, it shall be unlawful for any person knowingly or intentionally—
  • (1) to manufacture, distribute, or dispense, or possess with intent to manufacture, distribute, or dispense, a controlled substance;

Penalties - Federal Benefits
21 USC §862

• In ADDITION to sentence for offence,
  • Trafficking
    • 1st time – 5 yr, ineligible for federal benefits
    • 2nd time – 10yr.
    • 3rd time – permanently
  • Possession
    • 1st time – 1 yr, ineligible for federal benefits
    • 2nd time – up to 5 yr.
  • Federal Benefit
    • Includes: grant, contract, loan, professional license, or commercial license provided
    • Excludes: retirement, welfare, Social Security, health, disability, veterans benefit, public housing, or other similar benefit
  • NOTE: 21 USC §862a – denies federal funded state welfare and food stamps and benefits for conviction under state or federal law for possession or distribution
Cases

  • 201 months in prison
  • Member of a drug trafficking organization that distributed $16.9 million worth of marijuana
  • Purchased in California and sold in Kansas
  • Estimated to have distributed more than 8,000 lbs.

  • 5 yr. In prison
  • Stolen guns, 40lb. of marijuana
  • Conspiracy to distribute

Cases, Cont.

  • Sold marijuana in Michigan from 2009-2011, and growing.
  • Alleged importing from marijuana from Arizona
  • Michigan legalized medical marijuana in 2008
9th Cir.

- US v McIntosh
  - DOJ cannot spend money to prosecute people who violate federal drug laws but are in compliance with state medical marijuana laws.
  - Recreational only?
  - WA combined rec/med?
  - Congress could appropriate funds

State AG

- Nebraska AG “Nebraska has only one real choice, to uphold the law that exists for the protection of the public and the well-being of Nebraska’s families.”
Airports

- TSA Policy: TSA security officers do not search for marijuana or other drugs. In the event a substance that appears to be marijuana is observed during security screening, TSA will refer the matter to a law enforcement officer.

- Portland – PDX
  - Port authority will ensure compliance with local laws
  - Asked to leave the check point and come back in compliance
  - Allow travel on intra-state flights
  - [https://www2.portofportland.com/PDX/TravelTips](https://www2.portofportland.com/PDX/TravelTips)

- Seattle – SEA
  - Port of Seattle police said they’ve never confiscated pot or made a single marijuana arrest since it was legalized two-and-a-half years ago.

- Spokane - SIA
  - Will confiscate marijuana, due potential jeopardy of federal funding

Airports, Cont.

- Hawaii
  - HI Supreme Ct. found compliance with HI medical laws gives right to travel intra-state with marijuana
  - *Woodhall*, 301 P.3d at 611

- California – SFO
  - “allow card-holding medical marijuana patients to carry up to 8 oz. when traveling.”

- NOTE – once on a civil aircraft in possession of marijuana, in violation of federal law.
  - See, 21 USC §812.
Investment of Profits 21 USC §854

- (a) It shall be unlawful for any person who has received any income derived, directly or indirectly, from a violation of this subchapter … in which such person has participated as a principal …, to use or invest, directly or indirectly, any part of such income, or the proceeds of such income, in acquisition of any interest in, or the establishment or operation of, any enterprise which is engaged in, or the activities of which affect interstate or foreign commerce.

- (d) The provisions of this section shall be liberally construed to effectuate its remedial purposes.

Conclusions

- Increasing international discussions on historical decisions to criminalize marijuana
- Growing support at federal level for research on medical marijuana, irrespective of the next president
- Continued trend of states legalizing medical and recreational marijuana
- Increasing similarities in state laws and regulations
- Crossing state lines, don’t do it
  - Federal prosecution, if moving significant amounts
  - Airports follow local state rules, but don’t fly with it
Thank You!

Samuel Grosz, Esq.
Samuel David Law
Samuel@SamuelDavidLaw.com

Further Reading

- Controlled Substance Act (CSA)

- DEA Decision to Not Reschedule
  - https://fusiondotnet.files.wordpress.com/2013/12/press_release_191113e.pdf

- Expanded Research

- UN – Uruguay concern
  - https://fusiondotnet.files.wordpress.com/2013/12/press_release_191113e.pdf

- Trafficking
  - Proving Personal Use: the Admissibility of Evidence Negating Intent to Distribute Marijuana
    - http://repository.law.umich.edu/cgi/viewcontent.cgi?article=1218&context=mlr
Intellectual Property & The Cannabis Industry

Northwest Marijuana Law Conference
November 4, 2016

Neil Juneja
Gleam Law, PLLC

Trademark Law
Trademark Purpose

- Source Identifier
- Good Will
- Loyalty
- Reputation

- Trade names are NOT trademarks
- Domain names are NOT trademarks
What can the law protect

- Names
- Logos
- Trade dress
  - Product packaging
  - Interior/exterior design
  - Look and feel
- Color
- Smell
- Sound

“Likelihood of consumer confusion”

Sleekcraft factors (9th Circuit)

1. the strength of the mark;
2. the similarity of the marks;
3. the marketing channels used;
4. the proximity of the goods;
5. defendant’s intent in selecting its mark;
6. evidence of actual confusion;
7. the likelihood of expansion of the product lines
8. the type of goods and the degree of care likely to be exercised by the purchaser.

*Sleekcraft Boots*, 599 F.2d 341, 348 (9th Cir.1979).
Infringement

Test: Likelihood of consumer confusion

Strength

<table>
<thead>
<tr>
<th>Classification</th>
<th>Example</th>
<th>Weak</th>
<th>Strong</th>
</tr>
</thead>
<tbody>
<tr>
<td>Generic</td>
<td>Legal Weed</td>
<td>Not Distinctive</td>
<td>Inherently distinctive</td>
</tr>
<tr>
<td>Descriptive</td>
<td>Green Buds</td>
<td>Secondary meaning required</td>
<td></td>
</tr>
<tr>
<td>Suggestive</td>
<td>High-Flyer</td>
<td>Inherently distinctive</td>
<td></td>
</tr>
<tr>
<td>Arbitrary</td>
<td>Honu</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fanciful</td>
<td>Coined word – Kodak</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Protecting the Brand

Trademark Law

• Federal
• State
• Common Law

Federal trademark benefits

• Nationwide rights
• After 5 years of continuous use – incontestable
• ® can be used
• Trademark can lasts forever as long as continuous use in commerce
• Issues – must be used in interstate commerce
• Marijuana is considered scandalous and immoral
  • Prohibited by the Controlled Substances Act
State trademark

Oregon
- Unexamined

Washington
- Unexamined
- Issues with licensing - TPOI prevents variable royalties

California
- Examined
- No cannabis marks permitted

Colorado
- Unexamined
- Issues with sharing medical and recreational trademarks

Common Law

- Protection in the region of actual use in commerce
- Cannot expand into other’s territory
- Grandfathered-in with limitations
- Cannot expand beyond use
How to choose a great mark

• Don’t copy
• Be original
• Look for the strength of a trademark (distinctiveness)

Do Not:

• merely describe the product
• geographical descriptions
• Use your last name
  • Exception: McDonalds

• Appeal to kids – e.g. cartoon characters
Words not to use

Canna-
Mari-
THC
Sativa
Indica
Kush
Weed
420
Green *

USPTO Process

• Clearance Search – all uses in commerce
• TESS Trademark Electronic Search System
  Other uses in commerce
  TSDR – Trademark Status and Document Retrieval
• Application – TEAS – Trademark Electronic Application System
• 45 Classes of Goods and Service (e.g. smoking articles, apparel, advertising services)
• Office Action (e.g. Likely to cause consumer confusions; No lawful use in commerce (CSA))
• Publishing in the Official Gazette (TMOG)
• Time for Opposition – third party
• Registration
## Leveraging IP

<table>
<thead>
<tr>
<th>Involvement</th>
<th>Cost</th>
<th>Risk</th>
<th>Profit Potential</th>
</tr>
</thead>
<tbody>
<tr>
<td>Solo Use</td>
<td>$$$</td>
<td>High</td>
<td>Highest</td>
</tr>
<tr>
<td>Partnership</td>
<td>$$</td>
<td>Medium</td>
<td>Medium</td>
</tr>
<tr>
<td>License the IP</td>
<td>$</td>
<td>Low</td>
<td>Lowest</td>
</tr>
<tr>
<td>Assign (Sell)</td>
<td>0</td>
<td>Low</td>
<td>Variable</td>
</tr>
</tbody>
</table>

### Partnership

- Become an employee
- Run a product line
- Manage brand standards
- Cannot share profits or revenue unless a True Party of Interest
**Licensing IP**

True party issue

No variable royalties – unless True Party

- Fixed royalty
- Sell packaging
  - Not to be based on profit split
- Ancillary services

Do not Naked License, but do not exert too much control *(Barcamerica Int. and Freecyclesunnyvale)*

Can potentially move some money outside of 280e – check with your accountant

---

**Patent vs. Trade Secrets**

- **Patents** *(Federal)*
  - Requires Disclosure
  - Limited in time (20 years from filing; 15 years for plant patents)
  - Prosecution time – at least one year
  - Inventions
  - Designs
  - Plants
Patent vs. Trade Secrets

- **Trade Secrets** (State)
  - No disclosure to third parties
  - No time limit
  - Effective immediately
  - Information e.g. processes, customer lists, formulas, recipes, methods
    - Grow methods, extraction methods, know how

What is a Patent?

- Limited monopoly
- Power derives from the constitution
- Exclusionary right
  - Make
  - Sell
  - Import
  - Use
What can be patented (utility)

“Anything under the sun that is made by man.”

- Useful Process
- Machine
- Manufacture
- Composition of matter
- New and useful improvement thereof

Patentability Requirements

- Useful
- Novel
- Non-obvious
- No Statutory Bars
Other Patent Types

Design Patents
• Ornamental design of a functional item

Plant Patents
• Asexual reproduction

PVPA – Plant Variety Protection Act
• Sexual reproduction
• Must make a deposit of 3,000 viable seeds
Uniform Trade Secrets Law

RCW 19.108
Protected in contracts
Or if one knew or had reason to know that it is a trade secret

• Derives independent economic value from not being generally known and not being readily ascertainable
• Others can obtain economic value from disclosure
• Reasonable efforts to maintain secrecy

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Business Development
4th Annual NW Marijuana Law Conference
Seattle University  |  November 4, 2016

Christine Masse
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Business Development – Topics

- Mergers and acquisitions
- Equity investment
- Debt financing
- Structural issues
- Company valuation
Mergers and Acquisitions

- **Structure**
  - Acquisition of licensed business
    - If no license has yet issued, original applicant must stay on license until after license issues (i.e., sale of 90% of interest with remainder to follow post-licensure)
    - If license has already issued, original applicant may be fully bought out
    - New buyer must meet 6-month Washington residency

- **Asset sale/assignment**
  - Not prohibited, but not contemplated by the rules
    - RCW 69.50.339
      Transfer of license to produce, process, or sell marijuana—Reporting of proposed sales of outstanding or issued stock of a corporation.
      (1) If the state liquor and cannabis board approves, a license to produce, process, or sell marijuana may be transferred, without charge, to the surviving spouse or domestic partner of a deceased licensee if the license was issued in the names of one or both of the parties.
      - But, per practice, LCB is allowing for license “assignments”
Equity Investment

- LCB asserts that any ownership interest in a licensee, no matter how insignificant, triggers:
  - Vetting of owner, including spouse, as a true party of interest (See WAC 314-55-035)
  - Includes criminal history, personal background, and financial history
  - Requires Washington state residency

Equity Investment

- Vetting of all owners required
  - But see the actual language of RCW 69.50.339:
    - (2) The proposed sale of more than ten percent of the outstanding or issued stock of a corporation licensed under chapter 3, Laws of 2013, or any proposed change in the officers of such a corporation, must be reported to the state liquor and cannabis board, and state liquor and cannabis board approval must be obtained before the changes are made. A fee of seventy-five dollars will be charged for the processing of the change of stock ownership or corporate officers.
Equity Investment

- Washington residency requirements
  - But see the actual language of RCW 69.50.331:
    - (c) No license of any kind may be issued to:
      - (i) A person under the age of twenty-one years;
      - (ii) A person doing business as a sole proprietor who has not lawfully resided in the state for at least six months prior to applying to receive a license;
      - (iii) A partnership, employee cooperative, association, nonprofit corporation, or corporation unless formed under the laws of this state, and unless all of the members thereof are qualified to obtain a license as provided in this section; or
      - (iv) A person whose place of business is conducted by a manager or agent, unless the manager or agent possesses the same qualifications required of the licensee.

Debt Financing

"Financier" means any person or entity, other than a banking institution, that has made or will make an investment in the licensed business. A financier can be a person or entity that provides money as a gift, loans money to the applicant/business and expects to be paid back the amount of the loan with or without interest, or expects any percentage of the profits from the business in exchange for a loan or expertise.

See WAC 314-55-010(10)
Debt Financing

- Residency is no longer required per WAC 314-55-020(6)(b):
  - (b) Financiers will also be subject to criminal history investigations equivalent to that of the license applicant. Financiers will also be responsible for paying all fees required for the criminal history check. Financiers must meet the three-month residency requirement.

<table>
<thead>
<tr>
<th>True party of interest</th>
<th>Persons to be qualified</th>
</tr>
</thead>
<tbody>
<tr>
<td>Any entity or person (inclusive of financiers) that are expecting a percentage of the</td>
<td>Any entity or person who is in receipt of, or has the right to receive, a percentage</td>
</tr>
<tr>
<td>profits in exchange for a monetary loan or expertise. Financial institutions are not</td>
<td>of the gross or net profit from the licensed business during any full or partial calendar</td>
</tr>
<tr>
<td>considered true parties of interest.</td>
<td>or fiscal year.</td>
</tr>
<tr>
<td></td>
<td>Any entity or person who exercises control over the licensed business in exchange for</td>
</tr>
<tr>
<td></td>
<td>money or expertise.</td>
</tr>
<tr>
<td></td>
<td>For the purposes of this chapter:</td>
</tr>
<tr>
<td></td>
<td>• &quot;Gross profit&quot; includes the entire gross receipts from all sales and services made in,</td>
</tr>
<tr>
<td></td>
<td>upon, or from the licensed business.</td>
</tr>
<tr>
<td></td>
<td>• &quot;Net profit&quot; means gross sales minus cost of goods sold.</td>
</tr>
</tbody>
</table>
Debt Financing

- See WAC 314-55-035:
  - (3) **Financiers** - The WSLCB will conduct a financial investigation as well as a criminal background of financiers.
  - (4) **Persons who exercise control of business** - The WSLCB will conduct an investigation of any person or entity who exercises any control over the applicant's business operations. This may include both a financial investigation and/or a criminal history background.
  - (5) After licensure, a true party of interest, including financiers, must continue to disclose the source of funds for all moneys invested in the licensed business. The WSLCB must approve these funds prior to investing them into the business.

Debt Financing

- Other things to consider:
  - Loan covenants and control
  - Convertible debt
    - *But see* Application for Adding a Financier

As the applicant, I certify the following:

- The financier/leasing, gifting or investing money is not doing so with an expectation of a percentage or part of ownership in the business.
- The financier and spouse (if applicable) have resided in Washington State for at least three months prior to this application.
- The financier and spouse are aware they will undergo a financial and criminal background check.
Structural Issues

<table>
<thead>
<tr>
<th>True party of interest</th>
<th>Persons to be qualified</th>
</tr>
</thead>
<tbody>
<tr>
<td>Multilevel ownership structures</td>
<td>All persons and entities that make up the ownership structure (and their spouses).</td>
</tr>
</tbody>
</table>

- What does this mean?
- Use of holding companies?
- Where to raise investment?

