

**UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF COLORADO**

In re:)	
)	Case No. 20-12689 JGR
UC COLORADO CORPORATION,)	
)	Chapter 11
Debtor.)	(Request for Joint Administration Pending)

In re:)	
)	Case No. 20-12692 JGR
UNITED CANNABIS CORPORATION,)	
)	Chapter 11
Debtor.)	

DEBTORS’ RESPONSE TO ORDERS TO SHOW CAUSE

UC Colorado Corporation (“UC Colorado”) and United Cannabis Corporation (“UCANN” and together with UC Colorado, the “Debtors”), debtors-in-possession, by and through counsel Wadsworth Garber Warner Conrardy, P.C., respectfully respond to the Court’s Orders to Show Cause, and in support thereof state as follows:

INTRODUCTION

1. Courts that have weighed in on marijuana-related bankruptcy cases focus their inquiry on whether the debtor will be using marijuana-derived income to fund a plan of reorganization. That inquiry is straightforward in this case. Neither UC Colorado nor UCANN are in the marijuana business. To the contrary, all of the Debtors’ current operations relate to, and all revenues are solely derived from, the sale of legal CBD products that are made using CBD that is extracted from legal industrial hemp plants, which was legalized by the 2018 Agricultural Improvement Act, also known as the 2018 Farm Bill. No portion of the Debtors’ business violates the Controlled Substances Act, no portion of the Debtors’ current or future revenue is, or will be, derived from an illegal activity, and no portion of the Debtors’ plans of reorganization will rely in any way on income derived from criminal activity in violation of the Controlled Substances Act.

2. UC Colorado and UCANN are dedicated to the development, production, and distribution of legal industrial hemp-based therapeutics that contain CBD and that are designed to increase the quality of life for patients. Each entity serves a separate and distinct purpose. UC Colorado’s sole business purpose is the operation of extraction facilities that convert components of the legal industrial hemp flower into finished CBD products. UC Colorado’s extraction, testing and refinement facilities are located in the Denver metropolitan area and in Mead, Colorado. UC Colorado is a wholly owned subsidiary of UCANN.

3. Unlike UC Colorado, UCANN does not engage in operations. UCANN's assets consist of valid and enforceable patents under the patent laws of the United States that claim liquid cannabinoid formulations and licenses relating thereto that do not generate royalties. Additional assets of UCANN include a handful of subsidiaries that are currently not producing revenues, not operational or never have been operational, and shares in a publicly traded Canadian company.

4. Debtors' bankruptcy filings were precipitated by three significant events. First, a dramatic decline in the price of CBD in November 2019. Second, the spread of COVID-19 struck a major blow to the global economy resulting in reduced sales of CBD, industrial hemp and products made from industrial hemp. Third, in the week preceding the Debtors' bankruptcy filings, a creditor, Miner's Delight, LLC, commenced *ex parte* pre-judgment writ of attachment proceedings in the District Court for Jefferson County, Colorado, the execution of which would have resulted in the complete cessation of operations to the detriment of the creditor body and significant, if not complete, loss of jobs.

5. The first two events resulted in significant job losses. Prior to November 2019, UC Colorado had 150 employees. By the end of November 2019, following the crash of CBD prices, it laid off 57 employees, bringing the total number to 93. The ongoing depressed CBD prices and COVID-19 led to further layoffs. UC Colorado currently employs 40 people.

BACKGROUND

I. Procedural History

6. On April 20, 2020 (the "Petition Date"), each of the Debtors filed a voluntary petition for relief under chapter 11 of title 11 of the United States Code (the "Bankruptcy Code"). The Debtors are continuing in possession of their property and are operating and managing their business and affairs as debtors-in-possession pursuant to sections 1107 and 1108 of the Bankruptcy Code.

7. No trustee, examiner or official committee of unsecured creditors has been appointed in these cases.

8. Both cases were filed on an emergent basis to prevent creditor Miner's Delight, LLC from executing an *ex parte* prejudgment writ of attachment, the execution of which would have resulted in the complete cessation of operations. Due to the emergent nature of the filings, the Debtors' filings were deficient, and the deficiencies had to be cured on or before May 4, 2020. The deficient filings have been timely cured in both cases.

