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8 Attorneys for Petitioner/Plaintiff
9 HNHPC, INC.

10 SUPERIOR COURT OF THE STATE OF CALIFORNIA
11 FOR THE COUNTY OF ORANGE

12 HNHPC, INC.,

13 Plaintiff,

14 vs.

15 THE DEPARTMENT OF CANNABIS
16 CONTROL, AN ADMINISTRATIVE
17 DEPARTMENT OF THE STATE OF
18 CALIFORNIA; and DOES 1-50, inclusive,

19 Defendants.

CASE NO. 30-2021-01221014-CU-WM-CJC

**VERIFIED PETITION FOR WRIT OF
MANDAMUS AND COMPLAINT FOR:**

- 20 (1) PEREMPTORY WRIT OF
21 MANDATE; AND
- 22 (2) INJUNCTIVE RELIEF;

23 **Assigned for All Purposes**

24 Judge Gregory H. Lewis

25 Petitioner HNHPC, INC., (“Plaintiff” or “HNHPC”), by and through its attorneys, hereby
26 complains, alleges, and avers as follows against Respondents the DEPARTMENT OF CANNABIS
27 CONTROL, AN ADMINISTRATIVE DEPARTMENT OF THE STATE OF CALIFORNIA (“DCC”)
28 and Does 1-50 (collectively “Respondents”):

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2 **INTRODUCTION**

3 1. This action arises out of the failure of the Department of Cannabis Control (“DCC”) to
4 perform its mandatory and/or discretionary legal duties in implementing the provisions of the Medicinal
5 and Adult-Use Cannabis Regulation and Safety Act (“MAUCRSA”), which is codified at Business and
6 Professions Code (“B&P”) Sections 26000 et seq. B&P Section 26000 requires the DCC to, among other
7 things, “establish a comprehensive system to control and regulate the cultivation, distribution, transport,
8 storage, manufacturing, processing, and sale of cannabis and cannabis products. B&P Code § 26000(b).
9 That directive includes the express requirement that DCC create and implement a system, known in the
10 industry as “track and trace,” to track cannabis from the plant to end sale, and in the MAUCRSA DCC,
11 a department within the Business, Consumer Services, and Housing Agency (the “Agency”) of the State,
12 was given the “the power and duties” to “control[] and regulat[e]” the cannabis industry to ensure that
13 no unregulated and unchecked cannabis is cultivated, transported, manufactured, or ultimately sold in (or
14 transported outside of) California. B&P §§ 26010, 26010.5.

15 2. Notably, the Legislature decreed that in performing its duties, “protection of the public
16 shall be the highest priority for the [DCC],” and where public protection is inconsistent with other
17 interests sought to be promoted – including the collection of cultivation and excise taxes – it mandated
18 that “the protection of the public shall be paramount.” *Id.* at §26011.5. It is those very duties and
19 obligations the DCC has failed to perform as required, leading to the need for HNHPC to initiate this
20 lawsuit to *compel* it to perform its such duties, since it has inexplicably opted to “look the other way”
21 rather than protect the public and legal cannabis operators such as HNHPC from the illegal black-market
22 sale of cannabis and cannabis products.

23 3. Simply put, DCC’s failure to perform its legal duty to implement systems to properly track
24 and flag questionable transactions has led to the exponential rise of “burner distributors” (“Burner
25 Distros”) that conceal and launder State-grown cannabis for delivery to illegal dispensaries and other
26 unregulated markets within the State as well as for the illegal transport across state lines, all without
27 paying significant legally mandated taxes (such as cultivation and excise taxes) that other law abiding
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1 cannabis licensees are required (directly or indirectly) to pay to the State. *See, e.g.*, B&P §26080
2 (licensees not authorized to transport or distribute cannabis or cannabis products outside the state unless
3 authorized by federal law, which is it not). The burgeoning use of Burner Distros, and their involvement
4 in and the facilitation of the illegal and untaxed sale of cannabis and cannabis products in California, is
5 greatly harming not only the public, but also cannabis operators such as HNHPC who conduct their
6 business *legally* and comply with both the track and trace and taxation requirements of California law,
7 while at the same time the DCC is assisting “bad actor” Burner Distros in flouting the track and trace
8 system and selling to illegal dispensaries and the unregulated cannabis market without paying all of the
9 taxes owed to the State (so both they and those ultimately selling the cannabis illegally can effectively
10 “undercut” legitimate distributors and dispensaries and sell cheaper yet unregulated cannabis products).
11 HNHPC is informed and believes at least some of the cannabis is also illegally transported out of state.