Structural Issues

- Holding companies
  - Real property
  - Equipment
  - IP
  - Financing
  - Employee staffing
  - Transportation
  - Consultation
Company Valuation

- Federal law, other state laws
- Regulatory landscape – state and local
- Competition and number of licenses
- Scale (by regulations or at current location)
- Size of market/maturity
- Tax obligations
- Young market/no history/projections
- Liabilities – partners, investors, enforcement
- Key employees

Thank You

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Overview

- Federal Tax Issues that cannabis businesses face
- IRC § 280E
- Profitability 101
- “Deductions” for Cannabis businesses
- IRC § 471 Cost Accounting Rules
- Importance of Documentation
- Federal Tax Filing Requirements
- WA State Tax Overview
- Form 8300
- Choice of Entity Overview
Quick Facts:
- 25 States and DC allow medical marijuana
- WA, AK, CO and OR legalized recreational adult use (21 or older)
- WA Industry Participants
  - Producers (growers)
  - Processors
  - Retailers
- Marijuana is legal in the above states, it is still illegal under Federal Law
- Classified as a Schedule I drug under the Controlled Substance Act of 1970
- Subject to federal prosecution

Federal Tax Issues:
- Federal tax law applies to both legal and illegal businesses
- Generally, an illegal business is subject to tax and entitled to deduct the same business deductions as a legal business
  - 16th Amendment – Congress has power to collect tax on gross income. IRC § 61 – “…gross income means all income from whatever source derived…”
  - The courts have consistently included income from illegal activities under this law
  - Numerous court cases have allowed illegal businesses to deduct ordinary and necessary business deductions
Federal Tax Issues:

- Illegal payments cannot be deducted by either a legal or an illegal business on public policy grounds. These include:
  - Fines
  - Bribes
  - Kickbacks, etc.

- The public policy doctrine was codified under § 162(c) and (f).

Federal Tax Issues:

- **Jeffrey Edmonson v. Comm.** (TC Memo 1981-623)
  - Edmonson was a drug dealer (cocaine, amphetamines, and marijuana)
  - The taxpayer was allowed to deduct ordinary and necessary business expenses just as any legal business could
  - The Tax Court applied 162(a) to permit deductions for telephone, auto and even home office

- Congress reacted to the case by enacting IRC § 280E as part of Tax Equity and Fiscal Responsibility Act (TEFRA) in 1982
  - They felt that drug dealers should not be allowed any business expenses based on public policy grounds – See WAR ON DRUGS
**IRC § 280E:**

§ 280E provides:

No *deduction or credit shall be allowed for any amount paid or incurred during the taxable year in carrying on any trade or business if such trade or business (or the activities which comprise such trade or business) consists of *trafficking in controlled substances* (within the meaning of schedule I and II of the Controlled Substances Act) which is prohibited by Federal law or the law of any State in which such trade or business is conducted.

---

**IRC § 280E:**

§ 280E only applies to ordinary and necessary business deductions, but not to cost of goods sold. Why?

- Deductions are a matter of legislative grace
- Cost of goods sold are technically an adjustment taken into account in arriving at gross income rather than a deduction
- Reg. 1.61-3(a) and Reg. 1.162-1(a) refer to gross income as total sales less cost of goods sold
- This is a constitutional issue – power to tax under the 16th Amendment is limited to “income”
What does this mean?

- ALL deductions and credits are disallowed except Cost of Goods Sold (COGS) for Cannabis businesses
- Maximize COGS by utilizing cost accounting
- Cost containment is critical
- Minimize the non-deductible costs as much as possible
  - ✓ If these costs are out of control, difficult to achieve a break-even, let alone a profit
- Break-even = monthly fixed costs/GM%
  - ✓ Be sure to adjust GM by tax rate
- Remember to factor estimated taxes into monthly planning

Profitability 101

<table>
<thead>
<tr>
<th>Your Company</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Statement of Profit &amp; Loss</td>
<td></td>
</tr>
<tr>
<td>Gross Receipts</td>
<td>1,000</td>
</tr>
<tr>
<td>Cost of Good Sold</td>
<td>500</td>
</tr>
<tr>
<td><strong>Gross Margin</strong></td>
<td><strong>500</strong></td>
</tr>
<tr>
<td>Tax. Income</td>
<td></td>
</tr>
<tr>
<td>Operating Expenses</td>
<td>300</td>
</tr>
<tr>
<td>Non-deduct.</td>
<td></td>
</tr>
<tr>
<td>Pretax Income</td>
<td>200</td>
</tr>
<tr>
<td>Income Taxes</td>
<td>165</td>
</tr>
<tr>
<td>Net Income</td>
<td>35</td>
</tr>
</tbody>
</table>
Inventory Costing:

Inventory costing methods for tax purposes are generally covered by IRC § 471 and IRC § 263A

IRS Chief Counsel Memorandum 201504011 Release Date 1/23/2015:

- IRC § 263A (also known as UNICAP rules) does not apply to drug trafficking activities!
- If you couldn’t deduct it before, you cannot deduct it now
- Taxpayers should calculate COGS using applicable inventory-costing regulations under § 471 as they existed when § 280E was enacted
  - Regs Sec. 1.471-3(b) for resellers
  - Regs Secs 1.471-3(c) and 1.171-11 for producers
How to maximize COGS for a Producer/Processor?

- Set up books for cost accounting - break down the chart of accounts to include COGS and ordinary expenses
- Full absorption accounting rules IRC § 471 –
  - Include all direct costs
  - Include indirect costs (three categories)
    - Category I – **must** capitalize
    - Category II – **not required** to capitalize but adopts a “clear reflection of income” for IRS
    - Category III – based upon reporting on financial statements (book) but must be consistent with GAAP
- Accrual method of accounting
- Farmers are allowed to elect an inventory method of accounting, rather than cash receipts/disbursements

Direct Costs:

Must be **necessary** for production or manufacturing or processing

- Direct materials
  - Soil, plants, water and electricity for a producer (grower)
  - Flower, extracts, labels and packaging for a processor
  - Product purchases and secure inventory storage for a retailer
- Labor – trimming and watering plants, making edibles and packaging
- Payroll taxes
Indirect Costs – Category I:

Must be capitalized (included in inventory):
- Tools & Equipment not otherwise capitalized
- Repair expenses
- Maintenance
- Utilities (heat, power, light, water)
- Some rent – every facility has a restroom
- Some indirect labor (G&A) and supervisory wages & payroll taxes
- Indirect materials
- Quality control - testing

Indirect Costs – Category II:

Not required to be included in inventory but can be included if “clear reflection” of income (better matching of income and expense):
- Marketing and advertising
- Selling expenses – these cannot be added to inventory
- Other distribution expenses
- Interest
- R&D
- Tax depreciation and amortization in excess of book depreciation
- G&A and salaries necessary for activities as a whole
Indirect Costs – Category III:

Can be included in inventory if included in financial reports (book) if in accordance with GAAP:
- Real estate and property taxes
- Book depreciation - no bonus or §179. It’s not GAAP!
- Employee benefits
- Insurance necessary for production
- Don’t fit into categories I or II

What about the retailers?

Very few deductions allowed. COGS for retailer:
- Cost of product
- Some storage and delivery costs
- Security and traceability software
- Court cases to date involved retailers
  ✓ Jason Beck TC Memo 2015-149 assessed $1.25 million for 2007
  ✓ Martin Olive 139 TC 19 assessed $1.37 million for 2005
  ➢ CHAMP v Comm. 128 TC No. 14 (2007) - Does is makes sense to have more than one line of business?
  ➢ YES, if you want more deductions!
Consider A Second Line of Business...

More deductions if not trafficking in Sched I or II controlled substances if properly attributed to the business

- Must be more than incidental
- COMPLETE SEPARATION to distinguish between trades in accurate and consistent manner
  - Separate entities
  - Separate accounting
  - Separate area or location
  - Separate employees
  - Separate equipment
  - See a pattern?
- Use CHAMP case for example
- In Olive, deductions were denied because “caregiving” activities of dispensary were considered incidental to dispensing medical marijuana

Cost of Goods Sold Summary

**Producer/Processor:**
- Cost of Product (purchases)
- Freight In
- Payroll & Payroll Taxes (Direct Labor)
- Insurance
- Supplies & Materials
- Nutrients
- Testing
- Packaging
- Research & Development
- Rent
- Utilities
- Interest
- Small Equipment
- Depreciation
- Security
- Traceability

**Retailer:**
- Cost of Product (purchases)
- Payroll (limited)
- Rent (limited)
- Utilities (limited)
- Security
- Traceability (POS)
Got Sloppy Records?

- Taxpayers may not get the deductions they deserve
- Taxpayers bear the burden of proof on tax matters
- Martin Olive, 139 TC 19 couldn’t prove his deductions and was allowed 75% for COGS
  - Not a good idea to rely on the courts for tax breaks
  - Many cases where taxpayers lost out for lack of documentation
- Understand the tax law and keep EXCELLENT records
  - Taxpayers have the burden of proof

Documentation is not only critical, it’s REQUIRED!

- Set up a good accounting system and keep it up to date!
  - Utilize cost accounting
  - Good breakdown of chart of accounts
- QuickBooks, Zero, Peachtree
- POS System
- Keep Z tapes, bank statements, receipt books, invoices and receipts
- Must keep ALL records that support an item of income, deduction or credit until the period of limitation runs out
  - Could be doubled to 6 years if you under report income or overstate expenses!
- If your business is conducted with cash, keep a cash log to document activity and include the activity in accounting records
- Job descriptions and floor plans help to allocate costs!
Federal & State Tax Filing Obligations:

- Federal Income Tax – Due Annually
- Personal Property Tax – Due Annually
- WA State Combined Excise Tax (B&O & Sales Tax) – Due Monthly
- Marijuana Excise Tax – Due Monthly
- City/Local Taxes – Varies
- Payroll Taxes (941, 940, WA Employment Security and L&I) –
  Returns Due Quarterly
  - Payments may be due more frequently
- W-3, W-2s and 1099's – Due Annually
- Due Date Calendar (know what is due and when)

Washington State Taxes:

- Administered by the Department of Revenue
  - B&O tax applies to gross sales of all levels:
    - Producers
    - Processors
    - Retailers
- Retail sales tax (collected from customer at time of sale by retailer)
  - Applies to selling price of recreational marijuana, marijuana infused
    products and concentrates to consumers under the retailing classification
  - Applies to sales to residents and nonresidents. These are excluded from the
    limited nonresident sales tax exemption
  - Applies to marijuana, marijuana infused products and concentrates. Does
    not qualify for the food or prescription drug exemption
  - Medical marijuana is exempt beginning 7/1/16 (with valid recognition card
    only) taxable without valid card
**Washington State Taxes:**

- Administered by the Liquor and Cannabis Board
  - 37% marijuana excise tax on all sales of medical and recreational marijuana. Collected from customer at time of sale by the retailer and remitted to the LCB by the 20th of the following month
  - This tax does not apply to paraphernalia or non-marijuana sales
- Other taxes may apply:
  - City/local B&O taxes

**FinCEN Form 8300:**

- Routinely filed by:
  - Attorneys
  - Auto dealers
  - Cannabis businesses – producers & processors
- Now a concern for cannabis businesses!
- At least 30 Colorado businesses have been hit with Form 8300 audits
  - Questionnaires contain queries unrelated to forms
  - Clients should only address questions related to forms
- Businesses should not be concerned about filing the form
  - Be concerned what happens if they don’t
FinCEN Form 8300:

Report of Cash Payments over $10,000 Received in a Trade or Business

- Must file if company (or person) receives more than $10,000 in cash:
  - One transaction or 2 or more related transactions
  - Any transactions within a 24-hour period are considered related
  - Or more than a 24-hour period if recipient knows, or has reason to know, the transactions are related to a serious of connected transactions
  - Multiple payments for a single transaction any time the payments exceed $10,000 within any 12 month period

- Can be filed voluntarily filed for amounts under $10,000 for any suspicious transaction

- Must provide a statement to each person named on form on or before January 31 of the year following in which the cash was received
  - Must include name, telephone number and address of the information contact for the business

---

FinCEN Form 8300:

Exceptions to filing:

- Financial institution required to file FinCEN Report 112 or BSA Currency Transaction Report (BCTR)
- Casino required to file FinCEN Report 112
- Agent who receives cash from a principal if agent uses cash within 15 days and reportable on FinCEN Report 112
- Transactions that occur entirely outside US
- Transaction not in course of trade or business
FinCEN Form 8300:

- Must keep a copy of each Form 8300 for 5 years from date you file it
- Must file by 15\textsuperscript{th} day after the cash is received
- Must keep a copy of each Form 8300 for 5 years from date you file it
Scary = Form 8300 Penalties

Failure to File:
- $100 for 2015 now raised to $250 for 2016 per violation
- Aggregate annual limitation for businesses with annual gross receipts:
  - Exceeding $5M ceiling raised from $1.5M to $3M
  - Not exceeding $5M raised from $5M to $1M
- If failure is corrected within 30 days after required filing date penalties increased from $30 to $50 with aggregate limits
- Unchanged: Failure to file with intentional disregard to timely file correct form greater of $25K or amount of cash received not to exceed $100K. No aggregate ceiling

FinCEN Form 8300 Penalties – Failure to Furnish:
- Failure to Furnish statement of persons who names were required to be included raised from $100 to $250 per violation
- Aggregate annual limitation for businesses with gross receipts:
  - Exceeding $5M ceiling raised from $1.5M to $3M
  - Not exceeding $5M limitation is $1M
- If the violation is corrected within 30 days, the penalty has been raised from $30 to $50
- Aggregate annual limitation for businesses with gross receipts:
  - Exceeding $5M ceiling raised from $250K to $500K
  - Not exceeding $5M limitation is $500K
- Failure to furnish with intentional disregard
  - Greater of $250 or 10% of the aggregate items to be reported correctly
  - Or Greater of $500 per failure or 10% of aggregate amount of items to be reported correctly with no annual aggregate limitation
Choice of Entity:

- Pass-through entities
  - LLC and S Corporations
    - No tax at entity level (1065 or 1120S)
    - Taxes paid by individuals (1040)
  - C Corporation (tax at state level)
    - Tax paid at entity level (1120)
    - Tax liability stays with corporation
    - Potential double taxation but can control flow of income to individuals
    - Beware of double taxation with S Corp if wages not deductible for tax purposes. Tax on phantom income!

Choice of Entity is Tricky:

- C Corps are typically better for Cannabis Retailers
  - Tax liability stays with entity and not the owners
  - Can control income pushed down to owners
- Problems with S Corps and Cannabis businesses:
  - Possible to create unnecessary disallowed deductions with reasonable comp requirement
- Problem with Sole Proprietors and SMLLC
  - All income is subject to SE Tax
- Not a good one size fits all. We literally crunch the numbers for each client to see which is best!
Any Questions?

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Compensation, Hiring, & Firing for Cannabis Employers

Presented by:
Rochelle Nelson
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What makes cannabis employers different?

Washington State Liquor and Cannabis Board
I502 Specific Requirements

- Cannot employ anyone under 21 years of age.
- Employee security badges.
- Three year record retention: date of hire, training, payroll.
- Employees cannot share in profits.
- No independent contractors.
- License application/renewal questionnaire.

Hiring

- Application
  - Seattle’s Ban the Box
  - Background checks for I502 licensing?
- Interview Questions
  - Avoid asking questions that relate to protected class statuses or could be perceived as asking questions about protected class statuses.
  - But do not be afraid to be thorough:
    - Ask the tough questions
    - Check references
    - The 80/20 rule
Firing

Two Simple Rules To Remember
1. Have you fired other employees for similar reasons?
2. Can you show that others in the same protected class are treated fairly?

Marijuana Consumption & Drug Testing

“Can I let my employees smoke weed at work?”

No: State regulation prohibits allowing workplace consumption of alcohol or narcotics. WAC 296-800-11025
Compensation

- Must comply with all same FLSA and state and local requirements for minimum wage, overtime etc.
- No Profit Sharing
  - Bonuses (< 25%)
  - Commissions: a gray area
  - LCB’s stance on gratuities/tips
    - ORLA v. Perez
      - Only “customarily tipped” employees can participate in the tip pool
    - The “Coyote Ugly Case.”

