

## Corporate and Commercial Law

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### Update on Cannabis Legalization: Governments, Regulators and the Court Weigh In

As Canada continues towards the currently-anticipated July 2018 legalization of cannabis, there have been a number of recent major regulatory and legal developments related to the production, distribution and retail sale of cannabis, each occurring on October 16, 2017.

As outlined in our May 10, 2017 Update, *What's Next for Recreational Cannabis? Provincial Policy Considerations after the Introduction of Federal Legislation*, the proposed federal legislation (Bill C-45, first introduced in April) leaves much of the regulation of recreational cannabis to the provinces and territories. Since then, the provincial governments of Ontario, New Brunswick, and Alberta have released their plans for the regulation and sale of recreational cannabis. The provincial securities regulators and Canada's major stock exchange have each responded with policy clarifications; the securities regulators issued a notice outlining the specific disclosure requirements for issuers with, or who plan to have, U.S.-related cannabis activities, and the Toronto Stock Exchange (TSX) clarified its stance on the application of its listing requirements to issuers with U.S.-related cannabis activities. Finally, in Ontario, the continued operation of retail storefront dispensaries has been further curtailed by a recent decision of the Ontario Superior Court of Justice which issued temporary injunction against a number of dispensary operators and their landlords.

#### Provincial Regulatory Regimes Take Shape

*Ontario.* The Government of Ontario recently announced that it would pursue a model for the distribution and sale of cannabis similar to that currently in place in Ontario for alcohol, through government-run retail outlets. Under this proposal, a

subsidiary of the Liquor Control Board of Ontario (LCBO) will be responsible for the retail sale and distribution of cannabis, and will purchase products from Health Canada-licensed producers. Mirroring the LCBO model for alcohol and related products, the retail sale of cannabis and cannabis-related products will take place in dedicated, standalone retail locations, separate and apart from LCBO stores, as well as through online sales. The Ontario government currently expects 40 stores to be opened by July 2018, increasing to 80 by the end of the first year of legalization. Ontario also proposes to impose a legal age of 19 for the purchase and use of recreational cannabis.

*Alberta.* The Alberta government recently released the "Alberta Cannabis Framework", with a stated aim to keep regulatory costs and taxes low enough to compete with the illicit market. Under its model, consumers in Alberta will be able to purchase cannabis from government-regulated distributors, and only specialized retail outlets will be permitted to sell to the public. The Alberta government is currently considering two potential options for the ownership and operation of these retail outlets; one option would resemble Ontario's plan, consisting solely of government operated cannabis stores, while the second would involve government licensing of private retailers, mirroring the manner in which alcohol is currently sold in Alberta. Unlike Ontario, Alberta has proposed a legal age of 18 for the purchase and use of recreational cannabis.

*New Brunswick.* The New Brunswick government has created a new provincial Crown corporation which will be responsible for the supervision and oversight of the sale of cannabis products in the province. Unlike the proposed Ontario model, the New Brunswick Crown corporation will not be responsible for directly selling cannabis, but will instead work with other entities in the distribution chain. The government has not yet made a final decision on the precise parameters of the retail model, though it has already signed multimillion-dollar agreements with licensed producers with a view to ensuring adequate supply of cannabis.

*British Columbia.* In British Columbia, the government has yet to announce any official plans related to the

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regulation of the sale and distribution of cannabis products; it is in the midst of a five-week public consultation process to receive input from residents, municipal governments, First Nations and the cannabis industry. Nevertheless, in recent public statements, B.C. Premier John Horgan has indicated that his government will be considering multiple options, including the existing dispensary model. He also noted that his government's aim is to eliminate the black market, acknowledging the importance of a proper pricing and taxation model to achieve this goal. At the municipal level, the City of Vancouver has continued to issue licenses to dispensaries. In 2015, the City of Vancouver became the first municipality in the country to implement a regulatory framework within which business licenses can be granted to compliant dispensaries, and began to issue licenses in 2016. The City of Victoria has since followed suit.

## **TSX Review of Listed Companies with U.S.-Related Cannabis Activities**

On October 16, the TSX issued Staff Notice 2017-0009 (the "**TSX Notice**"). In the TSX Notice, the TSX reaffirmed the requirement that issuers must comply with all applicable laws as a condition for listing (and continued listing). Importantly, while noting that cannabis has been legalized or decriminalized in numerous states in the U.S., the TSX noted that the cultivation, distribution and possession of cannabis remain illegal at the federal level<sup>1</sup>. Accordingly, the TSX is of the view that issuers listed on its exchanges with ongoing business activities that violate U.S. federal law would not meet the TSX listing requirements. The TSX suggests that such activities may include a very broad range, including (a) direct and indirect ownership of or investments in entities involved in the cultivation, distribution and possession of cannabis in the U.S. (the "**Subject Entities**"), (b) commercial arrangements with Subject Entities akin to such investments or ownership, (c) providing services or products to Subject Entities and (d) other commercial or business arrangements with entities providing such services or products.

The TSX intends to begin reviewing listed companies conducting business in the U.S., and listed issuers in violation of U.S. federal law may be delisted from the

TSX's exchanges. Companies selected by the TSX for review will be contacted before the end of the year. In the meantime, the TSX notes that issuers listed on its exchanges should proactively work to address any gaps in their compliance with the TSX's listing requirements, which may include termination of the commercial or business arrangements or a complete divestiture of the applicable assets, business or investments.