9. On April 22, 2020, the Court entered orders in both cases requiring each of the Debtors and the United States Trustee (the "UST") to show cause in writing on or before May 4, 2020 why their cases should not be dismissed because the Court believes the Debtors may be engaged in the marijuana industry.

10. On April 29, 2020, the Debtors filed Unopposed Motions to Extend Time to Respond to Order to Show Cause (the "Motions to Extend"), requesting a short extension of the

deadline to respond to the Court's Orders to Show Cause to enable them to first focus on curing the deficiencies in their filings.

11. On April 29, 2020, Miner's Delight, LLC, filed a Reservation of Rights with respect to the Motion, but did not oppose the relief sought therein.

12. On April 30, 2020, the Court entered an order granting the Motions to Extend, thereby extending the deadline for the Debtors, the UST, and Ambria Investors LP to file responses to the Orders to Show Cause from May 4, 2020 to May 11, 2020.

II. Debtors' Operations

A. Debtors' Revenues and Operations Exclusively Relate to Legal Industrial Hemp

13. The Debtors' primary business is the operation of extraction facilities that convert components of industrial hemp flower into finished cannabidiol ("CBD") products. CBD, the second most prevalent of the active ingredients of cannabis, is derived directly from the hemp plant, which is a cousin of the marijuana plant. Peter Grinspoon, MD, *Cannabidiol (CBD) — what we know and what we don't*, HARVARD HEALTH PUBLISHING, HARVARD MEDICAL SCHOOL, (Aug. 24, 2018, 6:30 AM), <https://www.health.harvard.edu/blog/cannabidiol-cbd-what-we-know-and-what-we-dont-2018082414476>. The Debtors' products are derived from legal industrial hemp with a delta-9 tetrahydrocannabinol ("THC") concentration of not more than 0.3 percent on a dry weight basis. All of the Debtors' current revenues are derived from the sale of legal CBD products that were made from legal industrial hemp plants.

14. "Botanically, hemp and marijuana are from the same species of the plant, *Cannabis sativa*, but from different varieties or cultivars. However, hemp and marijuana are genetically distinct forms of cannabis that are distinguished by their use and chemical composition as well as by differing cultivation practices in their production." RENÉE JOHNSON, CONG. RESEARCH SERV., R44742, *DEFINING HEMP: A FACT SHEET 1* (2019). The Debtors do not grow, distribute, sell or knowingly purchase any marijuana plants or products; their business is strictly dedicated to the development, production, and distribution of targeted legal industrial hemp-based therapeutics designed to improve the quality of life for patients that suffer from a number of conditions. The Debtors' hemp-based products include therapeutics to supplement deficiencies related to the endocannabinoid system, including pain, neuropathy, arthritis, MS, IBS, autism, seizures, eczema, sleep, anxiety, head trauma, opioid dependency, and clinical endocannabinoid deficiencies, as well as products that provide targeted and large surface relief with combinations of aromatherapy. The Debtors also develop therapeutics for the management of the negative side effects of chemotherapy, management of rheumatoid arthritis, and treatment of brain cancer.¹

¹ The Debtors are careful to abide by current FDA rules prohibiting product claims. Accordingly, these statements, and similar statements herein, are made solely for the exclusive use of the Court in resolving the Orders to Show Cause.

B. Debtors' Assets and Corporate Structure

15. UC Colorado operates a state-of-the-art extraction facility, a testing facility, and a refinement lab, where components of industrial hemp flower are converted into finished CBD products. UC Colorado purchases industrial hemp flower from independent third-party farmers located throughout the continental United States.

16. UCANN has no substantive operations and is similar to a holding company. UCANN is the sole owner of UC Colorado. In addition to its ownership interest in UC Colorado, UCANN also has interests in the following subsidiaries:

- a. 95% interest in Prana Therapeutics, Inc. ("Prana"). Prana's primary asset is the therapeutic supplement Epidiferphane. Importantly, Epidiferphane does not contain any cannabis at all—neither extracts from legal industrial hemp nor marijuana. Epidiferphane is a natural therapeutic supplement that consists of a turmeric extract, a tea extract and compounds from cruciferous vegetables. Epidiferphane is used for the management of the negative side effects of chemotherapy, management of rheumatoid arthritis, and treatment of brain cancer. Prana licensed the use of Epidiferphane to NutriMed, LLC and Advesa, Inc. The Advesa, Inc. license agreement was terminated effective January 1, 2019. No revenues are currently being generated from the NutriMed, LLC license. Prana does not currently generate revenues for UCANN.
- b. The following subsidiaries either have never conducted business or are inactive:
 - i. 100% interest in UCANN California Corporation. UCANN California Corporation has not generated revenue since 2017 and has been inactive since 2019; and
 - ii. 100% interest in UC Oregon Corporation and 85% interest in Tennessee Extractions, LLC. Both of these entities were formed to perform hemp extraction in Oregon and Tennessee, respectively. However, neither have ever conducted business.
- c. UCANN participates in three joint ventures, the purpose of each is to carry on the business of making CBD distillate and isolate from legal industrial hemp:
 - i. Joint venture with Blue Water Green Bridge for extraction of CBD from legal industrial hemp in South Carolina;
 - ii. Joint venture with Slainte Operations, LLC for extraction of CBD from legal industrial hemp in Illinois; and
 - iii. Joint venture with Silver Point Holdings, LLC for extraction of CBD from legal industrial hemp in Tennessee.

17. Property of UCANN includes US Patent 9,730,911 B2 (“911 Patent”). The 911 Patent is valid and enforceable under the patent laws of the United States, 35 U.S.C. § 1, *et seq.* The 911 Patent claims various liquid cannabinoid formulations that contain the non-psychoactive cannabinoid, CBD, among other cannabinoids. The formulations are useful in alleviating the symptoms of chronic pain, paralysis, neuropathy, Crohn’s Disease, IBS, glaucoma, PTSD, anxiety, seizures, epilepsy, autoimmune disorders, autism, tumors and cancer.

18. The 911 Patent is subject to several licenses. All of the licensees are in default for failure to pay royalties. UCANN has not received any royalties since 2017 and will be filing a motion to reject the license agreements pursuant to 11 U.S.C. § 365(a). UCANN currently derives no revenues from the 911 Patent.

19. UCANN owns 87,000 shares of WeedMD, Inc. (“WeedMD”). WeedMD is a Canadian company that produces medical marijuana in compliance with Canada’s Cannabis Act. WeedMD is publicly traded over the counter in the United States, ticker OTCMKTS: WDDMF. As of the date of this response, the value of these shares is approximately \$25,230.00, which accounts for less than 0.6% of the total value of the Debtors’ assets assuming a value of at least \$4,000,000. UCANN is a passive investor in WeedMD. It has never participated in operations or received dividends. UCANN’s WeedMD shares are not necessary to an effective plan of reorganization because they do not generate any revenue and thus no revenue from these shares will be used to fund the Debtors’ plans of reorganization.

ARGUMENT AND AUTHORITIES

20. The Court’s Order to Show Cause finds that “Debtor appears to be engaged in the marijuana industry,” which is illegal under federal law. The Court ordered that the Debtor and the UST show cause why this case should not be dismissed, since the Court “cannot be asked to enforce the protections of the Bankruptcy Code in aid of a Debtor whose activities constitute a continuing federal crime.” For the reasons discussed below, no cause exists to dismiss these cases because the Debtors are not engaged in business that violates the Controlled Substances Act, 28 U.S.C. § 801, *et seq.* (the “CSA”).

I. Evolution of the Definition of Marijuana under The Controlled Substances Act and the De-Criminalization of Hemp

21. The CSA makes it a federal offense, punishable by fines and imprisonment, to manufacture, distribute, or dispense marijuana, or to possess marijuana with the intent to do the same. *See* 21 U.S.C. §§ 812, 841. As enacted, the CSA categorized all forms of cannabis, including marijuana and industrial hemp, as Schedule I drugs, including them in the same category as heroin. *See* 21 U.S.C. § 812. The CSA expressed a Congressional finding that Schedule I substances have a high potential for abuse and no current accepted medical use in treatment in the United States, and that there is a lack of accepted safety for their use under medical supervision. 21 U.S.C. § 812(b)(1).

22. Restrictions on hemp production in the United States were first relaxed as a result

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