12 4. The prevalence of Burner Distros (unfortunately) has become the worst kept secret in the
13 industry, and is well known to the DCC itself (which purposefully has chosen to do nothing about it).
14 HNHPC is informed that Burner Distros generally operate as follows. Operators (usually legal cannabis
15 operators) purchase or obtain distribution licenses in various local jurisdictions, often where cultivation
16 operations are prevalent and/or where such licenses are relatively easy and/or cheap to obtain or acquire.
17 Often, an operator will procure multiple local licenses by using an array of different “front men” who
18 agree to attach their names to the licenses (which is significant, as the State’s lack of enforcement has
19 made acting as a straw man for a Burner Distro an incredibly high yield, low risk endeavor). Once
20 licensed, the Burner Distros then purchase large quantities of cannabis from cultivators within the State.
21 In connection with those purchases, the Burner Distros (which by law are responsible for collecting and
22 paying all legally mandated cultivation and excise taxes) may or may not pay the “cultivation tax” to the
23 State (via payment to the California Department of Tax and Fee Administration (“CDTFA”).

24 5. Once the cannabis reaches the Burner Distros, however, the DCC effectively ceases
25 regulating or even monitoring what happens to that cannabis, and instead relies heavily if not exclusively
26 on *tips or complaints* to instigate investigations or enforcement proceedings against illegal operators. As
27 a result, Burner Distros evade payment of the 15% excise tax (which in practice amounts to a 27% tax
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1 levied on the wholesale price based on the State’s required “markup” rate) owed by distributors when the
2 cannabis products are delivered to retail dispensaries or and/or (to a lesser extent) even when they
3 illegally ship the cannabis out of state. As of the date of this Petition, HNHPC is informed and believes
4 the amount of excise taxes *evaded by* Burner Distros total *hundreds of millions of dollars* per year on
5 billions of dollars’ worth of cannabis and cannabis products, while legitimate distributors are forced to
6 pay the excise tax. The cost savings achieved by Burner Distros through the evasion of the excise taxes
7 alone allows illegal dispensaries and other unregulated markets to purchase *largely if not entirely*
8 *unregulated* cannabis from the Burner Distros at a steep discount, which they in turn sell at prices far
9 lower than legal dispensaries can sell comparable *regulated* cannabis products obtained from legitimate
10 distributors who in fact pay all such taxes. In essence, the DCC by its inaction has *significantly bolstered*
11 the illegal black market in California and encouraged the illegal export of cannabis across state lines.

12 6. By *knowingly fueling* the illegal sale of cannabis in the State, which fundamentally
13 undermines its primary delegated mission of public protection, DCC has also substantially undermined
14 the competitiveness and financial success of operators such as HNHPC who “play by the rules,”
15 encourage ever-increasing numbers of illegal dispensaries and other black market sellers who, because
16 they do not follow the law or abide by applicable regulations or taxation, can sell cannabis illegally “on
17 the street” at significantly lower prices than legal and law abiding dispensaries such as HNHPC can. This
18 places *legal* operators in an untenable “Catch-22” situation, and many decide to “play the same game”
19 and utilize Burner Distros themselves just to compete and/or to make up losses caused by the DCC’s
20 knowing indifference to the very situation it created and now refuses to address/rectify.

21 7. If DCC knows this is all going on – and it does – it begs the obvious question: why doesn’t
22 it do something about it? HNHPC believes the answer is two-fold. First, HNHPC believes the State (via
23 the CDTFA) is collecting substantial “cultivation taxes” from Burner Distros, and it wants that tax
24 revenue to continue flowing despite knowing it is receiving cultivation taxes on far more cannabis than
25 ultimately is being sold in licensed dispensaries (i.e., it knows significant amounts of cannabis is being
26 diverted to the black market or illegally transported out of state). Second, DCC knows its track and trace
27 system is an abject failure, knows Burner Distros are failing to pay hundreds of millions of dollars in
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1 taxes on *billions of dollars* of cannabis and cannabis products per year, but does not want to publicly
2 admit its system is a failure or that as designed and implemented it neither protects the public (its primary
3 mission) nor results in the payment of even a substantial portion of the total taxes actually due. So
4 instead, DCC apparently has opted to “stick its proverbial head in the sand” and to rely *not* on its track
5 and trace system to identify offenders or flag questionable transactions (as required), but instead to rely
6 solely on *tips and complaints from the public*. Stated differently, DCC knows its track and trace system
7 is garbage, but rather than fix it DCC instead only investigates people who are reported by others (which
8 of course causes its own set of problems, such as false information and/or wrongly motivated “tips” or
9 complaints specifically designed to get DCC to investigate the “tipster’s” competitors or industry rivals).

