

Good Weed, Inc.

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A successful real estate investor wishes to change the mission of his pink sheet listed corporation in which he and his family own most of the stock by getting into the distribution of medical marijuana and related products although federal law currently prohibits such activities. The federal law is not being enforced in some states that now allow distribution of marijuana for medical uses or sometimes for recreational use. There has been a boom in penny stocks in marijuana distribution and this investor sees an opportunity to make a quick profit. The case looks at these issues and at ethical issues in the sale of penny stocks.

Michael Rizzoto , known to everyone as "Mikey" is considering starting a new venture to help distribute medical marijuana (cannabis sativa) and marijuana used for recreational purposes. He also would like to distribute in the US European industrial hemp which may contain some cannabidiol in some states where such usage is currently allowed by state laws even though federal laws in the USA prohibit such activities. The current federal drug laws are controversial and some people believe that states that now allow distribution of medical marijuana in some states and recreational use of marijuana in two states (Colorado and Washington State) are appropriate especially to help those who believe that medical use of marijuana and related products is humane to help cure or alleviate some illnesses such as some forms of cancer and epilepsy and or believe that smoking marijuana is no worse than smoking cigarettes which is legal but controlled.

Mikey smoked marijuana regularly while attending college. He also sold marijuana and other illegal substances (mostly pills) but not hard drugs like cocaine or crack to classmates and was able to pay his tuition and other college costs, pay for his illegal drugs and buy a nice car out of his proceeds. In his senior year of college, he was caught selling marijuana to students and was convicted and sent to a penitentiary for two years. While in prison he stopped smoking marijuana and he successfully completed his college education with correspondence courses and independent study from his college. He accomplished this in order to get paroled after eighteen months in prison. He says that he never has personally taken any illegal substances again after prison but he believes that the federal drug laws are wrong.

After prison, Mikey went to work selling and renting commercial real estate. He became very successful as a salesman and set up a public corporation that is listed on the pink sheets. The corporation is chartered in his home state to use for ownership of real estate which he purchased over more than ten years of work as a realtor. His corporation currently owns real estate investments that are valued at over \$700,000.00.

Mikey recently read in Forbes Magazine an article, "High Times- Inside the Marijuana Stock Boom" (Nathan Vardi, FORBES, April 14, 2014, pp. 90-94) which describes the hype around legalized dealing in marijuana and how this has sent marijuana stocks on a rapid rise. The article has described how there are

now several persons with paper assets of many millions of dollars in marijuana related stocks that are regularly traded on the over-the-counter bulletin board, or pink sheets. Some of these stocks have no profits yet from their marijuana related business but their stocks have boomed.

Mikey is reasonably happy with his current life with a good income and satisfying work. He loves to sell things such as real estate to others. He is now in his early thirties. However, he would like to get really rich and thinks that the marijuana related business in approximately twenty states where it is allowed for medical purposes and two states where it is also allowed for recreational purposes is a good way to get rich fast right now when penny marijuana stocks are very hot. He has prepared a brief business plan to outline what he proposes to do in this field very quickly.

Mikey proposes to have his pink sheet listed over-the-counter corporation change its purpose from purchasing and operating commercial real estate projects to a company that works in the marijuana related fields where allowed by state laws or regulations in some states family me. He will change the name of his corporation to Good Weed, Inc. and sell off some of the real estate owned by the corporation to provide at least one half million dollars of capital to invest to start and grow his expected new business. He currently owns almost all the stock in the corporation in his name or in the name of family members and he will split the current stock owned by him and his family and a few small minority owners so that he and his family have twenty five million shares. He will keep control of the corporation. An additional twenty five million shares will be owned by the company as treasury stock and the remaining one million shares (after the stock split) will be owned by other shareholders. The shares held as treasury stock can be sold to others by the corporation to raise funds. Some of these other shares will be sold to the public when possible over the pink sheets and the funds raised will be used to help develop his new business. Some of these treasury shares will also be used as incentives for growers of marijuana and other substances so that they will distribute their product to his prospective clients such as clinics or sellers to consumers for their direct use. He will also distribute some shares to medical marijuana clinics or their principals and other sellers to the public as part of contracts with his company and these organizations to encourage these ultimate distributors to buy their products from the growers who will work with his corporation.