Compensation

- Applicable FLSA and WMA Exemptions
  - Agricultural Exemption
  - Retail/Service Establishment [!]
  - White-collar exemptions
    - Administrative
    - Executive
    - Computer professional
- FLSA salary-basis increases December 1, 2016

So who is exempt?
- Greenhouse manager
- Trimmers?
- Head of IT
- Retail store managers or supervisors?
- Budtenders?
Compensation

- Independent Contractor Status
  - I502 restrictions
  - Employee v. Independent Contractor test still unclear
  - Right to control
- Piece Rate Compensation
  - Demetrio v. Sakuma Brothers
  - Accounting for meal and rest periods

Other Employment Issues to Watch For:

- Required state and federal leave laws
- Local paid sick time requirements
- Personal and data privacy
- Disability accommodations
- Unlawful discrimination and retaliation
- Unlawful harassment
- Meal & rest breaks
- Restrictive covenants
- NLRA and employee Section 7 rights
Introduction

Sean Badgley
C3 Law Group PLLC

• Administrative Defense
  • Litigation
• Purchase/Sale of Licenses

Land Use

• LCB local objection process WAC 314-55-160
  • Landlord tenant negotiations
• Obtaining a local business license, permit, or Conditional Use Permit
For your Consideration: a Few Counter-Intuitive Items

Different Approaches

Moratoriums (discussed briefly later)

Permitted Use (with many caveats)
Seattle’s Title IV License
SMC 6.500

- Closely Mirrors WAC 314-55
- Probably meant to make city licensure easier with state approval
- Also classifies Cannabis as a different sort of activity

Different Approaches

Other Cities/Counties *purport* to adopt the definitions of the Code (WAC 314-55)
Industry Issues at the National Level

National political controversies are reflected in the local zoning codes

- Edibles
- Concentrates
- Pesticides

National Issues

**Edibles** are currently seen as potentially attractive to children

The production of **concentrates** is seen as a dangerous activity

**Pesticides** are (probably correctly) viewed as a source of uncertainty
National Issues

All of these issues are focused on
Processing

Locals (the frontline for public wrath) in WA are aware of these controversies, and have addressed such activities in their local zoning code.

Processing vs. “Processing”

State Definition:
“Processing” under WAC 314-55-077 contemplates all of these activities, plus packaging product for sale
Processing vs. “Processing”

Locals (with more time/incentive) have taken a more precise look at the activities of a specific processor.

Examples

- Extraction etc not allowed, but packaging is allowed
- Growing and packaging may be allowed across several different zones, such as Agricultural, light industrial, etc
- True ‘processing’ activities are typically confined to industrial-type zones.
  - E.g. Snoho only allows for such in “agricultural-industrial”
The Bottom line:

It’s impossible to know with any accuracy every locale’s treatment of cannabis

- Local zoning is not uniformly enforced, leading to confusion
- Rules are constantly changing
- Critical to understand your client’s plan with particularity

Best Laid Plans

Picture a client who’s figured out:

- Financing
- Acceptable (which is not to say competent) business partners
- And a location that is acceptable to LCB (no small task)
Best Laid Plans

Now the client learns that LCB will not permit her use...

Locations are a facet of the license itself
WAC 314-55-135(6)

(6) **Maintaining a licensed location.** Marijuana licenses are associated with a physical location. Persons operating without a WSLCB approved licensed location to produce, process, or sell marijuana will be discontinued.

Best Laid Plans

Now it’s unclear whether the locale will permit her intended use...

Locations are a facet of the license itself
WAC 314-55-135(6)

(6) **Maintaining a licensed location.** Marijuana licenses are associated with a physical location. Persons operating without a WSLCB approved licensed location to produce, process, or sell marijuana will be discontinued.
Best Laid Plans

Even if the client is disappointed, good lawyering has occurred!

While re-tooling a business plan is disheartening and somewhat time consuming it is far more desirable than having to cancel a lease (or in the case of Real Property acquisitions, unload a piece of land)

(It’s also less capital intensive)

All’s not Lost!

Moratoriums and Cannabis Licenses are Not Mutually Exclusive

LCB does not take local zoning into account in issuing license

Regarding locations, the local objection process is focused on whether LCB simply missed a prohibited location as part of its investigation

LCB will issue license in areas with a moratorium

That does NOT mean you tell your client to operate in that area, but rather that your client can secure a license to by the client time to relocate/sell the license, etc.
Even with diligent effort and attention, highly disruptive zoning issues still arise

- Snoho sudden reversal on retailers
- Tight allocation for retailers

Key Closing Points
- A license is a piece of property - therefore more protected than a license application
- LCB does not take local zoning into account in issuing license
- When in doubt, call the city/county planner
Cannabis Litigation Issues and Procedure

Presentation by Ryan Espegard

November 4, 2016

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Exhibits:

Latest Moratorium Challenge –

Plaintiffs’ Complaint for Land Use Petition and For Injunctive Relief, La Granja Farms, LLC v. Walla Walla County, Columbia County Superior Court, Cause No. 16-2-00053-2, (August 11, 2016) -  EXHIBIT A

“Illegal” Contracts Cases –


Order Denying Summary Judgment, North v. Wemhoff, Denver County District Court, Colorado, Cause No. 12CV3005, (June 21, 2013) -  EXHIBIT C
LCB Administrative Appeals Procedure

1. Administrative Procedures Act Governs

Washington’s Administrative Procedures Act, codified as RCW Chapter 34.05, governs the procedures for appealing an LCB agency action, whether it be a licensing, enforcement, or rulemaking challenge. The appeal procedure is largely the same between the different types of agency actions that may be challenged, but they do have some differences.

2. Exhaustion of Administrative Remedies & Requesting a Hearing

The most crucial requirement to properly challenging an LCB decision is the appellant’s obligation to exhaust administrative remedies prior to seeking judicial review. Many appellants are eager to get their matter before a judge, but failing to fully exhaust administrative remedies can be fatal to an appeal. RCW 34.05.534 states that exhaustion of administrative remedies is required except in limited circumstances of rulemaking challenges and where exhaustion would be futile.

Exhaustion of remedies is easy to comply with in certain circumstances. For a licensing denial or administrative violation notice (“AVN”) the LCB will send the applicant/licensee a form detailing the appeal rights and clearly articulating how to initiate an appeal. However, there are numerous instances when the LCB does not provide such notice. Nearly any licensing or enforcement decision can be appealed. RCW 34.05.413(1) states that an agency can commence a proceeding at any time with respect to a matter within its jurisdiction. An applicant/licensee simply needs to request the hearing. Once the request is made, the LCB is then required to either grant the request or state in writing why the request was denied pursuant to RCW 34.05.416. Presumably, a denial of a request for a hearing will mark the exhaustion of administrative remedies and will allow the applicant/licensee to proceed with judicial review.

3. Pre-Hearing Procedure

When the LCB accepts a request for an administrative hearing, the matter is initially forwarded to the Attorney General’s Office, then subsequently to the Office of Administrative Hearings (“OAH”). Once assigned to an administrative law judge (“ALJ”) at OAH, a prehearing conference will be scheduled. At that hearing, all prehearing matters may be addressed. Typically the hearing will result in established issue statements and a schedule to govern the matter. Appellants may request discovery if needed and should be allowed to submit prehearing briefing and motions if desired. During this process, the appellant should not rely exclusively on the public records requests to conduct discovery as the ALJ will have no influence over the speed of document production. Instead, specific discovery requests should be made if needed.

OAH Model Rules of Procedure can be found at Chapter 10-08 WAC.)
4. Hearing Conduct

Administrative appeals at OAH are conducted as informal mini trials. Both parties will have the opportunity to make opening statements and closing arguments. Both parties will present evidence and take witness testimony. While it is conducted in a fashion similar to a trial, it is less formal and does not strictly adhere to the rules of evidence. RCW 34.05.452. The hearing will be audio recorded.

5. Post Hearing Process

If post-hearing briefing has been requested by either party, the ALJ will typically permit it. The ALJ’s decision will then be made after the filing of all briefing. The ALJ’s decision is referred to as an Initial Order. The Initial Order becomes a Final Order unless either party files a petition for review of the Initial Order with the LCB pursuant to WAC 314-42-095(2). The LCB is then able to issue a Final Order affirming the Initial Order or revising it. The Final Order is subject to judicial review.

6. Judicial Review

Judicial review is governed by RCW 34.05.510 through RCW 34.05.598. The procedure starts with filing a petition for judicial review in Superior Court in Thurston County or in the county of the petitioner’s residence or principal place of business. The petition must be filed within 30 days of service of the final order or other agency action. The petitioner must establish standing to bring the action pursuant to RCW 34.05.530. Presumably standing will be established if the LCB granted the petitioner an adjudicative proceeding. If a hearing was denied, the petitioner must be prepared to argue standing.

It is important to note that since judicial review takes an appellate posture, issues that were not raised before the agency may typically not be raised upon judicial review. RCW 34.05.554. Additionally, the facts are also limited record developed during the underlying adjudicative proceeding. RCW 34.05.558. Thus, it is extraordinarily important for appellants to fully develop the factual record and all legal arguments during the administrative appeal.

7. Rulemaking Challenges

Rulemaking challenges do not follow the adjudicative proceeding process outlined above. Instead, the appellant may immediately seek judicial review, may petition the LCB to amend or repeal the rule, or may petition the legislature’s joint administrative rules committee.

See RCW 34.05.330; RCW 34.05.570(2); and RCW 34.05.630.
Table of Cases Discussed

1. Preemption Cases


County ordinance banned the use of most common class of biosolids. However, biosolids are regulated at the state level by the Department of Ecology. Court of Appeals, Division 2, found that the ordinance was preempted by state law because the ordinance prohibits what state law allows, the ordinance thwart’s the legislatures purpose, and the ordinance was an exercise of power not conferred to local governments under the statutory scheme regulating biosolids.

*State v. Seattle, 94 Wn.2d 162, 615 P.2d 461 (1980):*

The Court found that the City of Seattle’s Landmarks Preservation Ordinance was preempted by a statute granting authority to the University Board of Regents “raze” or “alter” buildings owned by the University. The ordinance conflicted with the statute because it required the University to seek permission to raze or alter landmark buildings despite the authority already granted by statute.


City ordinance imposing penalties for driving under the influence of intoxicating liquor was preempted to the extent it sought suspend driver’s licenses since the field of issuance, regulation, and suspension of such licenses was preempted by state statute. However, the ordinance was not preempted to the extent it imposed penalties within the maximums established by statute.

2. Special Relationship Exception to Public Duty Doctrine


Court found City liable to buyer of property who relied on negligent representation about the applicable zoning designation given by City employee.

3. Washing Illegal Contract Enforcement Case

*Evans v. Luster, 84 Wn. App. 447, 928 P.2d 455 (1996):*

Contractor could not recover fees on contract for services with property owner where contract was agreement to clear wetlands without a permit. “If a contract is illegal or flows from an illegal act, a court will leave the parties as it finds them.”
4. Retail Dispersion Ordinances


Court invalidated Bellevue’s first in time rule with respect to requirement that licensees not be located within 1,000 feet of one another. Methods for determining which licensee between competing licensees could be located first to establish 1,000 foot buffer were not properly established through the rulemaking process.
THE SUPERIOR COURT FOR THE STATE OF WASHINGTON
IN AND FOR COLUMBIA COUNTY

LA GRANJA FARMS, LLC, A Washington
Limited Liability Company, MARY HANSEN,
Property Owner, CRESTON ROGERSON, an
individual,
v.

WASHINGTON STATE ATTORNEY
GENERALS OFFICE AND THE
WASHINGTON STATE LIQUOR AND
CANNABIS BOARD, a state agency,

Defendant Intervenor,
v.

WALLA WALLA COUNTY;

Defendant.

NO. 16 2 00053 2

PLAINTIFF’S COMPLAINT FOR
LAND USE PETITION AND FOR
INJUNCTIVE RELIEF

I. INTRODUCTION

1.1 Plaintiffs bring this action to prevent Walla Walla County from improperly
enforcing fines as a result of improper enforcement of a zoning law. This action is brought
pursuant to Washington’s Land Use Petition Act (“LUPA”), RCW 36.70C et seq., Washington’s
Declaratory Judgment Act, RCW 7.24 et seq., RCW 7.16 et seq., governing extraordinary writs,
Civil Rule 65 governing injunctions and the common law.

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EXHIBIT “A”

II. PARTIES

2.1 Plaintiff Mary Hansen is a resident of Walla Walla County with a legal interest in property situated in unincorporated Walla Walla County identified by Tax Parcel Number: 380820140001 and with the common address of 2987k S Fork Coppei Rd, Waitsburg, WA 99361 (the “Property”).

2.2 Plaintiff La Granja Farms, LLC is a Washington State limited liability company with a legal interest in the Property.

2.3 Plaintiff Creston Rogerson is a resident of Walla Walla County with a legal interest in the Property.

2.4 Plaintiffs’ Hansen and Rogerson were at all times relevant residents of Walla Wall County. Plaintiff La Granja Farms, LLC was organized under Washington and has its principal place of business in Walla Wall County.

2.5 Defendant Intervenor Washington State Liquor and Cannabis Board ("WSLCB") is responsible for licensing and regulating the production of marijuana in the state of Washington and is a necessary party to the determination of the regulatory and licensing rights as issue in this lawsuit.

2.6 Defendant Intervenor Washington State Attorney General is the state agency responsible for representing the WSLCB,

2.7 Under RCW 36.01.010, Defendant Walla Walla County ("Defendant" or "the County" herein after) is, and at all times relevant was, a corporation organized and existing under the laws of Washington State with corporate powers to be sued.

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T:\WP\WlnLa Granja Farms\La Granja Farms, LLC v Walla Walla County (State LUPA appeal)\Readings - Initial0370290.docx

LAND USE PETITION, COMPLAINT FOR DECLARATORY RELIEF, WRIT OF MANDAMUS AND INJUNCTION

Page -- 2
III. JURISDICTION AND VENUE

3.1 Washington State superior courts have jurisdiction over the parties and subject matter, pursuant to RCW 2.08.010, RCW 7.16.160, RCW 7.24.010 and RCW 36.70C.040.

3.2 Venue in Columbia County Superior Court is proper pursuant to RCW 36.01.050 and the list of the two nearest judicial districts to Walla Walla Superior Court as provided by the Washington Courts’ website https://www.courts.wa.gov/court_dir/?fa=court_dir.filingvenue.

IV. FACTUAL ALLEGATIONS

4.1 Walla Walla County adopted a series of ordinances pursuant to its apparent authority as a County and codified those ordinances pursuant to WWCC 1.01.010 et seq. including a zoning code.

4.2 As part of its zoning code Walla Walla County adopted WWCC 17.16.010, which prohibits the “production, processing, storage, and retail sale of recreational marijuana” and reads in its entirety as follows:

Establishment of Uses

The use of a property is defined by the activity for which the building or lot is intended, designed, arranged, occupied or maintained. All applicable requirements of this code, or other applicable state or federal requirements, shall govern a use located in unincorporated Walla Walla County. Any recreational marijuana land use including, but not limited to, production, processing, storage, and retail sale of recreational marijuana and recreational marijuana-derived products are prohibited land uses in unincorporated Walla Walla County. (Ord. 269 (part), 2002; Ord. 312 (part), 2005; Ord. 343 §§ 1, 2, 2007; Ord. No. 371, § III (Exh. A, Pt. D), 8-3-2009; Ord. No. 425, § II, 11-17-14).

4.3 The WWCC does not define “recreational marijuana.”
4.4 The County’s enforcement officials, including Defendant Thomas Glover, have admitted under oath in official proceedings that the production of “medical marijuana” does not violate the provisions of WWCC 17.16.010.

4.5 To enforce prohibited zoning activities, the County adopted its own Notice-of-Violation and-Order system in WWCC 14.13.080. A notice of violation (“NOV”) letter is sent to the property owner after the County’s enforcing official determines one or more violations of the zoning code has been committed on the property. There is no hearing at the time the enforcing official sends the NOV to the property owner.

4.6 WWCC 14.13.080(C) gives the property owner ten calendar days to appeal the NOV to a hearing examiner pursuant to WWCC 14.11.030. This is the first opportunity for the property owner to get a hearing.

4.7 In any appeal, regardless of the penalty or enforcement decision, the County unlawfully and unconstitutionally places the burden upon the property owner to prove that the decision of the County or its officials was unlawful. WWCC 14.11.030.