10 8. By this lawsuit, HNHPC seeks to *compel* the DCC to actually perform its mandatory
11 and/or discretionary legal duties, including public protection and the creation and maintenance of a track
12 and trace system that in fact is capable of tracking and tracing cannabis throughout the entire process and
13 of identifying and flagging questionable transactions for further investigation and enforcement. The
14 DCC knows it has failed in such duties, has been told it both can and needs to make critical changes and
15 upgrades to its system in order to actually perform its mandated duties, but to date it has stubbornly and
16 inexplicably refused to so. And in the meantime, Burner Distros are selling *untold millions of pounds* of
17 *untaxed* and largely unregulated State-grown cannabis to illegal dispensaries, in the black market, and/or
18 to out of state customers, undercutting legal dispensary pricing, and threatening the integrity of the entire
19 system established by the Legislature in the MAUCRA. Yet because DCC has determined it is in the
20 State’s *financial and political interest* to look the other way, even while hundreds of millions of dollars
21 in excise taxes go uncollected and Burner Distros and illegal dispensaries and other black market sellers
22 are allowed run rampant throughout the State with virtually no effort by DCC to even try to stop it.

23 **PARTIES AND VENUE**

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25 9. Plaintiff HNHPC is and at all relevant times was a corporation formed and operating under
26 the laws of the State of California. HNHPC operates a State and locally licensed dispensary at 2400
27 Pullman Street, Santa Ana, California 92705. HNHPC is licensed by both the State and the City of Santa
28 Ana (the “City”) to operate a cannabis dispensary at the above location.

1 15. While the track and trace system DCC ultimately created/implemented, called “METRC,”
2 at present does not flag “irregularities” such as those transactions described above relating to Burner
3 Distros for further review or investigation, HNHPC is informed and believes the system easily *can be*
4 *re-designed or modified/upgraded* to flag such irregularities and ultimately identify Burner Distros, but
5 it would require the State first to agree to amend its current agreement with the developer of METRC to
6 authorize the work necessary to provide/add that capacity. Despite its knowledge of the issues and
7 despite being provided with a relatively simple and cost-effective solution, DCC to date has inexplicably
8 refused to authorize fixes to, or augmentation of, its current track and trace system. More specifically,
9 HNHPC is informed and believes DCC has been notified by METRC’s developers and others of the
10 issues with Burner Distros and their evasion of substantial cannabis taxes, has been told the current track
11 and trace system can be modified or upgraded to flag illegal or irregular conduct of Burner Distros that
12 it currently cannot track or flag, and that in response DCC has refused to authorize such modifications to
13 the METRC system.

14 16. The rhetorical question is this: why is DCC refusing to perform that necessary work? The
15 answer is simple. The State is collecting cultivation taxes from Burner Distros on volumes of cultivated
16 cannabis that DCC knows far exceed the amount that ultimately is sold in licensed dispensaries, so DCC
17 and the State have made the purposeful decision to *turn a blind eye* to illegal Burner Distros in order to
18 *keep that excess cultivation tax money flowing*; and (2) for political reasons DCC does not want to admit
19 the system it created for both public protection and revenue collection is an *abject failure* which neither
20 protects the public nor ensures payment of significant cannabis taxed owed by Burner Distros.

21 17. The following is an illustration of how HNHPC believes Burner Distros generally operate,
22 and more specifically how they evade DCC’s track and trace system and the payment of hundreds of
23 millions per year in excise taxes on billions of dollars’ worth of cannabis and cannabis products. It starts
24 as a locally licensed distributor that is either created as a Burner Distro or purchased for such purpose.
25 Often they operate out of small commercial or industrial spaces that are physically capable of storing or
26 handling only a fraction of the volume of cannabis they in fact “distribute,” which is one relatively easy
27 way DCC could (but does not) modify its track and trace system to “catch” the most egregious of Burner
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1 Distro operators (the State has all floor plans, and if a Burner Distro operates from a 800 SF location but
2 routinely purchase thousands of pounds of cannabis, that is a tell-tale sign of a Burner Distro). And they
3 usually are “owned” or operated by a straw-man who is paid by the true owner to use his/her name on
4 the license so that in the event of an enforcement action, the real owner/operator remains protected and
5 can continue the scheme via other entities (HNHPC is informed and believes DCC has never actually
6 shut down a Burner Distro).