In addition to working with growers to help them bring their product to medical marijuana clinics and to recreational providers where allowed by state law, Mikey is also very interested in the potential of selling industrial hemp which is produced in several countries in Europe in the states which allow use of medical marijuana. To do this and reduce his corporate taxes on these imports he will set up another corporation in a tax friendly country in Europe such as Ireland or Luxembourg or Andorra, using some of his shares and his family's shares as the beginning equity in this new European corporation. Most of the profits for selling the industrial hemp in the USA can then be made in Europe and sheltered from US taxes by being kept and reinvested in Europe. Some European countries have much lower taxes on companies that export to the US than US corporate taxes and it makes sense to Mikey to keep much of the expected profit in Europe and not have to pay US taxes until some of the profits are remitted to the US if they ever are remitted. It is prudent, according to Mikey, for him and his family to diversify their assets keep their taxes lower by keeping some of the assets in Europe.

Industrial hemp produced in Europe can apparently be exported to the US even though such hemp contains some trace amounts of cannabidiol. Some medical sources contend that this substance has medical effects that can reduce epileptic fits. When it gets to the US this hemp with trace amounts of cannabidiol which is not considered by the US government at this time to be psychoactive hemp may be processed by customers here into a hemp paste that can be used on the human body that may be considered by some as safe to use for medical purposes (Vardi, op cit p. 94). Apparently this is a gray area in the law that has not yet been examined by the FDA or the Federal Department of Agriculture or by state marijuana regulatory agencies.

Quick action is needed according to Mikey if he is to make profits out of this idea. First, the federal government Controlled Substances Act apparently prohibits the distribution of marijuana for medical uses and or sale of marijuana for recreational uses that have been passed by some states. Under the US Constitution, as interpreted by the US Supreme Court, the federal law is supreme and state law must yield to federal in many areas such as most commerce. Despite his oath of office to enforce the federal laws,

President Barrack Obama and his Attorney General, Eric Holder, may not have appropriately enforced these federal laws that make any usage of marijuana illegal in the United States. President Obama and Attorney General Holder do not support the present laws but they could perhaps be pressured by public opinion to change their minds at any time and start enforcing these laws as the US Constitution apparently would require until Congress changes the law. The failure of President Obama and Attorney General Holder to enforce these laws may also eventually lead to litigation in the federal courts which may well rule out any state approval of distribution of marijuana anywhere in the US without the approval of Congress.

Some politicians also are suggesting that President Obama and or Attorney General Holder should be removed from office because they are not upholding the requirement of their oaths of office to the Constitution that the executive branch of government enforce all the laws. Mikey does not believe that such a removal will occur even if the president's party loses control of both houses of Congress because few people have studied the Constitution and others may not consider this an important issue. Mikey is more worried that a new president elected in 2016 may decide to uphold the enforcement of laws regarding controlled substances as the Constitution apparently requires until Congress changes the laws which it may do subject to the approval of any legislation by the president. Perhaps an eventual change in laws by Congress may also lead to more government regulations as presently mostly the state regulations concentrate on how much marijuana is in the substance sold and there is no regulation of what other substances may be in the marijuana plants. Mikey is concerned also that some marijuana companies may not be successful in their operations and the stock bubble in marijuana stocks may end soon. Therefore, he has concluded that if he is to enter this business he must do so as soon as possible.