4.8 Pursuant to WWCC 14.11.030 the property owner appealing an enforcement decision or an assessment of any penalty, fine or criminal sanction is not entitled to any relief from that decision unless the Citizen can establish one of the following conditions:

1. The body or officer that made the decision engaged in unlawful procedure or failed to follow a prescribed process, unless the error was harmless;

2. The decision is an erroneous interpretation of the law, after allowing for such deference as is due the construction of a law by the administrative decision maker with expertise;

3. The decision is not supported by evidence that is substantial when viewed in light of the whole record before the hearing body;

T.W.U.P.A/Grande Fami/La Grande Fami, LLC v Walla Walla County (State LUPA appeal)9/3/2010

LAND USE PETITION,
COMPLAINT FOR DECLARATORY RELIEF,
WRIT OF MANDAMUS AND INJUNCTION
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4. The decision is a clearly erroneous application of the law to the facts; or

5. The decision is outside the authority or jurisdiction of the body or officer making the decision.

4.9 The County adopted codes setting forth a procedure to enforce its ordinances and to impose penalties on property owners. WWCC 14.13 et. seq.

4.10 The County set the civil monetary penalties of $250 a day regardless of the nature of the alleged violation.

4.11 The County includes prevailing-party attorney’s fees and costs against the property owner incurred by the County as a result of any enforcement action. WWCC 14.13.090.

4.12 In addition, the County authorizes its enforcement officers to charge violators with a gross misdemeanor punished by not more than 90 days in jail and a $1,000 fine or both, if the Citizen fails or refuses to comply with the directives of the enforcement officer. WWCC 14.13.100.

4.13 The County sent Plaintiffs an NOV dated August 11, 2015 determining Plaintiffs violated WWCC 17.16.010 by producing recreational marijuana. Plaintiffs appealed the NOV and requested a due-process hearing.

4.14 The Plaintiffs are licensed and lawful producers of medical marijuana on land they lawfully possess in unincorporated Walla Walla County.

4.15 Despite knowing that Plaintiffs are producers of medical marijuana and exempt from the prohibitions of WWCC 17.16.010, the County imposed a $250 daily fine upon the Plaintiffs for alleged violations of WWCC 17.16.010.
EXHIBIT “A”

4.16 The County sent Plaintiffs an invoice for the fines on October 20, 2015. According to the invoice, the fines began on August 27, 2015 before Plaintiffs were given the opportunity to be heard on the alleged violations in the August 11, 2015 NOV. The invoice included a penalty of $13,750, which was for 55 days at the rate of $250 per day. The invoice stated that Plaintiffs would receive an invoice each month assessing the monetary penalty.

4.17 The County sent a second Invoice for fines to Plaintiffs on November 20, 2015. The County reassessed the penalty from the October (55 days at $250 per day) invoice and included additional penalties from October 21 through November 20, 2015 for a total of $250 x 86 days or $21,500. Again, the document promised that the County would send monthly invoices to Plaintiffs assessing the monetary penalties.

4.18 The County did not send an invoice for penalties for December 2015, January 2016, or February 2016.

4.19 On January 11, 2016, Plaintiffs received a due-process hearing for appeal of the August 2015 NOV. The hearing was administrative and conducted by the County’s Hearing Examiner. The Hearing Examiner placed the full burden of proof on the Plaintiffs. Plaintiffs were required to prove the County’s actions were unlawful.

4.20 On February 10, 2016, the Hearing Examiner denied Plaintiffs’ appeal of the August 11th NOV and denied Plaintiffs’ motion for reconsideration March 2, 2016.

4.21 On March 1, 2016, the County sent its third invoice to Plaintiffs for the monetary penalties. This invoice reassessed all of the fines in the previous two invoices (August 27th through November 20th) and added additional fines from November 21, 2015 through March 1, 2016. For 188 days of penalties at $250 per day or a total of $47,000.
EXHIBIT “A”

4.22 Just as in the previous two invoices, the County allowed Plaintiffs to appeal of the penalties assessed in the invoices. On its face, such an appeal would include all penalties from August 27, 2015 through March 1, 2016. The invoice makes no distinction between what penalties the Plaintiffs have a right to appeal.

4.23 Plaintiffs appealed all $47,000 of penalties assessed in the March 1st invoice and requested a due-process hearing.

4.24 An administrative hearing occurred on May 9, 2016. On June 27, 2016, the County’s Hearing Examiner issued an order denying the appeal, but reduced the assessed penalties from $47,000 to $39,250 concluding that Plaintiffs ceased marijuana production and sales for the months of December (2015) and January (2016).

4.25 The County did not send a monthly invoice for any penalties accruing after the March 1, 2015 invoice.

4.26 Plaintiffs timely sought a motion to reconsider the Hearing Examiner’s June 27th decision and order. The Hearing Examiner denied the motion to reconsider on July 28, 2016.

4.27 As a result of the County’s actions, Plaintiffs have been deprived of important liberty and property interests without due process of law and run the risk of deprivation of important liberty and property interests in the future.

V. FIRST CAUSE OF ACTION

LAND USE PETITION
(RCW 36.70C)

5.1 Plaintiffs as described above are also the Petitioners for this land use petition filed in accordance with RCW 36.70C. Names of Petitioners are identical to Plaintiffs as stated above.
5.2 Petitioners restate the allegations in paragraphs 1.1 through 4.27 as though fully
set forth herein.

5.3 The names and address of Petitioners’ attorneys are Jerry Moberg and Patrick
Moberg, Jerry Moberg & Associates, PO Box 130 ♦ 124 3rd Ave SW, Ephrata, WA 98823.

5.4 The name and address of the local jurisdiction is the Walla Walla Community
Development Department, 310 Poplar St., Suite 200, Walla Walla, WA 99362.

5.5 The identification of the decision making officer is Thomas E. Glover, Director of
Walla Walla Community Development. Mr. Glover determined Petitioners violated WWCC
17.16.010 in a Notice of Violation dated August 11, 2015, a copy of which is attached hereto in
Exhibit “A”. Mr. Glover assessed fines as a result of the determined violations. A copy of the
invoices assessing the fines is attached hereto as Exhibit “B”. Janine “Nina” Batson, Walla
Walla Code Compliance Officer assisted in Mr. Glover’s determination. The Petitioners timely
appealed the NOV to the Walla Walla Hearing Examiner. Hearing Examiner Leland B. Kerr
upheld Mr. Glover’s determination of the zoning violation in his June 27, 2016 Decision and
Order, In the Matter of the Appeal of La Granja Farms, LLC, No. APP16-001, C15-0067. A
copy of the Hearing Examiner’s decision is attached hereto as Exhibit “C”. WWCC 14.11.060
requires Petitioners to file a motion for reconsideration before seeking relief under LUPA in the
superior court. Petitioners timely motioned the Hearing Examiner to reconsider the Decision and
Order. On July 28, 2016, the Hearing Examiner denied Petitioners’ motion to reconsider in his
Decision on Reconsideration, In the Matter of Appeal of La Granja Farms, LLC of Notice of
Violation and Order, No. APP16-001, CE15-0067, a copy of which is attached hereto as Exhibit
“C”. This land use petition seeks review of the June 27, 2016 Decision and Order and the July
28, 2016 Decision on Reconsideration issued by Walla Walla County.
EXHIBIT “A”

5.6 There are no additional parties to identify under RCW 36.70C.040(2)(b) through (d).

5.7 Petitioners all have a legal interest in the Property subject to the County’s final land use decision. The Petitioners have been aggrieved and adversely affected by the County’s decision, which is challenged in this petition.

Petitioners’ Concise Statement of Errors and Concise Statement of Facts

5.8 The County engaged in unlawful procedure in approving its ban against the production of recreational marijuana contained in WWCC 17.16.010.

5.8.1 The County first passed Ordinance No. 415 on September 16, 2013, which put a moratorium on all marijuana activity in the county. The County, as required by law, published legal notice for public hearing on the moratorium in the Waitsburg Times, the Walla Walla Union, and Walla Walla Daily Bulletin, a copy of the proof of publication is attached in Exhibit “D”. Nowhere in any of the notices does the County include the possibility of a ban against any licensed marijuana activity. In fact, Ordinance No. 415 does not include any language suggesting the County is going to ban any licensed marijuana activity. A copy of the Ordinance No. 415 is attached hereto as Exhibit “E”. In Section IV on page 9, the County provides the purpose of the moratorium:

The purpose of this moratorium and interim zoning Ordinance is to allow the County adequate time to study the secondary land use impacts associated with the location and siting of structures and uses in which marijuana production, marijuana processing or marijuana retailing may take place. In addition, the moratorium will allow the County adequate time to study the implementation of I-502, and to review any responses from Federal law enforcement. The County’s goal is to ultimately draft zoning and other possible regulations to address such developments and uses, to hold public hearings on such draft regulations and to adopt such regulations.
According to Ordinance No. 415, the County instituted a moratorium to allow time to
draft and implement regulations for the "implementation" of licensed marijuana businesses under
I-502. The County did not state in Ordinance No. 415 that it was considering a ban against all
recreational marijuana activity in the county. The duration of the moratorium was for twelve
months from September 16, 2013 until September 15, 2014.

5.8.2 Relying upon the County's notice that it would allow licensed production
of marijuana pursuant through adopted regulations. Petitioners went forward with an application
to receive a license from the state to produce marijuana. Petitioners invested a considerable sum
of money, time and effort in its application for its license. Petitioners received the license on
August 4, 2014.

5.8.3 A month later, on September 8, 2014, the County passed Ordinance No.
424 to extend the moratorium in Ordinance No. 415 for another 63 days. This is the first time
the County informs the public that it is considering a ban against recreational marijuana activity
throughout the county. The County later adopted Ordinance No. 425 banning the production of
recreational marijuana. However, since the moratorium expressed in Ordinance No. 424 was not
the same as the moratorium expressed in Ordinance No. 415—i.e. the new moratorium considers
banning all marijuana activity in the county where the previous moratorium did not—the
moratorium in Ordinance No. 424 cannot be considered as a continuation, and the Petitioners’
right to produce licensed marijuana vested on August 4, 2014 when Petitioners received their
license from the state. Because Petitioners’ rights to produce state-licensed marijuana vested, the
County’s determination that Petitioners violated WWCC 17.16.010 is erroneous.

5.9 The County engaged in unlawful procedure by assessing a fine against Petitioners
during the appeal process. The County stated in the August 11th NOV that it would start
assessing a $250 daily fine for violating WWCC 17.16.010 on August 26, 2015. August 26, 2015 was also the last day for Petitioners to appeal the NOV. The Petitioners timely appealed the NOV, yet the County began assessing the fine on August 26, 2015 anyway. The Walla Walla County Code does not authorize the County to assess a fine during a timely appeal of an NOV. The County’s assessment of the fine during the appeal process is, thus, an unlawful procedure.

5.10 The County engaged in unlawful procedure in its application of the zoning regulation contained in WWCC 17.16.010 against Petitioners.

5.10.1 WWCC 17.16.010 prohibits only the production of *recreational* marijuana in the County. The regulation does not provide a definition of recreational marijuana. The County’s zoning officials, including Thomas Glover, testified under oath that the production of medical marijuana is not prohibited under this regulation.

5.10.2 In July 1, 2015, the Washington legislature passed a law that combined the medical and recreational marijuana markets under one system regulated by the Washington Liquor and Cannabis Board. Under this law only state licensed producers can grow marijuana in Washington State. These licensed producers can grow either medical or recreational marijuana. La Granja Farms, LLC is a state licensed producer.

5.10.3 The only evidence as to whether La Granja Farms’ marijuana production was medical or recreational comes from Petitioner Creston Rogerson who testified the marijuana produced was medical. The County offered no evidence that the marijuana was recreational. The Hearing Examiner’s decision was an erroneous application of the prohibition in WWCC 17.16.010 against the production of *recreational* marijuana.

5.11 The Hearing Office and the County engaged in unlawful procedure by placing the burden of proof on the Petitioners. Pursuant to WWCC 14.11.030 in any appeal, regardless of
the penalty or enforcement decision, Walla Walla County unlawfully and unconstitutionally places the burden upon the Citizen to prove that the decision of the County or its officials was wrong.

5.12 The decision to enforce the prohibition in WWCC 17.16.010 against production of recreational marijuana was an erroneous interpretation of the code and outside the County’s authority.

5.12.1 Initially when Washington passed Initiative 502 legalizing the state-wide production and sale of recreational marijuana, there was some confusion whether the state law preempted any local jurisdictions ordinances regulating recreational marijuana including the legitimacy of bans against all licensed marijuana business.

5.12.2 Attorney General Bob Ferguson added to the confusion with his legal opinion, AGO 2014 No. 2, from January 16, 2014 that the state law did not preempt local jurisdictions from banning licensed marijuana activity.

5.12.3 The Washington State Legislature cleared up the confusion when it passed RCW 69.50.331(9), which only permits a local jurisdiction to “adopt an ordinance prohibiting a marijuana producer or marijuana processor from operating or locating a business within areas zoned primarily for residential use or rural use with a minimum lot size of five acres or smaller.”

5.12.4 The Petitioners operated their state-licensed marijuana production facility on land with a rural zoning and a minimum lot size of 40 acres.

5.12.5 The County’s ban of all recreational marijuana activity in all zoning classifications violates the general laws of the state (RCW 69.50.331(9)), and, thus, the ban is unconstitutional. Because the ban is unconstitutional, the application of the ban against Petitioners is outside of the County’s authority.
EXHIBIT "A"

5.13 The decision to assess a daily $250 fine during the NOV appeal process was also an erroneous interpretation of the code and outside the County's authority as the code does not authorize collection of a fine during the appeal process.

5.14 For the reasons stated above, the County's enforcement of WWCC 17.16.010, including all civil penalties assessed, is not supported by any evidence and is a clearly erroneous application.

5.15 For reasons stated above, the County's enforcement of the ban in WWCC 17.16.010, including all civil penalties assessed, violates Petitioners' Washington State Constitutional right not to be subject to laws that conflict with the general laws of the state.

5.16 For reasons stated above, the County's enforcement of the ban in WWCC 17.16.010, including all civil penalties assessed, violates Petitioners' Washington State Constitutional right to due process and equal protection.

5.17 For reasons stated above, the County's enforcement of the ban in WWCC 17.16.010, including all civil penalties assessed, violates Petitioners' Washington State Constitutional right against laws that grant special privileges and immunities.

Request for Relief Pursuant to the Land Use Petition Act

5.18 A determination that Petitioners have met their burden of proof for this petition under one or more of the standards listed in RCW 36.70C.130.

5.19 Reversal of the land use decision

VI. SECOND CAUSE OF ACTION

CONSTITUTIONAL VIOLATION OF ARTICLE XI, SECTION 11

6.1 Plaintiffs re-allege and incorporate the preceding paragraphs as if fully set forth herein.
6.2 The County has a public duty to act within the public’s interest and use its authority to legitimately exercise its police powers.

6.3 RCW 69.50.331(9) only allows counties to ban licensed recreational marijuana production and processing in residential zones and rural zones with a minimum lot size of five acres or less. The RCW reads:

(9) Subject to *section 1601 of this act, a city, town, or county may adopt an ordinance prohibiting a marijuana producer or marijuana processor from operating or locating a business within areas zoned primarily for residential use or rural use with a minimum lot size of five acres or smaller.

6.4 The County passed an ordinance that bans all license marijuana production and processing in all zoning classifications. The County codified the ban in WWCC 17.16.010, which reads, in pertinent part:

Any recreational marijuana land use including, but not limited to, production, processing, storage, and retail sale of recreational marijuana and recreational marijuana-derived products are prohibited land uses in unincorporated Walla Walla County.

6.5 WWCC 17.16.010 prohibits what RCW 69.50.010(9) permits creating a conflict with the general laws of the state of Washington. Article XI, Section 11 of the Washington State Constitution prohibits any county from enforcing any local laws that conflict with the general laws of the state:

SECTION 11 POLICE AND SANITARY REGULATIONS.
Any county, city, town or township may make and enforce within its limits all such local police, sanitary and other regulations as are not in conflict with general laws.

6.6 Plaintiffs’ Property is zoned as Remote Rural with a minimum lot size of 40 acres. Defendant’s action in enforcing WWCC 17.16.010 against Plaintiffs violates RCW
69.50.331(9) and Article XI, Section 11 of the Washington State Constitution. The County has a duty not to enforce an ordinance that conflicts with the general laws of the state of Washington against Plaintiffs and all residents in Walla Walla County.