7 18. Once up and running, Burner Distros will purchase a significant amount of cannabis from
8 one or more cultivators. HNHPC currently believes many (but not all) of the Burner Distros will pay the
9 cultivation tax on such purchases in order to placate the State and throw off suspicion about their
10 subsequent illicit activities (cultivation taxes range from \$1.35 per ounce of fresh plant, \$2.87 per ounce
11 of leaves, and \$9.65 per ounce of flower). But once they distribute the cannabis to black market sellers
12 or illegal dispensaries (or send it out of state), the Burner Distros do *not* pay the 15% “excise tax” (which
13 based on the State’s formula amounts to a 27% tax on the wholesale product of the products) that they
14 are required to collect and the pay to the State. And because DCC’s track and trace system does not flag
15 suspicious activity like small footprint distributors purchasing unreasonably large amounts of cannabis,
16 unreasonably long periods of time where the distributor claims it is “holding” purchased cannabis in its
17 facility, or discrepancies between the amount of cannabis purchased and the amount ultimately recorded
18 as being sold to licensed retail dispensaries, once the cannabis reaches the Burner Distros, DCC
19 effectively lacks the capacity to ferret out or flag questionable transactions or the failure to pay required
20 taxes. Instead, the DCC (and CDTF, which oversees tax payments) are relegated to performing only
21 tip or complaint-based investigations, which means if no one complains, Burner Distros potentially can
22 operate indefinitely without fear of detection or enforcement, and without paying all of the required taxes
23 that licensed dispensaries must pay to legitimate distributors for the cannabis products they sell.

24 19. As noted above, because the system essentially *fails to track* the cannabis once it reaches
25 the Burner Distros, DCC also cannot assure that the products reaching unlicensed dispensaries and the
26 black market – which are then sold to the public -- are safe and comply with all applicable legal, quality
27 or testing requirements, let alone that the State is receiving all applicable taxes due on that cannabis. This
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1 leads to two inevitable and ultimately devastating consequences for both legal operators such as HNHPC
2 and for the State: (1) free of having to pay hefty excise and other taxes, Burner Distros can sell cannabis
3 *cheap and mostly unregulated cannabis* to black market and illegal sellers, who in turn sell it cheaper
4 than HNHPC could at its dispensary – causing a significant loss in business and revenue by HNHPC and
5 other legal operators; and (2) the State (and its citizens) are deprived of hundreds in millions in tax
6 revenues per year on *billions of dollars* in cannabis and cannabis products, and are not assured the
7 cannabis they purchase is safe and meets all applicable requirements. DCC and the CDTEFA both are
8 well aware this is going on; they just *refuse to do anything about it*. HNHPC avers this injustice
9 immediately could be stopped or significantly reduced if DCC simply *complied with its legal duty* to
10 create and implement a track and trace system that actually *flags* these types of transactions and
11 irregularities for further investigation and prompt follow-up enforcement.

12 **FIRST CAUSE OF ACTION**
13 **PETITION FOR PEREMPTORY WRIT OF MANDATE**
14 (AGAINST ALL RESPONDENTS)

15 20. HNHPC incorporates as though set forth herein in full the allegations contained in
16 Paragraphs 1-19 above.

17 21. The Respondents had and have a legal duty to adhere to, follow and enforce the
18 applicable law. Here, as set forth above, the Respondents violated, *inter alia*, both their duties and the
19 provisions of the MAUCRA by failing to create a track and trace system that actually is capable of
20 identifying and flagging questionable transactions and information for investigation and subsequent
21 enforcement, as directed by the Legislature in B&P Section 26067, and by disregarding its duty to
22 protect the public from harms such as Burner Distros whose activities could be but are not being
23 monitored and flagged, let alone thereafter investigated and shut down. *See also* B&P §§26010,
24 26010.5, 26011.5, 26080.

25 22. HNHPC is informed and believes and based thereon alleges DCC has been informed and
26 is well aware that the current track and trace system cannot and is not flagging transactions and
27 information that would reveal the unlawful conduct of Burner Distros, and further that the developer of
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1 METRC has informed DCC the system *can be* upgraded/modified/augmented to in fact flag such
2 transactions and information, subject only to DCC’s and/or the State’s agreement to amend the
3 agreement with the developer to authorize that additional work. HNHPC is further informed and
4 believes and on that basis alleges the cost of such additional work would be relatively nominal, but that
5 the DCC/State is refusing to authorize that work (1) because of fear it would reduce the amount of
6 cultivation tax it presently collects; and/or (2) it does not want to admit its present system – the system
7 it was mandated to create and maintain specifically to protect the public and ensure proper regulation
8 and taxation of the cannabis industry – is an abject failure and does not work as has been falsely
9 represented or portrayed to both the public and to licensees like HNHPC.

