

# Decision Blocks Ch. 13 Bankruptcy for Cannabis Business Employee

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## How close can you get to a cannabis business before the doors of bankruptcy close?

If you work for a cannabis business, then bankruptcy relief may not be available to you, according to the *In re Blumsack* decision out of the U.S. Bankruptcy Court for the District of Massachusetts<sup>1</sup>. Whether an employee works for the Sinaloa Cartel or Bud's Buds<sup>2</sup>, that employment involves the cultivation, manufacture, possession, and/or distribution of a controlled substance in violation of federal law. Therefore, according to this decision, the employee's W-2 income is tainted with that illegality and cannot be used fund payments under a bankruptcy plan.

Numerous widely known bankruptcy court decisions prevent cannabis businesses and related entities from availing themselves of the reorganization provisions under chapter 11 of the Bankruptcy Code<sup>3</sup>. The results of these cases have left cannabis and ancillary companies in uncertain legal territory, having no clear rule addressing "how close one can go" to a state-legal marijuana business and still have access to bankruptcy protections. But, unlike the debtor in *In re Blumsack*, businesses have [alternatives under state law](#) that, while not as attractive as chapter 11, are serviceable in many instances.<sup>4</sup>

What is new about the recent decision in *In re Blumsack* is that the bankruptcy court door was closed to an individual who derives income from a cannabis business. In *Blumsack*, the court found that the debtor, a manager of a marijuana dispensary legal under Massachusetts law with no ownership interest in the business, was engaged in activities that violated federal criminal laws.<sup>5</sup> The court found that his employment included: distributing and possessing cannabis with intent to distribute; possessing a controlled substance without a prescription; aiding and abetting his employer in the unlawful distribution and possession of cannabis with intent to distribute; and conspiracy to commit the crimes of distribution and possession of cannabis with the intent to distribute.

Chapter 13 bankruptcies, and chapter 11 cases for high-income/high-net-worth individuals, are most often used by people who want to save their homes from foreclosure. If they get into financial distress, they file chapter 13 or chapter 11 reorganization cases rather than chapter 7 liquidation cases. In this case, the court decided these protections from foreclosure were not available to the debtor – in essence, potentially causing the debtor to lose his home. Had he been employed by any other state-legal business, he would not have suffered this risk.

The debtor in *Blumsack* argued that denying him the right to remain in his chapter 13 case defeats the reason for consumer bankruptcy: allowing individuals to reorganize their financial affairs and gain a "fresh start" on their financial lives. He pointed out that any employee of a marijuana-involved business – including even a warehouse attendant who stacks boxes or a web designer – is committing a crime. Further, the debtor argued that, given the marijuana industry's contribution to a wide spectrum of the Massachusetts economy, an adverse

decision in his case would render a large swath of the community – including the janitorial agency that cleans a dispensary, a pizza shop where dispensary employees get their lunch, Federal Express that delivers packages for a dispensary, the electric utility company, public schools, and perhaps even 2.3 million Walmart employees – ineligible for bankruptcy relief because they derive an economic benefit from marijuana-related businesses.

The court was unpersuaded by the debtor’s arguments. The court disregarded the debtor’s “slippery slope” and policy arguments by noting that it was deciding only the single case before it.

The U.S. Supreme Court has admonished the bankruptcy courts to enforce the text of the Bankruptcy Code according to its plain meaning.<sup>6</sup> Chapter 13 of the Bankruptcy Code requires a debtor’s plan to be proposed “in good faith and not by any means forbidden by law”.<sup>7</sup> The court found that debtor’s plan in this case would be funded by, and would require the Chapter 13 Trustee to administer, wages derived from illegal activities. Therefore, the court found that the plan failed the § 1325(a)(3) requirement and confirmation was denied.

Going further, the court also found that the debtor could not seek the benefits and protections of federal bankruptcy laws while continuously and contemporaneously undertaking and earning income from actions that violate federal criminal laws. The court, therefore, granted the United States Trustee’s motion to dismiss the bankruptcy case for cause.<sup>8</sup>

Finally, the court found that it would be an abuse of process to permit the debtor to obtain the protections and benefits of the federal bankruptcy laws while continuing to commit federal crimes. Because this constitutes an abuse of the bankruptcy process, the court held this was an additional ground for dismissal.<sup>9</sup>

The policy arguments made by the debtor may be very well taken. However, it will remain to future cases outside of Massachusetts to agree or disagree with the *Blumsack* court and to decide the seminal question of “how close can one go?” to a cannabis business before the doors to the bankruptcy court are closed to you. We suspect there will be many more such cases decided in the immediate future which will begin to answer that question. Should future courts answer this question utilizing the reasoning employed by the court in *In re Blumsack*, however, even a small dollar amount received by an individual through legitimate dealings with a state-legal cannabis business could taint that person’s entire income with illegality, and bar the bankruptcy court door.

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[1] *In re Blumsack*, 2023 WL 214293, 2023 Bankr. LEXIS 108 (Bankr.D.Mass. Jan. 17, 2023).

[2] Bud’s Buds was a fictional marijuana dispensary on the television show “Last Man Standing.” See [https://lastmanstanding.fandom.com/wiki/Bud%27s\\_Buds](https://lastmanstanding.fandom.com/wiki/Bud%27s_Buds)

[3] See, e.g., *In re Burton*, 610 B.R. 633, 637-38(9<sup>th</sup> Cir. BAP 2020); *In re Basrah Custom Design, Inc.*, 600 B.R. 368, 382-83 (Bankr. E.D. Mich. 2019; cf. *Garvin v. Cook Investments NW, SPNWY, LLC*, 922 F.3d 1031 (9<sup>th</sup> Cir. 2019)).

[4] Heidi Urness and Timothy Byrd, Pot Cos. Can Rely on State Law for Bankruptcy Safeguards (available at <https://www.law360.com/articles/1531461/pot-cos-can-rely-on-state-law-for-bankruptcy-safeguards>)

[5] 2023 WL 214293 at \*5-7.

[6] *See, e.g., Hartford Underwriters Ins. Co. v. Union Planters Bank, N.A.*, 530 U.S. 1, 6 (2000); *U.S. v. Ron Pair Enterprises, Inc.*, 489 U.S. 235, 242 (1989).

[7] 11 U.S.C. § 1325(a)(3).

[8] 11 U.S.C. § 1307(c).

[9] 11 U.S.C. § 105(a). These holdings imply that cases under chapter 7 also would be denied. The issue will be left to future cases to decide.

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