6.7 Plaintiffs have and will continue to suffer irreparable harm from the County’s unconstitutional enforcement of WWCC 17.16.010. The County has enforced and will continue to enforce a $250 daily fine against Plaintiffs. Compliance with WWCC 17.16.010 will force Plaintiffs to terminate its licensed business to produce and process marijuana, costing Plaintiffs tens of thousands of dollars in startup capital and millions in lost profits. Plaintiffs are entitled to temporary injunction, permanent injunction or both, as may be necessary to restrain the County from enforcing WWCC 17.16.010.

6.8 For the reasons stated herein, a real, justiciable violation exists between Plaintiffs and Defendant regarding interpretation and enforcement of WWCC 17.16.010, which is an invalid law because it conflicts with the general laws of the state of Washington.

VII. THIRD CAUSE OF ACTION

WRITS OF MANDAMUS, CERTIORARI, PROHIBITION
(RCW 7.16 et seq.)

7.1 Plaintiffs re-allege and incorporate the preceding paragraphs as if fully set forth herein.

7.2 In the event the Court will not entertain Plaintiffs’ Declaratory Judgment action as to allow complete and full relief to Plaintiffs, then Plaintiffs will have no plain, speedy or adequate remedy at law.

7.3 Defendant’s enforcement of WWCC 17.16.010, which is an invalid law because it conflicts with the general laws of the state of Washington, is an act for which a Writ of Mandamus, Certiorari, or Prohibition lies. Plaintiffs are entitled to apply for and obtain issuance
of a statutory writ to prevent the County from enforcing an unconstitutional ordinance against
Plaintiffs and to allow Plaintiffs to operate the licensed marijuana business on the Property.

7.4 For reasons set forth above, the Court should issue an extraordinary writ pursuant
to RCW 7.16 et seq, declaring the County's actions to be unlawful and ordering the County to
stop its prosecution of Plaintiffs under WWCC 17.16.010.

VIII. PRAYER FOR RELIEF

1. A determination that Petitioners have met their burden of proof for their LUPA
petition under one or more of the standards listed in RCW 36.70C.130, and the County's land
use decision is reversed;

2. A determination that WWCC 17.16.010 is unconstitutional as applied to
Plaintiffs;

3. For a Writ of Mandamus or Prohibition ordering Defendant to stop prosecution of
Plaintiffs under WWCC 17.16.010;

4. For a Writ of Certiorari ordering Defendant to stop prosecution of Plaintiffs under
WWCC 17.16.010;

5. For injunctive relief to restrain Defendant from prosecuting Plaintiffs under
WWCC 17.16.010;

6. For permission to amend the pleadings to conform to the proof; and

7. For such other and further relieve as may be just and equitable.

DATED August 6, 2016.

JERRY MOBERG, WSBA #5232
PATRICK R. MOBERG, WSBA #41323
Attorneys for Plaintiffs’
EXHIBIT "B"

IN THE SUPERIOR COURT OF ARIZONA
IN AND FOR THE COUNTY OF MARICOPA

MICHELE RENE HAMMER, individually,
Plaintiff,
v.
TODAY'S HEALTH CARE II, a Colorado corporation
Defendant.

MARK W. HAILE, an unmarried man,
Plaintiff,
v.
TODAY'S HEALTH CARE II, a Colorado corporation
Defendant.

Case No: CV2011-051310
(CONсолIDATED WITH CV2011-051311)

JUDGMENT OF DISMISSAL
(Assigned to the Honorable Michael R. McVey)

This matter having come on for oral argument on January 18, 2012, the Court having considered:

1. Plaintiffs’ Motion for Summary Judgment;
2. Plaintiffs’ Separate Statement of Facts in Support of their Motion for Summary Judgment;
3. Today’s Health Care II’s Response to Plaintiff’s Motion for Summary Judgment;

860399/15501-1
## EXHIBIT “B”

1. Today’s Health Care II Cross-Motion for Summary Judgment;
3. Plaintiffs’ Reply to Defendant’s Response to Motion for Summary Judgment and Plaintiffs’ Response to Defendant’s Cross-Motion for Summary Judgment;
5. Plaintiffs’ Notice of Errata to Supplemental Statement of Facts; and

The Court having considered the pleadings on file herein and having heard oral argument of counsel for the parties finds the following:

### Facts as Undisputed.

1. On or about August 12, 2010, each of the Plaintiffs entered into separate loan agreements with Defendant, Today’s Health Care II, a Nevada corporation (“THC”).
2. Each Plaintiff loaned THC $250,000 for the stated purpose of financing a "retail medical marijuana sales and growth center". Each loan was memorialized by a loan agreement and a promissory note (the "loan documents").
3. These loan documents required THC to pay Plaintiffs interest at the rate of 12% per annum on the 12th day of each month.
4. The agreement provided that in the event of a default, THC had five (5) days within which to cure its default.
5. If THC failed to cure its default within five (5) days, Plaintiffs were entitled to repayment of the principal loan amount at a default interest rate of 21%, plus any costs and attorneys’ fees associated with enforcement and collection.
6. THC failed to timely pay interest on the loans by March 12, 2011.
7. As of March 17, 2011, THC defaulted on its obligations under the loan obligation.
EXHIBIT “B”

Legal Analysis.

The sole legal issue presented by both the Motion for Summary Judgment, as well as the Cross Motion for Summary Judgment is whether the loan documents are enforceable, or whether they are void and unenforceable due to illegality. As mentioned, both loan agreements specifically provide as follows:

“Borrower shall use the loan proceeds for a retail medical marijuana sales and grow center.”

The retail medical marijuana sales and grow center was located in Colorado.

Colorado, like Arizona, has adopted a scheme by which patients may obtain amounts of marijuana for medicinal purposes with a prescription from a physician. However, the United States’ Controlled Substances Act (“CSA”) makes it illegal to manufacture, distribute, or dispense or possess with intent to manufacture, distribute, or dispense a controlled substance. 21 U.S.C.A. § 841. The United States still categorizes marijuana as a Schedule I, controlled substance pursuant to the CSA and Federal Criminal Statutes. 21 U.S.C.A. § 812. It is unlawful to knowingly open, lease, rent, use or maintain property for the manufacturing, storing, or distribution of controlled substances. 21 U.S.C.A. § 856. Finally, under Federal Law, it is unlawful to aid and abet the commission of a Federal crime. 18 U.S.C.A. § 2.

In Gonzales v. Raisch, 545 U.S. 1, 125 S.Ct. 2195, 162 L.Ed. 2d. 1, (2005), the U.S. Supreme Court addressed the conflict between Federal Law, which continues to outlaw the possession and distribution of marijuana, and state medical marijuana laws. In that case, the Supreme Court held that prohibition of such sales of marijuana is properly within Congress’ authority under Art. I, Sec. 8 of the United States Constitution (The Commerce Clause). Thus, dispensation of marijuana, even for medicinal purposes, remains illegal – state law notwithstanding.

EXHIBIT “B”

Plaintiffs argue the promissory notes are still enforceable despite the recitation of an
illegal purpose in the Loan Agreement, because the promissory notes can be enforced without any
proof of an illegal purpose. However, a contract which in itself is not unlawful either in what it
promises or in the consideration for the promise may nevertheless be rendered void as against
public policy as part of a general scheme to bring about an unlawful result. 8 Williston on
Contracts section 19:11 (4th Ed.).

The explicitly stated purpose of these loan agreements was to finance the sale and
distribution of marijuana. This was in clear violation of the laws of the United States. As such,
this contract is void and unenforceable. This Court recognizes the harsh result of this ruling.
Although Plaintiffs did not plead any equitable right to recovery such as unjust enrichment, or
restitution, this Court considered whether such relief may be available to these Plaintiffs.
Equitable relief is not available when recovery at law is forbidden because the contract is void as
against public policy. Landi v. Arkules, 172 Ariz. 126, 136, 835 P.2d 458, 468; DOBBS ON
REMEDIES § 13.5, at 994-47. The rule is that a contract whose formation or performance is
illegal is, subject to several exceptions, void and unenforceable. But this is not all, for one who
enters into such a contract is not only denied enforcement of his bargain, he is also denied
restitution for any benefits he has conferred under the contract. Id.

This Court finds that there are no genuine issues of material fact and that THC is entitled
to judgment as a matter of law. Therefore,

**IT IS ORDERED** granting summary judgment on Defendant’s Cross Motion for
Summary Judgment and dismissing Plaintiffs’ Complaint with prejudice.

**IT IS FURTHER ORDERED** denying Plaintiffs’ Motion for Summary Judgment.
As the contracts are void as against public policy, no attorneys’ fees are awarded to
Defendant. However,

**IT IS ORDERED** awarding Defendant its taxable costs in the amount of $_____.

Dated ____________________

Honorable Michael R. McVey

860399/15501-1
EXHIBIT "B"

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Granted

Signed on this day, April 17, 2012

/S/ Michael McVey
Judicial Officer of Superior Court
EXHIBIT “C”

DISTRICT COURT, CITY & COUNTY OF DENVER, COLORADO
1437 Bannock Street
Denver, Colorado 80202

 Plaintiff: CHARLES NORTH, individually, and as a member and manager of HERBAL SOLUTIONS, LLC

v.

Defendants: CARL WEMHOFF, and COLORADO COLITIS, LLC d/b/a HERBAL REMEDIES, INC., a successor in interest to HERBAL SOLUTIONS, LLC

DATE FILED: June 21, 2013 12:36 PM
CASE NUMBER: 2012CV3005

▲ COURT USE ONLY ▲

Case Number: 12CV3005
Courtroom: 280

ORDER DENYING MOTION FOR SUMMARY JUDGMENT

THIS MATTER comes before the Court on Defendants’ Joint Motion for Summary Judgment filed on April 10, 2013, and Plaintiffs’ Motion for Leave to Amend Complaint filed on May 1, 2013. The Court, having reviewed the related pleadings, relevant authorities, and being otherwise fully advised in the premises herein, FINDS and ORDERS as follows:

I. Background

Plaintiff Charles North (“Plaintiff”) and Defendant Carl Wemhoff (“Defendant”) met in 2006. Sometime in 2008, the parties decided to open a medical marijuana dispensary. On February 25, 2009, the parties formed Herbal Solutions, LLC (“Herbal Solutions”) by filing articles of organization with the Colorado Secretary of State. The parties agreed to each have a 50% membership interest in Herbal Solutions. Defendant alleges that no written operating agreement was ever drafted for the company and that the agreement under which Plaintiff and Defendant operated Herbal Solutions was oral and created over multiple conversations between the parties.

Plaintiff alleges that in April 2009, he became aware that Defendant removed money and medical marijuana from the company without authorization and that Defendant was growing marijuana and selling it outside of Herbal Solutions. In June 2009, the parties had a physical altercation that resulted in Plaintiff’s arrest. As a result of that altercation, Defendant petitioned the Adams County Court for a restraining order against Plaintiff. The restraining order remains in place today.
EXHIBIT “C”

Defendant alleges that after the altercation, he attempted to wind down Herbal Solutions and made several offers to buy out or settle with Plaintiff. Defendant alleges that Plaintiff refused to sell his interest in Herbal Solutions.

On June 13, 2009, Defendant formed Herbal Remedies, Inc. (“Herbal Remedies”) by filing articles of incorporation with the Colorado Secretary of State. Plaintiff alleges that Herbal Remedies is a medical marijuana dispensary that provides the same or similar medical marijuana service as Herbal Solutions. Plaintiff also alleges that Defendant transferred assets from Herbal Solutions to Herbal Remedies without authorization. Plaintiff contends that these assets include $35,000 worth of equipment and labor that Plaintiff contributed to Herbal Solutions, client files, and the medical marijuana product that Plaintiff grew and provided to Herbal Solutions.

On May 15, 2012, Plaintiff initiated this action pro se against Defendant and Colorado Colitas, LLC d/b/a Herbal Remedies. After Plaintiff retained counsel, Plaintiff filed an Amended Complaint on July 12, 2012, alleging five claims for relief: 1) a derivative action against Defendant on behalf of Herbal Solutions, 2) imposition of constructive trust or equitable lien against Defendant, 3) dissolution of Herbal Solutions, 4) accounting from Defendant, and 5) conversion against Defendant and Herbal Remedies.

II. Summary Judgment Standard of Review

The court may grant a motion for summary judgment when the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law. C.R.C.P. 56(c); Bebo Const. Co. v. Mattax & O’Brien, P.C., 990 P.2d 78 (Colo. 1999). The court may not grant summary judgment when pleadings and affidavits show material facts in dispute. GE Life and Annuity Assur. Co. v. Fort Collins Assemblage, Ltd., 53 P.3d 703, 706 (Colo. App. 2001).

A material fact is one that will affect the outcome of the case. Struble v. American Family Ins. Co., 172 P.3d 950 (Colo. App. 2007); Krane v. St. Anthony Hosp. Systems, 738 P.2d 75 (Colo. App. 1987). The moving party has the initial burden of showing no genuine issue of material fact exists; the burden then shifts to the nonmoving party to establish that there is a triable issue of fact. AviComm, Inc. v. Colo. Pub. Utils. Comm’n, 955 P.2d 1023 (Colo. 1998). Once the party moving for summary judgment has made a convincing showing that genuine issues of fact are lacking, the opposing party cannot rest upon the mere allegations or denials in

III. Analysis

Defendants first argue that summary judgment should be granted in favor of Defendants because Herbal Solutions was founded upon a void and unenforceable agreement. The Court disagrees.

Defendants allege that Herbal Solutions was founded upon an agreement to operate a business that manufactured, distributed, and dispensed marijuana. Defendants argue that because it is illegal under federal law to possess or use marijuana, the agreement that created Herbal Solutions is void and unenforceable. In support of their argument, Defendants rely on an Order issued by Judge Pratt of the 18th Judicial District of Colorado. Judge Pratt found that a contract between two parties that involved medical marijuana was void as against public policy. (Defendants’ Exh. 2) Judge Pratt’s Order is not binding on this Court.

In his Order, Judge Pratt found that contracts in contravention of public policy are void and for the protection of the public, should not be enforced. *(Id.)* While the Court agrees with Judge Pratt that illegal contracts and contracts against public policy should not be enforced, under current Colorado law, the sale and use of medical marijuana and marijuana in general is neither illegal nor against public policy. The medical use of marijuana has been legal in Colorado since the State Constitution was amended in 2000. Furthermore, in 2012, the People of the State of Colorado voted to legalize the personal use of marijuana for persons over twenty-one years of age.

The People of the State of Colorado have determined that medical, and now, recreational marijuana, should be available legally in this state. Accordingly, what was an industry previously operating in the shadows now is an industry operating under force of state law. With the privileges afforded the marijuana industry by the voters come obligations, including all obligations inherent in operating in the legitimate commercial world. This includes business relationships and obligations such as contracts, operating agreements and corporate articles and bylaws, among many other things. These relationships must be enforceable so that this newly legitimate industry does not devolve into commercial anarchy. Accordingly, until this Court is advised otherwise, it will enforce these commercial relationships in accordance with Colorado law, notwithstanding federal law that makes possession and sale of marijuana illegal.
EXHIBIT “C”

Defendants next argue that Plaintiffs’ claims for derivative action should be dismissed because Plaintiff failed to comply with the requirements of C.R.C.P. 23.1 in filing this action. The Court disagrees.

C.R.C.P. 23.1 states, “in a derivative action brought by one or more shareholders or members to enforce a right of a corporation or of an unincorporated association, ... the complaint shall be verified.” C.R.C.P. 23.1.

Defendants argue that Plaintiff did not verify his Second Amended Complaint filed on July 12, 2012. Plaintiffs agree that the Second Amended Complaint was not verified, but filed a Motion to Amend the Complaint, attaching a verification contemporaneously with their response. Additionally, Plaintiffs assert that their original Complaint and First Amended Complaint were both verified and served on Defendants thereby giving Defendants proper notice of this action.

Plaintiffs filed their first Complaint on May 15, 2012. This Complaint was verified and properly served on Defendant on May 31, 2012. Plaintiffs filed their First Amended Complaint on June 27, 2012. This Complaint added Herbal Remedies as a defendant. The First Amended Complaint was also verified and properly served on Defendant on July 1, 2012. Plaintiffs filed their Second Amended Complaint on July 12, 2012. This Complaint replaced Herbal Remedies as a defendant with Colorado Colitas, LLC d/b/a Herbal Remedies. This complaint was not verified but was served on Defendant, as owner of Colorado Colitas, on July 15, 2012.