## **CSA Notice 31-352: New Disclosure Requirements for Cannabis Companies**

The Canadian Securities Administrators (CSA) also weighed in on October 16 by issuing CSA Notice 51-352 (the "**CSA Notice**"). Like the TSX, the CSA Notice noted the continuing illegality of cannabis at the U.S. federal level and the fact the federal guidance outlined in the Cole Memoranda may be rescinded or changed at any time. However, unlike the TSX, the CSA Notice does not seek to prohibit issuers from engaging in or with U.S.-related cannabis activities; rather, the CSA Notice reiterated the disclosure requirements applicable to issuers.

The CSA Notice confirms that Canada's securities regimes are primarily disclosure-based, with requirements for timely and accurate disclosure of information, to ensure that each issuer's disclosure fairly presents all material facts and risks, enabling investors to make informed investment decisions. Based on this principle, the CSA Notice stipulates specific disclosure requirements for issuers that have, or are in the process of developing, U.S.-related cannabis activities. The specific disclosure requirements will depend on an issuer's involvement in U.S.-related cannabis activities, ranging from those directly cultivating or distributing cannabis in the U.S. to those that are not directly engaged in but provide services or products or have other financial or business arrangements with entities that engage in U.S.-related cannabis activities. Such requirements include disclosure of the issuer's involvement in or with U.S.-related cannabis activities, compliance with state regulatory frameworks, as well as information related to the risk of potential enforcement of federal cannabis laws by the U.S.

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<sup>1</sup> The TSX acknowledges that the memoranda issued by Deputy Attorney General Cole (under the Obama Administration) in August 2013 and February 2014 (the "**Cole Memoranda**") provides the (then) U.S. federal government's guidance concerning the enforcement of federal law (including U.S. federal money laundering legislation on the proceeds from cannabis-related business activities). However, as the TSX pointed out, the Cole Memoranda do not have the force of law and can be revoked or amended at any time, especially given the public musings of the Trump Administration (including the Attorney General Sessions) on the subject.

federal government. The CSA expects issuers to provide all such required disclosure clearly and prominently in prospectus filings and other required continuing disclosure documents and securities filings.

Mindful of the evolving legal landscape at the U.S. federal level, the CSA expressly reserves its right to re-examine its views in these matters.

## **Injunctions Against Dispensaries in the City of Toronto**

On October 16, the Ontario Superior Court of Justice granted the City of Toronto (the “City”) an interlocutory injunction against a number of unlicensed cannabis dispensaries, prohibiting the operators from selling, storing, or distributing cannabis. The City had originally applied for the interim injunction in February of this year, likely as a continuation of the City’s efforts to close dispensaries. Despite previous warnings, police raids and ticketing, dispensary operators have continued to operate and open new storefronts in Toronto.

The decision in *Toronto (City) v Lanova Outsourcing Corp.* granted a temporary injunction not only against dispensary operators, but also against the landlords of the properties in which this business is conducted, directing landlords to stop the use of their properties for the illicit selling, storage, or distribution of cannabis. The interlocutory injunction is a temporary order in advance of a hearing for a permanent injunction, currently not expected until December 2018, in which the applications of the City and the dispensaries will be heard in full.

In its decision, the Court held that the balance of convenience favoured the City’s request for an interlocutory order. In its analysis, the Court found that public interest would be better served by maintaining the existing regulatory regime, rather than the continued operation of dispensaries until the case’s full hearing in 2018. Furthermore, the dispensaries’ operation in contravention of validly enacted bylaws was found to constitute a potential harm to the public interest.

The Court declined the City’s request for further orders to close the dispensaries if they do not adhere to the injunction.

## **What’s Next?**

As the date of legalization approaches, it is expected that provincial governments will roll out additional

details of their distribution plans and begin to operationalize their regimes.

In particular, provinces have been, and are expected to become increasingly, active in their enforcement of marijuana laws to consolidate control over the once-illicit market from dispensaries and organized crime. On October 19, 2017, the Government of Ontario convened an ‘enforcement summit’ in which the Minister of Community Safety and Correctional Services met with the leaders of Ontario’s law enforcement and First Nations communities to map out the pathway to legalization. Among other things, the aim of the summit is to identify barriers, resolve resource deficits and discuss potential new tools (i.e., programs, legislation and regulation) to address drug-impaired driving, possession and public consumption, dispensaries, and the illicit market. This effort is expected to produce a coordinated and multidisciplinary strategy against illegal operators, and to make way for Ontario’s proposed model of government-owned specialty retail outlets. Current barriers that may need to be resolved by this enforcement strategy might include local enforcement funding constraints, border issues, First Nations partnerships, and solutions to the lengthy resource-intensive legal manoeuvres that police and municipalities are required to use to close dispensaries (as evident in the *Lanova Outsourcing Corp.* case noted above).

As they design and implement their distribution policies, all different levels of governments are also expected to increase their demands on the federal government to provide clarity on its cannabis policies and investments. In particular, these efforts will likely be aimed at receiving clarity on the direction of federal cannabis and impaired driving legislative initiatives, plans for cannabis supply management, public awareness and health efforts, as well as federal funding for law enforcement in support of cannabis legalization and regulation. For provincial, territorial and local-level government planners, these remaining issues are significant and will need to be addressed to adequately build and deploy their distribution and retail regimes.

For further information, please contact any member of our Corporate and Commercial Law Group.