QUESTIONS FOR DISCUSSION

1. 1. Do you think that Mikey can make a large sum of money if he enters this business at this time?
2. 2. Is Mikey's business plan adequate planning to start a new business? If not, what else is needed?
3. 3. Is Mikey's goal of making a lot of money during a rise in speculation a legitimate goal for a public corporation controlled by Mikey or is this merely a scam on innocent investors?
4. 4. If such a plan might be considered a scam, should the SEC and or state corporate regulatory agencies adopt new regulations to minimize the risks of such speculation to innocent investors who may not understand the downside of such possible investments?
5. 5. Should marijuana be a legal substance in any state that wishes to make it legal for medical purposes with adequate controls and perhaps for recreational use or is this a matter that should be decided by the federal Congress and be the same for the entire country?
6. 6. Should US tax laws be revised to lower US taxes on corporations to levels found in most other countries to retain corporate capital and jobs in the US?
7. 7. Do European countries have any responsibility to regulate export of substances such as industrial hemp that may be used in the US for purposes that may be considered by some to be possibly dangerous to the good health of ultimate purchasers in the US?

GOOD WEED, INC. INSTRUCTOR'S NOTE

CASE SYNOPSIS

This case focuses on a successful real estate investor who wishes to change the mission of his public pink sheet listed corporation where he and his family owns most of the shares to get into the distribution of medical marijuana and other related products such as distribution of European industrial hemp which may contain some cannabidiol in some states that now allow distribution of such products for health reasons and for recreational use in a few states even though federal laws on drugs and related substances prohibit such activities. The current US administration has not been enforcing these federal laws in these states as the administration is sympathetic to the possible use of marijuana and related substances for health reasons and possibly also for recreational use. Consequently, there has been a boom in the price of penny stocks in the marijuana related industry and the investor who controls his public pink sheet listed corporation sees an opportunity to make large profits for himself and his family by focusing the new mission of the corporation on this new industry and selling some of his investment in the corporation to the public using the penny stock market at expected high profits due to the boom in this industry. The case looks at these issues and ethical issues in the sale of penny stocks.

COURSES AND LEVELS

This case can be used in several courses including Business Law, Investment Management, international Business and Business Strategy, as well as in Business Ethics courses. It is probably best used as an undergraduate case.

INTRODUCTION

The individual (Mikey Rizzoto) considering changing the mission of his listed pink sheet corporation from real estate to distribution of marijuana and related products served time in a prison as a young man for illegal distribution of drugs. Since leaving prison, he completed college and went on to a career of success in real estate sales and investment. He believes that the federal laws on distribution of marijuana and related products are wrong. He also is tempted to go into this industry because of a boom in penny stock prices of marijuana distribution stocks even though few companies if any have made a good return to date for such businesses. He thinks he can take advantage of this boom or bubble in the prices of marijuana distribution related corporations even before he gets into the distribution of these substances. He also thinks that there is little risk that the federal government under the present Obama administration will decide to begin enforcing the federal laws about distribution of drugs such as marijuana even if they lose control of both houses of Congress. The name of the individual and the size of his corporation have been changed to protect the confidentiality of the person and corporation discussed in this case.

SOCIAL & CULTURAL ENVIRONMENT

The social & cultural environment of the United States at the current time shows an ambivalence about the distribution of marijuana and related products. A significant part of the population of some states are sympathetic to the use of marijuana and related substances to try to alleviate or cure some diseases. Some persons are also sympathetic to the distribution and use of marijuana and related substances for recreational purposes and at least two states now allow this use under their current drug distribution policies (Colorado and Washington State). Even these two states insist that any marijuana distributed in their states must be grown in their states so a national market in marijuana distribution does not seem likely at this time. At the same time as there is some support for use of marijuana there is a strong effort to further regulate and to attempt to reduce smoking of tobacco along with a growing effort

to regulate use of nicotine inhalers and nicotine patches which have become more profitable in the tobacco related industry. The failure of the current Obama administration to enforce all the federal drug laws regarding marijuana has alienated some persons who believe that the US Constitution requires all laws to be enforced by the administration until such laws are revised by Congress. Some persons believe that marijuana may be more harmful to the health of young persons than allowing the widespread distribution of marijuana for alleged health purposes to alleviate or cure some diseases. Thus, public opinion on the idea that marijuana and related products should be distributed to the public or to patients easily for some purposes is divided.