“A motion to amend is entitled to a lenient examination.” Polk v. Denver Dist. Court, 849 P.2d 23, 25 (Colo. 1993). “If the underlying facts or circumstances relied upon by a plaintiff may be a proper subject of relief, he ought to be afforded an opportunity to test his claim on the merits. In the absence of any apparent or declared reason-such as undue delay, bad faith or dilatory motive on the part of the movant, repeated failure to cure deficiencies by amendments previously allowed, undue prejudice to the opposing party by virtue of allowance of the amendment, futility of amendment, etc.-the leave sought should, as the rules require, be ‘freely given.’” Id.

Given that two previous complaints were verified and served on Defendant, the Court finds that Defendants had sufficient notice of this action and that no undue prejudice will be imposed on Defendants by allowing Plaintiffs to amend their complaint. Therefore, Plaintiffs’ Motion for Leave to Amend Complaint is GRANTED. The Court finds that Plaintiffs’ Second Amended Complaint is sufficiently verified to comply with C.R.C.P. 23.1.
EXHIBIT “C”

Finally, Defendants argue that Plaintiffs’ claims for derivative action should be dismissed because Plaintiff failed to make a written demand upon Defendant pursuant to C.R.S. §7-80-714. C.R.S. §7-80-714 states, “no member shall commence a derivative proceeding pursuant to this part 7 unless: (a) A written demand has been made upon the limited liability company to take suitable action.” C.R.S. §7-80-714(1). A written demand need not be made if such demand would be futile. Bell v. Arnold, 487 P.2d 545, 547 (Colo. 1971).

Defendants argue that Plaintiff failed to make a written demand on Defendant and failed to plead that such a demand would be futile. Plaintiffs argue that prior to the commencement of this action numerous written demands were made to Defendant detailing the commencement or threat of legal action. Furthermore, Plaintiffs argue that a written demand was not required, as the factual allegations in this action dictate that a written demand would have been futile.

There are disputed issues of fact regarding whether or not a written demand was made by Plaintiff to Defendant. However, the facts as alleged in Plaintiffs’ Second Amended Complaint clearly demonstrate that a written demand would have been futile. The Colorado Supreme Court has held that if it is self-evident that a written demand would be futile, a plaintiff is not required to plead futility and a written demand is not required. Hirsch v. Jones Intercable, Inc., 984 P.2d 629, 635 (Colo. 1999). Here, Defendant is the only other member of Herbal Solutions and is an alleged wrongdoer. Plaintiff alleges that Defendant wrongfully transferred assets from Herbal Solutions to his new company, Herbal Remedies. Therefore, the Court finds that it is self-evident from the facts as alleged in the Complaint that it would have been futile for Plaintiff to make a written demand on Defendant.

IV. Conclusion

For the reasons stated above, Defendants’ Joint Motion for Summary Judgment is DENIED and Plaintiffs’ Motion for Leave to Amend Complaint is GRANTED.

ENTERED June 20, 2013.

BY THE COURT:

J. Eric Elliff
District Court Judge
Cannabis Litigation
Issues and Procedure

Presentation by Ryan Espegard
November 4, 2016

Appeals of LCB Decisions

• Governed by the Administrative Procedures Act, RCW 34.05

• RCW 34.05.534 – A petition for judicial review may only be filed after exhausting all administrative remedies available within the agency.
  – Exceptions for rulemaking appeals, where statute states that exhaustion is not required, and where remedies would be patently inadequate, exhaustion would be futile, or grave irreparable harm resulting from exhaustion requirement would outweigh public policy in favor of exhaustion.

• RCW 34.05.413(1) – Agency can commence a proceeding at any time regarding subject matter within its jurisdiction.

• RCW 34.05.416 – Agency must respond to written request for an adjudicative proceeding.
Appeals of LCB Decisions

The Waiting Game:

• Requests acknowledged by the LCB, then forwarded to AG’s Office.

• AG is responsible for requesting a hearing before an Administrative Law Judge (ALJ) at the Office of Administrative Hearings (OAH).

• Assigned ALJ will schedule a prehearing conference.

• Many months can pass before ALJ is assigned.

Appeals of LCB Decisions

OAH Hearing Conduct:

• Informal evidentiary hearing.

• RCW 34.05.452 - Does not strictly adhere to rules of evidence.

• Engage in discovery if needed.

• Briefing allowed when requested.

• Initial Order vs. Final Order
Appeals of LCB Decisions

Judicial Review:
• Petition filed in Superior Court within 30 days of service of the Final Order.
• Must satisfy standing requirements of RCW 34.05.530.
• Review limited to issues and record developed before the agency. RCW 34.05.554 and 558.

Appeals of LCB Decisions

Rulemaking Challenges:
• May immediately seek judicial review.
• May petition LCB to amend or repeal the rule.
• May petition the legislature’s joint administrative rules committee.
• RCW 34.05.330; 570(2); and 630.
Suing the LCB for Damages?

- Public Duty Doctrine – No liability for negligence if duty is owed to the public rather than the individual.
- Special Relationship Exception:
  - Direct contact between public official and injured plaintiff.
  - Express Assurance given by public official to injured plaintiff.
  - Justifiable reliance by plaintiff.
  - Court found City liable to buyer of property who relied on negligent representation about the applicable zoning designation given by City employee.

Illegal Contracts

  - “If a contract is illegal or flows from an illegal act, a court will leave the parties as it finds them.”
- A claim that a contract is illegal is used by a defendant in litigation in attempt to avoid enforcement of the agreement.
- Arizona and Colorado Examples
Oral Agreements

- Oral agreements are dangerously common in the marijuana industry.
- 3 year statute of limitations typically applies. See RCW 4.16.080(3).
- Parol Evidence Rule – Extrinsic evidence may be presented in case of oral agreement, and is likely necessary.
- RCW 25.15.006(7):
  - “‘Limited liability company agreement’ means the agreement, including the agreement as amended or restated, whether oral, implied, in a record, or in any combination, of the member or members of a limited liability company concerning the affairs of the limited liability company and the conduct of its business.

Securities Law Violations

- RCW 21.20.010(2) – “It is unlawful for any person, in connection with the offer, sale or purchase of any security, to directly or indirectly: . . . to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading.

- RCW 21.20.430(1) – “ (1) Any person, who offers or sells a security in violation of any provisions of RCW 21.20.010, 21.20.140 (1) or (2), or 21.20.180 through 21.20.230, is liable to the person buying the security from him or her, who may sue either at law or in equity to recover the consideration paid for the security, together with interest at eight percent per annum from the date of payment, costs, and reasonable attorneys’ fees, less the amount of any income received on the security, upon the tender of the security, or for damages if he or she no longer owns the security. Damages are the amount that would be recoverable upon a tender less (a) the value of the security when the buyer disposed of it and (b) interest at eight percent per annum from the date of disposition.
Arbitration

• Does it solve problems with “illegal contracts?”

• Confidentiality

• Mandatory Arbitration vs. Mutually Agreed Binding Arbitration

• What about discovery?

Product Liability Cases

• RCW 7.72.030
  – A manufacturer is subject to liability if a claimant’s harm was proximately caused by the negligence of the manufacturer in that the product was not reasonably safe as designed or not reasonably safe because adequate warnings or instructions were not provided.

• RCW 7.72.040
  – Product seller is not liable unless the seller is negligent, breaches an express warranty, or makes an intentional misrepresentation.
  – Product seller is liable if manufacturer is insolvent.

• Dram Shop Liability for Retailers?
Landlord/Tenant

- RCW 59.12.030 - Tenant “is guilty of unlawful detainer” when Tenant maintains possession after:
  - Natural termination of the lease.
  - Default in the payment of rent, after properly served notice to pay or vacate (3 days)
  - Breach of other condition or covenant of the lease, after proper notice to cure or vacate (10 days).

- WAC 314-55-135(4) requires notice of eviction.
- WAC 314-55-135(6) – license will be discontinued without a location.

Moratorium Challenges

- Article XI, Sec. 11 of the Washington Constitution grants authority to cities to “make and enforce . . . all such local police, sanitary and other regulations as are not in conflict with general laws.”

- An ordinance is preempted when:
  - Statute occupies the field, leaving no room for concurrent jurisdiction.
  - Ordinance and statute cannot be harmonized.
    - Ex: Ordinance forbids what statute authorizes.
Vested Rights

- Vested Right vs. Legal Non-Conforming Use
- RCW 19.27.095(1) – Completed building permit application for a structure shall be considered under the land use control ordinances in effect at the time of the application.
- RCW 58.17.020 – Subdivision of land will similarly vest rights.
RPC 1.7

CONFLICT OF INTEREST: CURRENT CLIENTS

(a) Except as provided in paragraph (b), a lawyer shall not represent a client if the representation involves a concurrent conflict of interest. A concurrent conflict of interest exists if:

(1) the representation of one client will be directly adverse to another client; or

(2) there is a significant risk that the representation of one or more clients will be materially limited by the lawyer's responsibilities to another client, a former client or a third person or by a personal interest of the lawyer.

(b) Notwithstanding the existence of a concurrent conflict of interest under paragraph (a), a lawyer may represent a client if:

(1) the lawyer reasonably believes that the lawyer will be able to provide competent and diligent representation to each affected client;

(2) the representation is not prohibited by law;

(3) the representation does not involve the assertion of a claim by one client against another client represented by the lawyer in the same litigation or other proceeding before a tribunal; and

(4) each affected client gives informed consent, confirmed in writing (following authorization from the other client to make any required disclosures).

[Originally effective September 1, 1985; amended effective September 1, 1995; September 1, 2006.]

Comment

General Principles

[1] [Washington revision] Loyalty and independent judgment are essential elements in the lawyer's relationship to a client. Concurrent conflicts of interest can arise from the lawyer's responsibilities to another client, a former client or a third person or from the lawyer's own interests. For specific Rules regarding certain concurrent conflicts of interest, see Rule 1.8. For former client conflicts of interest, see Rule 1.9. For conflicts of interest involving prospective clients, see Rule 1.18. For definitions of "informed consent" and "confirmed in writing," see Rule 1.0A(e) and (b).

[Comment [1] amended effective April 14, 2015.]

[2] Resolution of a conflict of interest problem under this Rule requires the lawyer to: 1) clearly identify the client or clients; 2) determine whether a conflict of interest exists; 3) decide whether the representation may be undertaken despite the existence of a conflict, i.e., whether the conflict is consentable; and 4) if so, consult with the clients affected under paragraph (a) and obtain their informed consent, confirmed in writing. The clients affected under paragraph (a) include both of the clients referred to in paragraph (a) (1) and the one or more clients whose representation might be materially limited under paragraph (a) (2).

[3] A conflict of interest may exist before representation is undertaken, in which event the representation must be declined, unless the lawyer obtains the informed consent of each client under the conditions of paragraph (b). To determine whether a conflict of interest exists, a lawyer should adopt reasonable procedures, appropriate for the size and type of firm and practice, to determine in both litigation and non-litigation matters the persons and issues involved. See also Comment to Rule 5.1. Ignorance caused by a failure to institute such procedures will not excuse a lawyer's violation of this Rule. As to whether a client-lawyer relationship exists or, having once been established, is continuing, see Comment to Rule 1.3 and Scope.

[4] If a conflict arises after representation has been undertaken, the lawyer ordinarily must withdraw from the representation, unless the lawyer has obtained the informed consent of the client under the conditions of paragraph (b). See Rule 1.16. Where more than one client is involved, whether the lawyer may continue to represent any of the clients is determined by the lawyer's ability to comply with duties owed to the former client and by the lawyer's ability to represent adequately the remaining client or clients, given the lawyer's duties to the former client. See Rule 1.9. See also Comments [5] and [29].

[5] Unforeseeable developments, such as changes in corporate and other organizational affiliations or the addition or realignment of parties in litigation, might create conflicts in the midst of a representation, as when a company sued by the lawyer on behalf of one client is bought by another client represented by the lawyer in an unrelated matter. Depending on the circumstances, the lawyer may have the option to withdraw from one of the representations in order to avoid the conflict. The lawyer must seek court approval where necessary and take steps to minimize harm to the clients. See Rule 1.16. The lawyer must continue to protect the confidences of the client from whose representation the lawyer has withdrawn. See Rule 1.9(c).

See also Washington Comment [36].

Identifying Conflicts of Interest: Directly Adverse

[6] Loyalty to a current client prohibits undertaking representation directly adverse to that client without that client's informed consent. Thus, absent consent, a lawyer may not act as an advocate in one matter against a person the lawyer represents in some other matter, even when the matters are wholly unrelated. The client as to whom the representation is directly adverse is likely to feel betrayed, and the resulting damage to the client-lawyer relationship is likely to impair the lawyer's ability to represent the client effectively. In addition, the client on whose behalf the adverse representation is undertaken reasonably may fear that the lawyer will pursue that client's case less effectively out of deference to the other client, i.e., that the representation may be materially limited by the lawyer's interest in retaining the current client. Similarly, a directly adverse conflict may arise when a lawyer is required to cross-examine a client who appears as a witness in a lawsuit involving
another client, as when the testimony will be damaging to the client who is represented in the lawsuit. On the other hand, simultaneous representation in unrelated matters of clients whose interests are only economically adverse, such as representation of competing economic enterprises in unrelated litigation, does not ordinarily constitute a conflict of interest and thus may not require consent of the respective clients.

[7] Directly adverse conflicts can also arise in transactional matters. For example, if a lawyer is asked to represent the seller of a business in negotiations with a buyer represented by the lawyer, not in the same transaction but in another, unrelated matter, the lawyer could not undertake the representation without the informed consent of each client.

Identifying Conflicts of Interest: Material Limitation

[8] Even where there is no direct adverseness, a conflict of interest exists if there is a significant risk that a lawyer's ability to consider, recommend or carry out an appropriate course of action for the client will be materially limited. For example, a lawyer asked to represent several individuals seeking to form a joint venture is likely to be materially limited in the lawyer’s ability to recommend or advocate all possible positions that each might take because of the lawyer's duty of loyalty to the others. The conflict in effect forecloses alternatives that would otherwise be available to the client. The mere possibility of subsequent harm does not itself require disclosure and consent. The critical questions are the likelihood that a difference in interests will eventuate and, if it does, whether it will materially interfere with the lawyer's independent professional judgment in considering alternatives or foreclose courses of action that reasonably should be pursued on behalf of the client.

See also Washington Comment [37].

Lawyer’s Responsibilities to Former Clients and Other Third Persons

[9] In addition to conflicts with other current clients, a lawyer’s duties of loyalty and independence may be materially limited by responsibilities to former clients under Rule 1.9 or by the lawyer’s responsibilities to other persons, such as fiduciary duties arising from a lawyer’s service as a trustee, executor or corporate director.

Personal Interest Conflicts

[10] The lawyer’s own interests should not be permitted to have an adverse effect on representation of a client. For example, if the probity of a lawyer’s own conduct in a transaction is in serious question, it may be difficult or impossible for the lawyer to give a client detached advice. Similarly, when a lawyer has discussions concerning possible employment with an opponent of the lawyer's client, or with a law firm representing the opponent, such discussions could materially limit the lawyer's representation of the client. In addition, a lawyer may not allow related business interests to affect representation, for example, by referring clients to an enterprise in which the lawyer has an undisclosed financial interest. See Rule 1.8 for specific Rules pertaining to a number of personal interest conflicts, including business transactions with clients. See also Rule 1.10 (personal interest conflicts under Rule 1.7 ordinarily are not imputed to other lawyers in a law firm).

[11] (Washington revision) When lawyers representing different clients in the same matter or in substantially related matters are related as parent, child, sibling, or spouse, or if the lawyers have some other close familial relationship or if the lawyers are in a personal intimate relationship with one another, there may be a significant risk that client confidences will be revealed and that the lawyer’s family or other familial or intimate relationship will interfere with both loyalty and independent professional judgment. See Rule 1.8(1). As a result, each client is entitled to know of the existence and implications of the relationship between the lawyers before the lawyer agrees to undertake the representation. Thus, a lawyer so related to another lawyer ordinarily may not represent a client in a matter where that lawyer is representing another party, unless each client gives informed consent. The disqualification arising from such relationships is personal and ordinarily is not imputed to members of firms with whom the lawyers are associated. See Rules 1.8(k) and 1.10.