10 23. To the extent Respondents claim they had or have discretion in the creation,
11 implementation, and/or operation of the track and trace system, HNHPC contends they abused that
12 discretion, that their actions and determinations on such matters were/are arbitrary, capricious, unfair,
13 unlawful, corrupt, and against the overwhelming weight of facts and evidence available to them at the
14 time, and/or were the result of “unreasonable” policies and procedures that are not permitted. *See*
15 *Common Cause v. Bd. of Supervisors*, 49 Cal. 3d 432, 442 (1989) (“Mandamus may issue, however, to
16 compel an official both to exercise discretion (if he is required by law to do so) and to exercise it under
17 a proper interpretation of the applicable law”); *Anderson v. Philips*, 13 Cal. 3d 733, 737 (1975) (where
18 mandamus respondent refuses to act based on interpretation of law, “the writ will lie if that
19 determination is erroneous”); *Inglin v. Hoppin*, 156 Cal. 483, 491 (1909) (mandamus “will lie to correct
20 abuses of discretion, and will lie to force a particular action by the inferior tribunal or officer, when the
21 law clearly establishes the petitioner’s right to such action”).

22 24. There is no plain, speedy or adequate remedy in the ordinary course of law available to
23 HNHPC, it has a substantial and direct beneficial interest in enforcing Respondents’ mandatory and/or
24 discretionary duties and/or correcting its abuses of discretion as it has been directly and financially
25 harmed by the offending conduct alleged herein, and HNHPC legally is entitled to performance by the
26 Respondents of such duties and/or to the proper exercise of discretion under the correct legal
27 interpretation of the MAUCRA.

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SECOND CAUSE OF ACTION
INJUNCTIVE RELIEF
(AGAINST ALL DEFENDANTS)

25. HNHPC incorporates as though set forth herein in full the allegations contained in Paragraphs 1-24 above.

26. HNHPC seeks an injunction compelling Respondents to comply with their mandatory and/or discretionary legal duties vis-à-vis the track and trace system and their enforcement obligations under State law, and mandating that they create and maintain a track and trace system that is capable of identifying and flagging for further investigation questionable transactions and information HNHPC believes would, if instituted, ferret out and ultimately stop or at least greatly reduce the illegal actions of Burner Distros and also assist in identifying and shutting down illegal and unregulated dispensaries and illegal black market sellers of cannabis products – all while significantly increasing revenue to the State from the payment of proper excise and/or cultivation taxes by distributors operating in the State.

PRAYER FOR RELIEF

WHEREFORE, based on the foregoing, HNHPC prays for the following relief:

First Cause of Action

1. For the granting of its petition for mandamus as set forth above;
2. For the recovery of costs and/or attorneys' fees, to the extent permitted by law;
3. For such other or different relief as deemed necessary or appropriate by the Court.

Second Cause of Action

1. For the granting of injunctive relief as requested above;
2. For the recovery of costs and/or attorneys' fees, to the extent permitted by law; and
3. For such other or different relief as deemed necessary or appropriate by the Court.

DATED: September 14, 2021

LAW OFFICE OF JEFF AUGUSTINI

By: 

JEFF AUGUSTINI

Attorneys for Petitioner HNHPC, INC.

DEMAND FOR JURY TRIAL

HNHPC demands a jury trial on any and all claims and allegations properly triable to a jury.

DATED: September 14, 2021

LAW OFFICE OF JEFF AUGUSTINI

Jeff Augustini

By: _____

JEFF AUGUSTINI

Attorneys for Petitioner HNHPC, INC.

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VERIFICATION

State of California, County of Los Angeles

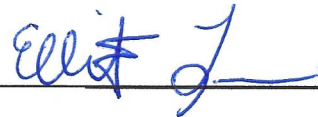
I have read the foregoing **VERIFIED PETITION FOR WRIT OF MANDATE AND COMPLAINT FOR: (1) PEREMPTORY WRIT OF MANDAMUS; AND (2) INJUNCTIVE RELIEF**; and know its contents.

I have been authorized by Petitioner HNHPC, INC. to make this verification for and on its behalf, and I make this verification for that reason.

I am informed and believe and on that basis allege that the claims, allegations and averments stated in the foregoing document are true based upon the information reasonably available to me.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct

Executed on September 15, 2021, at Long Beach, California.



ELLIOT LEWIS