CORPORATE GOVERNANCE

Public pink sheet corporations are usually able to change their missions with approval of the board of directors of the corporation. In many jurisdictions in the USA, stockholders need not be asked to also formally approve a change of mission of a corporation. Some stock exchanges also do not require approval by the stock exchange of a change in mission of the corporation which is listed on the exchange on the pink sheets. Corporate boards of directors may also split the shares of stock without stockholder approval being required in some jurisdictions. Mr. Rizotto has control of a majority of shares in his pink sheet listed corporation and a friendly board of directors. He probably can get a change of the mission of this corporation accepted by the board of directors and can also get a split of stock that would make the price of shares listed for his corporation attractive to those who like to invest in penny stocks and are willing to speculate on the future price of a stock in the marijuana distribution field during the current high prices of such stocks even absent any real recent earnings in this field. The stock exchange on which his corporation is listed on the pink sheets has listed other stocks in the marijuana field. The attorney for the corporation must check all of this out before such changes can be recommended to the board of directors and to the stock exchange and to the state or states where the stock will be sold if needed under state blue sky laws after the proposed change in mission.

SOURCE NOTE

Information germane to this case is available at a number of sources. Students can find out much of this information on the internet looking up legalization of drug use, medical marijuana and related subjects. The growing controversy over possibly regulating use of nicotine inhalers and patches is also available on the internet or by consulting the Index to the New York Times and the Index to the Wall Street Journal and the Business Periodical Index and related sources. Cogent consideration of this case by the better students means that they will do this research especially if suggested to do so by the instructor.

PEDAGOGICAL METHOD

Instructors will need to play an active role in teaching this case. It is recommended that the instructor give a short lecture on businesses that may be illegal in some jurisdictions such as drug distribution and use, illegal gambling on sports, prostitution and organized crime in general. The organized criminal syndicates may in some industries and places prevent legal alternatives by physically threatening possible new competitors where drug distribution or something similar has taken place. For example bookmaking on horse races and sports survive despite legalization of such betting on off track betting in some states. The organized crime syndicate pays winnings quickly without disclosure to tax authorities the names and amounts of winners and can also illegally make loans for gambling available to their customers despite high interest rates by illegal lenders to gamblers through illegal bookmakers. Waste disposal by mob controlled garbage disposal companies may enable dumpers of trash to be able to more cheaply dispose of chemicals in air conditioners for example than could perhaps be done using trash collectors who follow the laws of disposing of such trash at a financial savings to the dumpers of the trash using mob controlled garbage disposal services that do not carefully follow the environmental regulations for trash disposal.

Lack of familiarity with the roles (the corporation promoter/owner -Mikey and a possible purchaser of the stock in his corporation by a speculator) will probably preclude role playing. Emphasis should probably be on discussing the major issues in the case such as legalization of drug distribution, recreational use of drugs such as marijuana, the ethics of penny stock distributors and their stock exchanges, the failure to follow the US Constitution by the Obama administration, and the difference in public opinion about regulating tobacco and regulating marijuana.

DISCUSSION QUESTIONS

1. Do you think that Mikey can make a large sum of money if he enters this business at this time?

If Mikey follows the same process as other promoters of marijuana penny stocks, he can probably make a lot of money very quickly by selling some of his shares to speculators unless the boom in marijuana stocks collapses. Speculators in these stocks seem to be purchasing these stocks on the hopes that the boom in their prices (despite some setbacks) will continue. They seem to buy without looking at any of the standard investment fundamentals of Graham and Dodd and other traditional investment counselors and analysts. The lack of any significant earnings by any marijuana stocks to date does not seem to bother some of these speculators. If the boom turns into a bubble and the bubble collapses, whoever owns these stocks will take possibly large losses.