[12] [Reserved.]

Interest of Person Paying for a Lawyer’s Service

[13] A lawyer may be paid from a source other than the client, including a co-client, if the client is informed of that fact and consents and the arrangement does not compromise the lawyer’s duty of loyalty or independent judgment to the client. See Rule 1.8(f). If acceptance of the payment from any other source presents a significant risk that the lawyer's representation of the client will be materially limited by the lawyer's own interest in accommodating the person paying the lawyer’s fee or by the lawyer's responsibilities to a payer who is also a client, then the lawyer must comply with the requirements of paragraph (b) before accepting the representation, including determining whether the conflict is consentable and, if so, that the client has adequate information about the material risks of the representation.

Prohibited Representations

[14] Ordinarily, clients may consent to representation notwithstanding a conflict. However, as indicated in paragraph (b), some conflicts are nonconsentable, meaning that the lawyer involved cannot properly ask for such agreement or provide representation on the basis of the client’s consent. When the lawyer is representing more than one client, the question of consentability must be resolved as to each client.

[15] Consentability is typically determined by considering whether the interests of the clients will be adequately protected if the clients are permitted to give their informed consent to representation burdened by a conflict of interest. Thus, under paragraph (b)(1), representation is prohibited if in the circumstances the lawyer cannot reasonably conclude that the lawyer will be able to provide competent and diligent representation.

See Rule 1.1 (Competence) and Rule 1.3 (Diligence).

[16] [Washington revision] Paragraph (b)(2) describes conflicts that are nonconsentable because the representation is prohibited by applicable law. For example, in some states substantive law provides that the same lawyer may not represent more than one defendant in a capital case, even with the consent of the clients, and under federal criminal statutes certain representations by a former government lawyer are prohibited,
Despite the informed consent of the former client. In addition, decisional law in some states other than Washington limits the ability of a governmental client, such as a municipality, to consent to a conflict of interest. See Washington Comment [38].

[17] [Washington revision] Paragraph (b)(3) describes conflicts that are nonconsentable because of the institutional interest in vigorous development of each client's position when the clients are aligned directly against each other in the same litigation or other proceeding before a tribunal. Whether clients are aligned directly against each other within the meaning of this paragraph requires determination of the context of the proceeding. Although this paragraph does not preclude a lawyer's multiple representation of adverse parties to a mediation (because mediation is not a proceeding before a "tribunal" under Rule 1.0A(m)), such representation may be precluded by paragraph (b)(1).

[Comment [17] amended effective April 14, 2015.]

See also Washington Comment [38].

Informed Consent

[18] [Washington revision] Informed consent requires that each affected client be aware of the relevant circumstances and of the material and reasonably foreseeable ways that the conflict could have adverse effects on the interests of that client. See Rule 1.0A(e) (informed consent). The information required depends on the nature of the conflict and the nature of the risks involved. When representation of multiple clients in a single matter is undertaken, the information must include the implications of the common representation, including possible effects on loyalty, confidentiality and the attorney-client privilege and the advantages and risks involved. See Comments [30] and [31] (effect of common representation on confidentiality).

[Comment [18] amended effective April 15, 2014.]

[19] Under some circumstances it may be impossible to make the disclosure necessary to obtain consent. For example, when the lawyer represents different clients in related matters and one of the clients refuses to consent to the disclosure necessary to permit the other client to make an informed decision, the lawyer cannot properly ask the latter to consent. In some cases the alternative to common representation can be that each party may have to obtain separate representation with the possibility of incurring additional costs. These costs, along with the benefits of securing separate representation, are factors that may be considered by the affected client in determining whether common representation is in the client's interests.

See also Washington Comment [39].

Consent Confirmed in Writing

[20] [Washington revision] Paragraph (b) requires the lawyer to obtain the informed consent of the client, confirmed in writing. Such a writing may consist of a document executed by the client or one that the lawyer promptly records and transmits to the client following an oral consent. See Rule 1.0A(b). See also Rule 1.0A(n) (writing includes electronic transmission). If it is not feasible to obtain or transmit the writing at the time the client gives informed consent, then the lawyer must obtain or transmit it within a reasonable time thereafter. See Rule 1.0A(b). The requirement of a writing does not supplant the need in most cases for the lawyer to talk with the client, to explain the risks and advantages, if any, of representation burdened with a conflict of interest, as well as reasonably available alternatives, and to afford the client a reasonable opportunity to consider the risks and alternatives and to raise questions and concerns. Rather, the writing is required in order to impress upon clients the seriousness of the decision the client is being asked to make and to avoid disputes or ambiguities that might later occur in the absence of a writing.

[Comment [20] amended effective April 15, 2014.]

Revoking Consent

[21] A client who has given consent to a conflict may revoke the consent and, like any other client, may terminate the lawyer's representation at any time. Whether revoking consent to the client's own representation precludes the lawyer from continuing to represent other clients depends on the circumstances, including the nature of the conflict, whether the client revoked consent because of a material change in circumstances, the reasonable expectations of the other client and whether material detriment to the other clients or the lawyer would result.

Consent to Future Conflict

[22] [Reserved.]

Conflicts in Litigation

[23] Paragraph (b)(3) prohibits representation of opposing parties in the same litigation, regardless of the clients' consent. On the other hand, simultaneous representation of parties whose interests in litigation may conflict, such as coplaintiffs or codefendants, is governed by paragraph (a)(2). A conflict may exist by reason of substantial discrepancy in the parties' testimony, incompatibility in positions in relation to an opposing party or the fact that there are substantially different possibilities of settlement of the claims or liabilities in question. Such conflicts can arise in criminal cases as well as civil. The potential for conflict of interest in representing multiple defendants in a criminal case is so grave that ordinarily a lawyer should decline to represent more than one codefendant. On the other hand, common representation of persons having similar interests in civil litigation is proper if the requirements of paragraph (b) are met.

[24] Ordinarily a lawyer may take inconsistent legal positions in different tribunals at different times on behalf of different clients. The mere fact that advocating a legal position on behalf of one client might create precedent adverse to the interests of a client represented by the lawyer in an unrelated matter does not create a conflict of interest. A conflict of interest exists, however, if there is a significant risk that a lawyer's action on behalf of one client will materially limit the lawyer's effectiveness in representing another client in a different case; for example, when a decision favoring one client will create a precedent likely to seriously weaken the
position taken on behalf of the other client. Factors relevant in determining whether the clients need to be advised of the risk include: where the cases are pending, whether the issue is substantive or procedural, the temporal relationship between the matters, the significance of the issue to the immediate and long-term interests of the clients, the potential for material limitation include the duration and intimacy of the lawyer’s relationship with the client or clients involved, the functions being performed by the lawyer, the likelihood that disagreements will arise and the likely prejudice to the client from the conflict. The question is often one of proximity and degree. See Comment [8].

When a lawyer represents or seeks to represent a class of plaintiffs or defendants in a class-action lawsuit, unnamed members of the class are ordinarily not considered to be clients of the lawyer for purposes of applying paragraph (a)(1) of this Rule. Thus, the lawyer does not typically need to get the consent of such a person before representing a client suing the person in an unrelated matter. Similarly, a lawyer seeking to represent an opponent in a class action does not typically need the consent of an unnamed member of the class whom the lawyer represents in an unrelated matter.

Nonlitigation Conflicts

Conflicts of interest under paragraphs (a)(1) and (a)(2) arise in contexts other than litigation. For a discussion of directly adverse conflicts in transactional matters, see Comment [7]. Relevant factors in determining whether there is significant potential for material limitation include the duration and intimacy of the lawyer’s relationship with the client or clients involved, the functions being performed by the lawyer, the likelihood that disagreements will arise and the likely prejudice to the client from the conflict. The question is often one of proximity and degree. See Comment [8].

For example, conflict questions may arise in estate planning and estate administration. A lawyer may be called upon to prepare wills for several family members, such as husband and wife, and, depending upon the circumstances, a conflict of interest may be present. In estate administration the identity of the client may be unclear under the law of a particular jurisdiction. Under one view, the client is the fiduciary; under another view the client is the estate or trust, including its beneficiaries. In order to comply with conflict of interest rules, the lawyer should make clear the lawyer’s relationship to the parties involved.

Whether a conflict is consentable depends on the circumstances. For example, a lawyer may not represent multiple parties to a negotiation whose interests are fundamentally antagonistic to each other, but common representation is permissible where the clients are generally aligned in interest even though there is some difference in interest among them. Thus, a lawyer may seek to establish or adjust a relationship between clients on the assumption that a business in which two or more clients are entrepreneurs, working out the financial reorganization of an enterprise in which two or more clients have an interest or arranging a property distribution in settlement of an estate. The lawyer seeks to resolve potentially adverse interests by developing the parties’ mutual interests. Otherwise, each party might have to obtain separate representation, with the possibility of incurring additional cost, complication or even litigation. Given these and other relevant factors, the clients may prefer that the lawyer act for all of them. See also Washington Comment [40].

Special Considerations in Common Representation

In considering whether to represent multiple clients in the same matter, a lawyer should be mindful that if the common representation fails because the potentially adverse interests cannot be reconciled, the result can be additional cost, embarrassment and recrimination. Ordinarily, the lawyer will be forced to withdraw from representing all of the clients if the common representation fails. In some situations, the risk of failure is so great that multiple representation is plainly impossible. For example, a lawyer cannot undertake common representation of clients where contentious litigation or negotiations between them are imminent or contemplated. Moreover, because the lawyer is required to be impartial between commonly represented clients, representation of multiple clients is improper when it is unlikely that impartiality can be maintained. Generally, if the relationship among the clients becomes antagonistic, the parties’ interests can be adequately served by common representation is not very good. Other relevant factors are whether the lawyer subsequently will represent both parties on a continuing basis and whether the situation involves creating or terminating a relationship between the parties.

A particularly important factor in determining the appropriateness of common representation is the effect on client-lawyer confidentiality and the attorney-client privilege. With regard to the attorney-client privilege, the prevailing rule is that, as between commonly represented clients, the privilege does not attach. Hence, it must be assumed that if litigation eventuates between the clients, the privilege will not protect any such communications, and the clients should be so advised.

As to the duty of confidentiality, continued common representation will almost certainly be inadequate if one client asks the lawyer not to disclose to the other client information relevant to the common representation. This is so because the lawyer has an equal duty of loyalty to each client, and each client has the right to be informed of anything bearing on the representation that might affect that client’s interests and the right to expect that the lawyer will use that information to that client’s benefit. See Rule 1.4. The lawyer should, at the outset of the representation, advise each client that information will be shared and that the lawyer will have to withdraw if one client decides that some matter material to the representation should be kept from the other. In limited circumstances, it may be appropriate for the lawyer to proceed with the representation when the clients have agreed, after being properly informed, that the lawyer will keep certain information confidential. For example, the lawyer may reasonably conclude that failure to disclose one client’s trade secrets to another client will not adversely affect representation involving a joint venture between the clients and agree to keep that information confidential with the informed consent of both clients.

When seeking to establish or adjust a relationship between clients, the lawyer should make clear that the lawyer’s role is not that of partisanship normally expected in other circumstances and, thus, that the clients may be required to assume greater responsibility for decisions than when each client is separately represented. Any limitations on the scope of the representation made necessary as a result of the common representation should be fully explained to the clients at the outset of the representation. See Rule 1.2(c).

Subject to the above limitations, each client in the common representation has the right to loyal and diligent representation and the protection of Rule 1.9 concerning the obligations to a former client. The client also has the right to discharge the lawyer as stated in Rule 1.16.
See also Washington Comment [41].

Organizational Clients

[34] A lawyer who represents a corporation or other organization does not, by virtue of that representation, necessarily represent any constituent or affiliated organization, such as a parent or subsidiary. See Rule 1.13(a). Thus, the lawyer for an organization is not barred from accepting representation adverse to an affiliate in an unrelated matter, unless the circumstances are such that the affiliate should also be considered a client of the lawyer, there is an understanding between the lawyer and the organizational client that the lawyer will avoid representation adverse to the client’s affiliates, or the lawyer’s obligations to either the organizational client or the new client are likely to limit materially the lawyer’s representation of the other client.

[35] A lawyer for a corporation or other organization who is also a member of its board of directors should determine whether the responsibilities of the two roles may conflict. The lawyer may be called on to advise the corporation in matters involving actions of the directors. Consideration should be given to the frequency with which such situations may arise, the potential intensity of the conflict, the effect of the lawyer’s resignation from the board and the possibility of the corporation’s obtaining legal advice from another lawyer in such situations. If there is material risk that the dual role will compromise the lawyer’s independence of professional judgment, the lawyer should not serve as a director or should cease to act as the corporation’s lawyer when conflicts of interest arise. The lawyer should advise the other members of the board that in some circumstances matters discussed at board meetings while the lawyer is present in the capacity of director might not be protected by the attorney-client privilege and that conflict of interest considerations might require the lawyer’s recusal as a director or might require the lawyer and the lawyer’s firm to decline representation of the corporation in a matter.

Additional Washington Comments (36 – 41)

General Principles

[36] Notwithstanding Comment [3], lawyers providing short-term limited legal services to a client under the auspices of a program sponsored by a nonprofit organization or court are not normally required to systematically screen for conflicts of interest before undertaking a representation. See Comment [1] to Rule 6.5. See Rule 1.2(c) for requirements applicable to the provision of limited legal services.

Identifying Conflicts of Interest: Material Limitation

[37] Use of the term “significant risk” in paragraph (a)(2) is not intended to be a substantive change or diminishment in the standard required under former Washington RPC 1.7(b), i.e., that “the representation of the client may be materially limited by the lawyer’s responsibilities to another client or to a third person, or by the lawyer’s own interests.”

Prohibited Representations

[38] In Washington, a governmental client is not prohibited from properly consenting to a representational conflict of interest.

Informed Consent

[39] Paragraph (b)(4) of the Rule differs slightly from the Model Rule in that it expressly requires authorization from the other client before any required disclosure of information relating to that client can be made. Authorization to make a disclosure of information relating to the representation requires the client’s informed consent. See Rule 1.6(a).

Nonlitigation Conflicts

[40] Under Washington case law, in estate administration matters the client is the personal representative of the estate.

Special Considerations in Common Representation

[41] Various legal provisions, including constitutional, statutory and common law, may define the duties of government lawyers in representing public officers, employees, and agencies and should be considered in evaluating the nature and propriety of common representation.

[Comments adopted effective September 1, 2006.]
RPC 1.2
SCOPE OF REPRESENTATION AND ALLOCATION OF AUTHORITY BETWEEN CLIENT AND LAWYER

(a) Subject to paragraphs (c) and (d), a lawyer shall abide by a client’s decisions concerning the objectives of representation and, as required by RPC 1.4, shall consult with the client as to the means by which they are to be pursued. A lawyer may take such action on behalf of the client as is impliedly authorized to carry out the representation. A lawyer shall abide by a client’s decision whether to settle a matter. In a criminal case, the lawyer shall abide by the client’s decision, after consultation with the lawyer, as to a plea to be entered, whether to waive jury trial and whether the client will testify.

(b) A lawyer’s representation of a client, including representation by appointment, does not constitute an endorsement of the client’s political, economic, social or moral views or activities.

(c) A lawyer may limit the scope of the representation if the limitation is reasonable under the circumstances and the client gives informed consent.

(d) A lawyer shall not counsel a client to engage, or assist a client, in conduct that the lawyer knows is criminal or fraudulent, but a lawyer may discuss the legal consequences of any proposed course of conduct with a client and may counsel or assist a client to make a good faith effort to determine the validity, scope, meaning or application of the law.

(e) [Reserved.]

(f) A lawyer shall not purport to act as a lawyer for any person or organization if the lawyer knows or reasonably should know that the lawyer is acting without the authority of that person or organization, unless the lawyer is authorized or required to so act by law or a court order.

[Originally effective September 1, 1985; amended effective October 1, 2002; October 29, 2002; September 1, 2006; September 1, 2011.]

