

Canadian Securities Regulators Provide Guidance on Issuers Engaging in Cannabis Related Business Activities in the US

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On October 16, 2017, the Toronto Stock Exchange and the TSX Venture Exchange (collectively, the Exchanges) issued notices providing guidance to those companies with business activities related to the cultivation, distribution or possession of marijuana in the United States (the Subject Entities). In particular, the Exchanges' notices provide that the Subject Entities could be subject to an in-depth review based on their continuous disclosure records, which could result in de-listing on the applicable Exchange. In contrast, the Canadian Securities Administrators (the CSA) took a more lenient approach in its Staff Notice issued on October 16, 2017, addressed to issuers engaging in cannabis related activities in the US.

The Exchanges note that while there are a number of US states that have legalized cannabis use to various degrees and subject to various conditions, cannabis remains illegal at the federal level. The conflicting state and federal laws have created uncertainty, especially under the current Trump administration, as to whether the US federal government will take steps to intervene in states where marijuana has been legalized. As such, given the current legal landscape surrounding cannabis south of the border, the Exchanges have adopted the position that "Issuers with ongoing business activities that violate US federal law regarding marijuana are not complying with the Exchanges' Requirements."

The Exchanges have provided the following list of activities (in order of priority of concern) that will impact their continued listing review processes:

- i. direct or indirect ownership of, or investment in, Subject Entities;
- ii. commercial interests or arrangements with Subject Entities that are similar in substance to ownership of, or investment in, Subject Entities;
- iii. providing services or products that are specifically designed for, or targeted at, Subject Entities; or
- iv. commercial interests or arrangements with entities engaging in the business activities described in (iii).

The Exchanges' notices highlight that the Exchanges will group issuers in the cannabis space into two main categories when performing their continued listing reviews. One group will consist of issuers with "business activities that involve the cultivation, distribution or possession of marijuana in any jurisdiction," while the second group issuers do not participate in any of those activities, but do appear to be engaging in "Ancillary Services Activities" (which are comprised of the activities listed in (iii) and (iv) above). The Exchanges' notices recommend that all listed issuers in the cannabis sector begin to proactively address the compliance requirements laid out in Section 306, Section 325 and Part VII of the TSX Company Manual and Policy 2.1 and Policy 2.9 of the TSX Venture Exchange Manual, as applicable.

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While the Exchanges' notices indicate a shift to a more strict regulatory approach towards listed issuers in the cannabis sector, the CSA's Staff Notice only emphasizes a greater need for full and proper disclosure by those same issuers. Louis Morisset, CSA Chair and President and CEO of the Autorité des marchés financiers, stated that the CSA "expect[s] issuers with marijuana-related activities in the U.S. to address the current legal and regulatory environment in their disclosures, including any risks that result from changes in the approach to enforcement of US federal law." The CSA's disclosure-based approach is based on the assumption that issuers involved in the US cannabis industry are operating in compliance with the laws and regulations of a US state in which cannabis activity is legal, and with the knowledge and acceptance that such activities remain illegal at the federal level.

The disclosure requirements apply, on a varied basis, to issuers that are either directly or indirectly involved in the cultivation and distribution of cannabis, as well as any issuer that provides ancillary goods and/or services to third parties involved in the US cannabis industry. (These goods and services are not limited to financing, branding, recipes, leasing, consulting or administrative services.) The CSA Staff Notice provides that issuers failing to provide the appropriate disclosure may be subject to certain regulatory consequences, such as receipt refusals with regards to prospectus offerings, requests for restatements of non-compliant filings, and referrals for appropriate enforcement action.

While the long term implications of these notices on the growth of the Canadian cannabis sector remains to be seen, issuers in the space have had mixed reviews of the conflicting frameworks and there has been significant volatility in market trading prices throughout the day. Some issuers have praised the Exchanges' efforts to clarify their positions on cannabis issuers with US activities, while others have expressed concern with the lack of clarity surrounding the definition of Ancillary Services Activities. Issuers have reacted more favourably towards the CSA's Staff Notice in general, as its proposed framework does not hinder the activities of issuers listed on the Canadian Securities Exchange operating in parts of the US.

We Can Help

For more information on how Cassels can assist your business and ensure that you are complying with the Exchange requirements, please contact a member of our firm's cross-disciplinary Cannabis Group.

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