

CSA STAFF NOTICE 51-352 (REVISED) - ISSUERS WITH U.S. MARIJUANA-RELATED ACTIVITIES

By Rick Moscone and Russell Sanders

With much uncertainty surrounding the rapidly growing marijuana industry following the rescission of the Obama-era Cole Memorandum, the Canadian Securities Administrators (the "CSA") reiterated a position that bodes well for Canadian issuers involved in U.S. marijuana activities: that a disclosure-based approach remains appropriate in light of the risks posed by an inconsistent legal framework.

In the U.S., there is a conflict between state and federal law related to marijuana. Certain U.S. states permit the cultivation, sale and use of marijuana within a regulatory framework notwithstanding that marijuana continues to be listed as a controlled substance, and therefore illegal, under U.S. federal law. Before the emergence of Attorney General Jeff Sessions, the U.S. Department of Justice indicated that it would not intervene in states that have authorized this conduct so long as the state in question has implemented a robust and effective regulatory program. The Cole Memorandum was rescinded by Attorney General Sessions in early January 2018, giving federal prosecutors the discretion to enforce federal law including in states in which marijuana is legal.

Before this drastic policy shift, the CSA laid out its disclosure expectations of issuers with marijuana activities in U.S. states in which such activities were legal, given the prospect of prosecution and asset seizure by federal authorities. Following the rescission of the Cole Memorandum, the CSA updated its expectations by outlining the extent of what issuers must disclose based on their degree of involvement in the cultivation and/or distribution of marijuana in the U.S.:

- **Direct involvement** - the issuer is directly involved in the cultivation and/or sale of marijuana;
- **Indirect involvement** - the issuer has a non-controlling interest in an entity that is directly involved in the U.S. marijuana industry; and
- **Material ancillary involvement** - the issuer provides goods or services not limited to financing, branding, recipes, leasing, consulting or administrative services to third parties that are directly involved in the U.S. marijuana industry.

Set out below are the disclosure requirements of issuers with U.S. marijuana-related activities:



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1. All Issuers With U.S. Marijuana Related Activities

- Indicate whether the issuer has direct, indirect or material ancillary involvement;
- Prominently state that marijuana is illegal under U.S. federal law and that enforcement of the law is a significant risk;
- Discuss any statements and other available guidance made by federal authorities or prosecutors regarding the risk of enforcement in any jurisdiction where the issuer conducts U.S. marijuana-related activities;
- Outline related risks including, among others, the risk that third party service providers could suspend or withdraw services and that the risk the regulatory bodies could impose certain restrictions on the issuer's ability to operate in the U.S.;
- Given the illegality of marijuana under U.S. federal law, discuss the issuer's ability to access both public and private capital and indicate what financing options are (or are not) available in order to support continuing operations;
- Quantify the issuer's balance sheet and operating statement exposure to U.S. marijuana-related activities; and
- Disclose if legal advice has not been obtained, either in the form of a legal opinion or otherwise, regarding (i) compliance with applicable regulatory state frameworks; and (ii) potential exposure and implications arising from U.S. federal law.

2. Issuers With Direct Involvement

- Outline the regulations for U.S. states in which the issuer operates and confirm how the issuer complies with applicable licensing requirements and the regulatory framework enacted by the applicable U.S. state;
- Discuss the issuer's program for monitoring compliance with U.S. state law on an ongoing basis, outline internal compliance procedures, and provide a positive statement indicating that the issuer is in compliance with U.S. state law and the related licensing framework; and
- Promptly disclose any non-compliance, citations or notices of violation which may have an impact on the issuer's license, business activities or operations.

3. Issuers With Indirect Involvement

- Outline the regulations for U.S. states in which the issuer's investee(s) operate;
- Provide reasonable assurance, through either positive or negative statements, that the investee's business is in compliance with applicable licensing requirements and the regulatory framework enacted by the applicable U.S.; and
- Promptly disclose any non-compliance, citations or notices of violation, of which the issuer is aware, that may have an impact on the investee's license, business activities or operations.

* Negative statements may include statements that the issuer is not aware of non-compliance.

4. Issuers With Material Ancillary Involvement

- Provide reasonable assurance, through either positive or negative statements, that the applicable customer's or investee's business is in compliance with applicable licensing requirements and the regulatory framework enacted by the U.S. state.

The CSA has mandated that the disclosure referenced above be prominently displayed in prospectuses, marketing materials, annual information forms, management's discussion and analysis, and listing statements, as applicable. Furthermore, the disclosure must be updated on an ongoing basis in the event of a change in government policy, as was the case with the rescission of the Cole Memorandum.

Exchange Listings

In addition to allowing issuers with U.S. marijuana-related activities to continue to operate so long as they comply with the disclosure requirements set out above, the CSA provided further reinforcement to issuers by permitting stock exchanges to decide, on an individual basis, whether to list entities with U.S. marijuana-related activities. This is a positive development for current and prospective issuers as the Canadian Securities Exchange, which has been actively supportive of issuers involved in the marijuana industry, including those with U.S. involvement, remains a viable option to list securities.