Comment

Allocation of Authority between Client and Lawyer

[1] [Washington revision] Paragraph (a) confers upon the client the ultimate authority to determine the purposes to be served by legal representation, within the limits imposed by law and the lawyer’s professional obligations. The decisions specified in paragraph (a), such as whether to settle a civil matter, must also be made by the client. See RPC 1.4(a)(1) for the lawyer’s duty to communicate with the client about such decisions. With respect to the means by which the client’s objectives are to be pursued, the lawyer shall consult with the client as required by RPC 1.4(a)(2) and may take such action as is impliedly authorized to carry out the representation. See also RPC 1.1, comments [6] and [10] as to decisions to associate other lawyers or LLLTs.

[Comment 1 amended effective September 1, 2016.]

[2] On occasion, however, a lawyer and a client may disagree about the means to be used to accomplish the client’s objectives. Clients normally defer to the special knowledge and skill of their lawyer with respect to the means to be used to accomplish their objectives, particularly with respect to technical, legal and tactical matters. Conversely, lawyers usually defer to the client regarding such questions as the expense to be incurred and concern for third persons who might be adversely affected. Because of the varied nature of the matters about which a lawyer and client might disagree and because the actions in question may implicate the interests of a tribunal or other persons, this Rule does not prescribe how such disagreements are to be resolved. Other law, however, may be applicable and should be consulted by the lawyer. The lawyer should also consult with the client and seek a mutually acceptable resolution of the disagreement. If such efforts are unavailing and the lawyer has a fundamental disagreement with the client, the lawyer may withdraw from the representation. See Rule 1.16(b)(4). Conversely, the client may resolve the disagreement by discharging the lawyer. See Rule 1.16(a)(3).

[3] At the outset of a representation, the client may authorize the lawyer to take specific action on the client’s behalf without further consultation. Absent a material change in circumstances and subject to Rule 1.4, a lawyer may rely on such an advance authorization. The client may, however, revoke such authority at any time.

[4] In a case in which the client appears to be suffering diminished capacity, the lawyer’s duty to abide by the client’s decisions is to be guided by reference to Rule 1.14.

Independence from Client’s Views or Activities

[5] Legal representation should not be denied to people who are unable to afford legal services, or whose cause is controversial or the subject of popular disapproval. By the same token, representing a client does not constitute approval of the client’s views or activities.

Agreements Limiting Scope of Representation

[6] The scope of services to be provided by a lawyer may be limited by agreement with the client or by the terms under which the lawyer’s services are made available to the client. When a lawyer has been retained by an insurer to represent an insured, for example, the representation may be limited to matters related to the insurance coverage. A limited representation may be appropriate because the client has limited objectives for the representation. In addition, the terms upon which representation is undertaken may exclude specific means that might otherwise be used to accomplish the client’s objectives. Such limitations may exclude actions that the client thinks are too costly or that the lawyer regards as repugnant or imprudent.
[7] Although this Rule affords the lawyer and client substantial latitude to limit the representation, the limitation must be reasonable under the circumstances. If, for example, a client's objective is limited to securing general information about the law the client needs in order to handle a common and typically uncomplicated legal problem, the lawyer and client may agree that the lawyer's services will be limited to a brief telephone consultation. Such a limitation, however, would not be reasonable if the time allotted was not sufficient to yield advice upon which the client could rely. Although an agreement for a limited representation does not exempt a lawyer from the duty to provide competent representation, however, it is a factor to be considered when determining the legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation. See Rule 1.1.  

See also Washington Comment [14].

Criminal, Fraudulent and Prohibited Transactions

[9] Paragraph (d) prohibits a lawyer from knowingly counseling or assisting a client to commit a crime or fraud. This prohibition, however, does not preclude the lawyer from giving an honest opinion about the actual consequences that appear likely to result from a client's conduct. Nor does the fact that a client uses advice in a course of action that is criminal or fraudulent of itself make a lawyer a party to the course of action. There is a critical distinction between presenting an analysis of legal aspects of questionable conduct and recommending the means by which a crime or fraud might be committed with impunity.  

[10] When the client's course of action has already begun and is continuing, the lawyer's responsibility is especially delicate. The lawyer is required to avoid assisting the client, for example, by drafting or delivering documents that the lawyer knows are fraudulent or by suggesting how the wrongdoing might be concealed. A lawyer may not continue assisting a client in conduct that the lawyer originally supposed was legally proper but then discovers is criminal or fraudulent. The lawyer must, therefore, withdraw from the representation of the client in the matter. See Rule 1.16(a). In some cases, withdrawal alone might be insufficient. It may be necessary for the lawyer to give notice of the fact of withdrawal and to disaffirm any opinion, document, affirmation or the like. See Rule 4.1.  

[11] Where the client is a fiduciary, the lawyer may be charged with special obligations in dealings with a beneficiary.  

[12] Paragraph (d) applies whether or not the defrauded party is a party to the transaction. Hence, a lawyer must not participate in a transaction to effectuate criminal or fraudulent avoidance of tax liability. Paragraph (d) does not preclude undertaking a criminal defense incident to a general retainer for legal services to a lawful enterprise. The last clause of paragraph (d) recognizes that determining the validity or interpretation of a statute or regulation may require a course of action involving disobedience of the statute or regulation or of the interpretation placed upon it by governmental authorities.

[13] If a lawyer comes to know or reasonably should know that a client expects assistance not permitted by the Rules of Professional Conduct or other law or if the lawyer intends to act contrary to the client's instructions, the lawyer must consult with the client regarding the limitations on the lawyer's conduct. See Rule 1.4(a)(5).  

Additional Washington Comments (14-17)

Agreements Limiting Scope of Representation

[14] An agreement limiting the scope of a representation shall consider the applicability of Rule 4.2 to the representation. (The provisions of this Comment were taken from former Washington RPC 1.2(c).) See also Comment [11] to Rule 4.2 for specific considerations pertaining to contact with a person otherwise represented by a lawyer to whom limited representation is being or has been provided.  
[Comment [14] amended effective April 14, 2015.]  
[Comments originally effective September 1, 2006.]  

Acting as a Lawyer Without Authority

[15] Paragraph (f) was taken from former Washington RPC 1.2(f), which was deleted from the RPC by amendment effective September 1, 2006. The word "state" has been changed from "willfully" to one of knowledge or constructive knowledge. See Rule 1.0A(f) & (j). Although the language and structure of paragraph (f) differ from the former version in a number of other respects, paragraph (f) does not otherwise represent a change in Washington law interpreting former RPC 1.2(f).  
[Comment [15] adopted effective September 1, 2011.]  

[16] If a lawyer is unsure of the extent of his or her authority to represent a person because of that person's diminished capacity, paragraph (f) of this Rule does not prohibit the lawyer from taking action in accordance with Rule 1.14 to protect the person's interests. Protective action does not constitute a violation of this Rule.  
[Comment [15] adopted effective September 1, 2011.]  

[17] Paragraph (f) does not prohibit a lawyer from taking any action permitted or required by these Rules, court rules, or other law when withdrawing from a representation, when terminated by a client, or when ordered to
continue representation by a tribunal. See Rule 1.16(c).

[Comment [15] adopted effective September 1, 2011.]

Special Circumstances Presented by Washington Initiative 502 (Laws of 2013, ch. 3)

[18] At least until there is a change in federal enforcement policy, a lawyer may counsel a client regarding the validity, scope and meaning of Washington Initiative 502 (Laws of 2013, ch. 3) and may assist a client in conduct that the lawyer reasonably believes is permitted by this statute and the other statutes, regulations, orders, and other state and local provisions implementing them.

[Comment [18] adopted effective December 9, 2014.]
IN THE SUPREME COURT OF THE STATE OF HAWAI‘I

In the Matter of the

HAWAI‘I RULES OF PROFESSIONAL CONDUCT

ORDER AMENDING RULE 1.2(d) OF THE HAWAI‘I RULES OF PROFESSIONAL CONDUCT
(By: Recktenwald, C.J., Nakayama, McKenna, Pollack, and Wilson, JJ.)

IT IS HEREBY ORDERED that Rule 1.2(d) of the Hawai‘i Rules of Professional Conduct, is amended, effective as of the filing of this order, as follows (new material is underscored):

Rule 1.2. SCOPE OF REPRESENTATION AND ALLOCATION OF AUTHORITY BETWEEN CLIENT AND LAWYER.

(d) A lawyer shall not counsel a client to engage, or assist a client, in conduct that the lawyer knows is criminal or fraudulent, but a lawyer may discuss the legal consequences of any proposed course of conduct with a client and may counsel or assist a client to make a good faith effort to determine the validity, scope, meaning, or application of the law, and may counsel or assist a client regarding conduct expressly permitted by Hawai‘i law, provided that the
lawyer counsels the client about the legal consequences, under other applicable
law, of the client’s proposed course of conduct.

***

DATED: Honolulu, Hawai‘i, October 20, 2015.

/s/ Mark E. Recktenwald
/s/ Paula A. Nakayama
/s/ Sabrina S. McKenna
/s/ Richard W. Pollack
/s/ Michael D. Wilson
Rule 1.2. Scope of Representation and Allocation of Authority Between Client and Lawyer.

Colo. RPC 1.2(2012)
Rule 1.2 — Scope of Representation and Allocation of Authority Between Client and Lawyer

**Reflects changes received through March 24, 2014**

(a) Subject to paragraphs (c) and (d), a lawyer shall abide by a client's decisions concerning the objectives of representation and, as required by Rule 1.4, shall consult with the client as to the means by which they are to be pursued. A lawyer may take such action on behalf of the client as is impliedly authorized to carry out the representation. A lawyer shall abide by a client's decision whether to settle a matter. In a criminal case, the lawyer shall abide by the client's decision, after consultation with the lawyer, as to a plea to be entered, whether to waive jury trial and whether the client will testify.

(b) A lawyer's representation of a client, including representation by appointment, does not constitute an endorsement of the client's political, economic, social or moral views or activities.

(c) A lawyer may limit the scope or objectives, or both, of the representation if the limitation is reasonable under the circumstances and the client gives informed consent. A lawyer may provide limited representation to pro se parties as permitted by C.R.C.P. 11(b) and C.R.C.P. 311(b).

(d) A lawyer shall not counsel a client to engage, or assist a client, in conduct that the lawyer knows is criminal or fraudulent, but a lawyer may discuss the legal consequences of any proposed course of conduct with a client and may counsel or assist a client to make a good faith effort to determine the validity, scope, meaning or application of the law.

Source: (a), (c), and comment amended and adopted June 17, 1999, effective July 1, 1999; entire Appendix repealed and readopted April 12, 2007, effective January 1, 2008.

COMMENT

Allocation of Authority between Client and Lawyer

[1] Paragraph (a) confers upon the client the ultimate authority to determine the purposes to be served by legal representation, within the limits imposed by law and the lawyer's professional obligations. The decisions specified in paragraph (a), such as whether to settle a civil matter, must also be made by the client. See Rule 1.4(a)(1) for the lawyer's duty to communicate with the client about such decisions. With respect to the means by which the client's objectives are to be pursued, the lawyer shall consult with the client as required by Rule 1.4(a)(2) and may take such action as is impliedly authorized to carry out the representation.
[2] On occasion, however, a lawyer and a client may disagree about the means to be used to accomplish the client's objectives. Clients normally defer to the special knowledge and skill of their lawyer with respect to the means to be used to accomplish their objectives, particularly with respect to technical, legal and tactical matters. Conversely, lawyers usually defer to the client regarding such questions as the expense to be incurred and concern for third persons who might be adversely affected. Because of the varied nature of the matters about which a lawyer and client might disagree and because the actions in question may implicate the interests of a tribunal or other persons, this Rule does not prescribe how such disagreements are to be resolved. Other law, however, may be applicable and should be consulted by the lawyer. The lawyer should also consult with the client and seek a mutually acceptable resolution of the disagreement. If such efforts are unavailing and the lawyer has a fundamental disagreement with the client, the lawyer may withdraw from the representation. See Rule 1.16(b)(4). Conversely, the client may resolve the disagreement by discharging the lawyer. See Rule 1.16(a)(3).

[3] At the outset of a representation, the client may authorize the lawyer to take specific action on the client's behalf without further consultation. Absent a material change in circumstances and subject to Rule 1.4, a lawyer may rely on such an advance authorization. The client may, however, revoke such authority at any time.

[4] In a case in which the client appears to be suffering diminished capacity, the lawyer's duty to abide by the client's decisions is to be guided by reference to Rule 1.14

Independence from Client's Views or Activities

[5] Legal representation should not be denied to people who are unable to afford legal services, or whose cause is controversial or the subject of popular disapproval. By the same token, representing a client does not constitute approval of the client's views or activities.

Agreements Limiting Scope of Representation

[6] The scope of services to be provided by a lawyer may be limited by agreement with the client or by the terms under which the lawyer's services are made available to the client. When a lawyer has been retained by an insurer to represent an insured, for example, the representation may be limited to matters related to the insurance coverage. A limited representation may be appropriate because the client has limited objectives for the representation. In addition, the terms upon which representation is undertaken may exclude specific means that might otherwise be used to accomplish the client's objectives. Such limitations may exclude actions that the client thinks are too costly or that the lawyer regards as repugnant or imprudent.

[7] Although this Rule affords the lawyer and client substantial latitude to limit the representation, the limitation must be reasonable under the circumstances. If, for example, a client's objective is limited to securing general information about the law the client needs in order to handle a common and typically uncomplicated legal problem, the lawyer and client may agree that the lawyer's services will be limited to a brief telephone consultation. Such a limitation, however, would not be reasonable if the time allotted was not sufficient to yield advice upon which the client could rely. Although an agreement for a limited representation does not exempt a lawyer from the duty to provide competent representation, the limitation is a factor to be considered when determining the legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation. See Rule 1.1.

[8] All agreements concerning a lawyer's representation of a client must accord with the Rules of Professional Conduct and other law. See, e.g., Rules 1.1, 1.8 and 5.6

Criminal, Fraudulent and Prohibited Transactions

[9] Paragraph (d) prohibits a lawyer from knowingly counseling or assisting a client to commit a crime or fraud. This prohibition, however, does not preclude the lawyer from giving an honest opinion about the actual consequences that appear likely to result from a client's conduct. Nor does the fact that a client uses advice in a course of action that is criminal or fraudulent of itself make a lawyer a party to the course of action. There is a critical distinction between presenting an analysis of legal aspects of questionable conduct and recommending the means by which a crime or fraud might be committed with impunity.
When the client's course of action has already begun and is continuing, the lawyer's responsibility is especially delicate. The lawyer is required to avoid assisting the client, for example, by drafting or delivering documents that the lawyer knows are fraudulent or by suggesting how the wrongdoing might be concealed. A lawyer may not continue assisting a client in conduct that the lawyer originally supposed was legally proper but then discovers is criminal or fraudulent. The lawyer must, therefore, withdraw from the representation of the client in the matter. See Rule 1.16(a). In some cases, withdrawal alone might be insufficient. It may be necessary for the lawyer to give notice of the fact of withdrawal and to disaffirm any opinion, document, affirmation or the like. See Rule 4.1.

Where the client is a fiduciary, the lawyer may be charged with special obligations in dealings with a beneficiary. Paragraph (d) applies whether or not the defrauded party is a party to the transaction. Hence, a lawyer must not participate in a transaction to effectuate criminal or fraudulent avoidance of tax liability. Paragraph (d) does not preclude undertaking a criminal defense incident to a general retainer for legal services to a lawful enterprise. The last clause of paragraph (d) recognizes that determining the validity or interpretation of a statute or regulation may require a course of action involving disobedience of the statute or regulation or of the interpretation placed upon it by governmental authorities.

If a lawyer comes to know or reasonably should know that a client expects assistance not permitted by the Rules of Professional Conduct or other law or if the lawyer intends to act contrary to the client's instructions, the lawyer must consult with the client regarding the limitations on the lawyer's conduct. See Rule 1.4(a)(5).

A lawyer may counsel a client regarding the validity, scope, and meaning of Colorado constitution article XVIII, secs. 14 & 16, and may assist a client in conduct that the lawyer reasonably believes is permitted by these constitutional provisions and the statutes, regulations, orders, and other state or local provisions implementing them. In these circumstances, the lawyer shall also advise the client regarding related federal law and policy.