2. Is Mikey's business plan adequate planning to start a new business? If not, what else is needed?

If Mikey is seriously considering a long term future in this business, his business plan is totally inadequate. He needs to study other distributors of these products. He needs to look at how the products will be acquired and at what price, how they will be marketed, operating practices to see that the laws of each state where operations will take place are followed in terms of who can purchase the products under state laws and how the product will be safely stored without access to persons who do not have any legal right under state law to purchase it. He also will have to study the success and policies of other distributors of this process to see what else will be required to make a profit over the long term for his shareholders. He will have to make financial projections as to when a breakeven can be achieved and how much profit can be projected for his shareholders using pro forma financial statements. If students have not studied business plans the instructor can ask them to look at standard business plans on the internet or can discuss developing a standard business plan with them using this business as an example.

3. Is Mikey's goal of making a lot of money during a rise in speculation a legitimate goal of a public corporation controlled by Mikey or is this merely a scam on innocent investors?

Opinion on this issue is likely to be sharply divided depending on the philosophy of the students. Some will claim that purchase of stocks is a buyer beware situation. The average investor may never have the sophistication of a Warren Buffet and the buyer should always be wary. Buying stock based on hope without careful review of the proposed business plan and proposed financial projections may be foolish. Some persons like to gamble on stocks and others will need to take the standard Graham and Dodd approach to investing by carefully looking at all the numbers and considering other factors such as the vagueness of the legality of these new marijuana companies. Some will say that buyers should be allowed to gamble as they would like to do. Others will say that such kind of speculation should be regulated by governments.

4. If such a plan might be considered a scam, should the SEC and or state corporate regulatory agencies adopt new regulations to minimize the risks of such speculation to innocent investors who may not understand the downside of such possible investments?

Stock promoters might be required by state or federal regulators to furnish prospective buyers of such stocks with warnings about the speculative nature of such investments. The instructor may discuss the state blue sky laws in the state where the school is located with students and they may then discuss

whether such regulations make sense or will more or less regulations be best in the long run public interest.

5. Should marijuana be a legal substance in any state that wishes to make it legal for medical purposes with adequate controls and perhaps for recreational use or is this a matter that should be decided by the federal Congress and be the same for the entire country?

This is a matter that will have a lot of different opinions. Some persons will support the present federal laws on these substances and they will suggest that these laws be enforced as required by the US Constitution. Others will suggest amending the federal laws. Some others will say that they believe that the federal laws be repealed and let any state regulate this situation as it wishes. Discussion of these issues is usually helpful to students in deciding their own views on these issues.

6. Should US tax laws be revised to lower US taxes on corporations to levels found in most other countries to retain corporate capital and jobs in the US?

Opinion on this is also divided. Some persons favor high corporate taxes and would increase present levels of taxes on corporations even though it may cost a flight of jobs and business to other countries. Others say present US tax policies on corporate taxes causes loss of jobs and business to other areas of the world. The example within the US of companies moving to lower tax states is likely to be repeated worldwide with disparity of taxes on corporations. Some others will go even further and say that there should be no taxes on corporations and that present tax systems based on income should be eliminated and replaced by consumption taxes.

7. Do European countries have any responsibility to regulate export of substances such as industrial hemp that may be used in the US for purposes that may be considered by some to be possibly dangerous to the good health of ultimate purchasers in the US?

Again, there is division of points of view on this topic. Some persons think that exports should be regulated by the governments where they are manufactured. Others believe that this is the responsibility of the governments of countries that import goods as is generally common at present and that additional regulation by exporters will just increase the costs of regulation and is unnecessary. Countries attempting to prohibit imports of illegal products, such as the US government, sometimes ask the help of other governments to try to prevent production of illegal substances as is the case currently of asking the help of governments in other countries to prevent growing of poppies that may be used to manufacture illegal substances.