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Antitrust litigation is coming to cannabis

By Lisl Dunlop, Sam Sherman, and Barbara Samaniego

As more states and even the federal government move towards legalization, the cannabis industry continues to grow. As with other industries, increasing size and consolidation brings heightened scrutiny under the antitrust laws. While cannabis is no stranger to antitrust — in 2019, there were nine "second request" investigations into cannabis mergers from the Department of Justice — so far, lawsuits challenging cannabis companies for violating the antitrust laws have been rare. That may be changing.

In 2021, a California jury handed down a $5 million verdict ($15 million when trebled) in a case against a group of medical marijuana collectives for conspiring to prevent a competitor from opening a competing dispensary. That case — *Richmond Compassionate Care Collective v. Koziol* — was brought in California state court under California's Cartwright Act.

A few weeks ago, True Social Equity in Cannabis (TSE) sued cannabis companies Akerna, Green Thumb Industries (GTI), Verano, Surterra, and ILDISP LLC (a joint venture between GTI and Verano) in the U.S. District Court in Illinois under the federal antitrust laws.

While the TSE complaint is likely to be dismissed at an early stage, it does raise some interesting questions about the basis for antitrust liability and highlights some potential risk areas for cannabis companies.

Background

TSE is an unincorporated association, whose members consist of consumers of branded marijuana in Illinois, workers in the branded marijuana industry, entrepreneurs in ancillary hemp-related ventures, and competitors and potential competitors of the defendants. GTI, Verano, and Surterra grow, manufacture, and sell cannabis products. Akerna is an enterprise software company that supplies software to track prices, supply, and demand of cannabis. According to the Complaint, the defendant companies compete in the Illinois cannabis market, and share pricing information and collude to charge monopolistic prices as part of the "Chicago Cartel."

TSE's claims are likely to fail

Even assuming TSE's factual allegations are true, they are unlikely to establish an antitrust violation.

First, TSE's complaint is basically about a price-fixing conspiracy, although TSE brought its claim under a different statute (more about that below). But even if TSE did make price-fixing allegations, its complaint doesn't support such claims. At most, TSE alleges that Akerna's technology somehow allowed GTI, Verano and Surterra to share information about prices, supply, and demand for cannabis in order to keep prices high in Illinois. But there are no specifics about how this conspiracy was effectuated: no communications between defendants, or any explanation of how or when they conspired to raise prices. And, while the complaint states that GTI, Verano and Surterra raised prices, it doesn't identify a single instance of them

actually doing so. Allegations like these don't give defendants sufficiently concrete information about what they will need to defend against; as such, they are routinely dismissed.

Second, to sue under the federal antitrust laws, a party must challenge business practices that reduce competition marketwide; antitrust laws protect market competition, not individual competitors. The complaint doesn't explain how the alleged collusion damaged competition, such as by reducing supply or raising prices of cannabis sold in the Illinois market.

Third, the entire basis for TSE's claims is that the defendants have violated Section 8 of the Clayton Act, which prohibits director interlocks between competing companies. TSE's complaint is short on further specifics, apart from identifying one overlapping director — a person who is allegedly both the chief financial officer and a board member of GTI, and a board member of Akerna — but GTI and Akerna are not direct competitors. There are also vague allegations about directors from competing companies being on the board of a joint venture, but again it is not clear how this would violate Clayton 8.

Fourth, TSE probably lacks the legal right to sue on these claims. A party can only bring a lawsuit if it has actually suffered some injury that the defendant caused. Even if the conduct complained of resulted in the kinds of harm that TSE claims — higher prices, lost job opportunities, and an inability to obtain state cannabis licenses — these harms were likely not sustained by TSE itself, but by its members.

Finally, TSE seeks a remedy that falls far outside the normal bounds. The typical remedy under Clayton 8 is to require the defendant to eliminate any overlapping directorates. Instead, TSE asks the court to ban the defendants from conducting business in Illinois and divest all their assets.

Takeaways for cannabis operators

Although TSE's suit is likely to fail, it does raise some interesting questions. Not all complaints will be as thin and poorly written as TSE's, and as cannabis companies continue to grow they will become a target for litigation. The antitrust laws could be a prime avenue of attack for prospective plaintiffs, as cannabis companies may be less familiar with the types of conduct that could attract antitrust liability.

In addition to private litigation risks, there also is the potential for interest from the federal antitrust agencies. The DOJ has recently indicated a renewed interest in investigating and enforcing Clayton 8, the prohibition against director interlock. An easy fix here is for cannabis operators to pay close attention to the composition of their boards to guard against this risk.

More generally, however, cannabis companies should be on the lookout for conduct that skirts the antitrust laws, in particular in their dealings with competitors and others in the industry. The DOJ will prosecute criminally antitrust crimes such as price-fixing, bid-rigging, and market allocation. And such enforcement is not only focused on markets for downstream products, but also labor markets. With a variety of specialist employees, agreements about not poaching each other's staff or agreeing on wage levels could expose cannabis companies to serious liability. Antitrust compliance and education can mitigate against these risks and possibly nip any potential problems in the bud.

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