

NOVEMBER 13, 2019

Canadian Securities Authorities Address Cannabis Issuers' Conflicts of Interest

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Staff of the securities regulatory authorities in Ontario, British Columbia, Québec, New Brunswick, Saskatchewan, Manitoba and Nova Scotia (collectively, Staff) has released CSA Multilateral Staff Notice 51-359 – *Corporate Governance Related Disclosure Expectations for Reporting Issuers in the Cannabis Industry* (Guidelines) aimed at reporting issuers in the cannabis industry in Canada (Cannabis Issuers). The Guidelines are meant to address what Staff calls “inadequate transparency” regarding cross-ownership of financial interests by Cannabis Issuers and their directors and executive officers.

The Guidelines address both disclosure requirements in the context of mergers and acquisitions in the cannabis industry (M&A Transactions) and disclosure relating to director independence in general.

Guideline Overview

Disclosure in M&A Transactions

Staff expressed concerns that as the cannabis market expanded, many Cannabis Issuers and their directors and executive officers participated in the financing of other Cannabis Issuers, resulting in overlapping debt and equity interests or other business relationships that were not always disclosed in the context of M&A Transactions.

Staff is of the view that detailed disclosure of the cross-ownership of financial interests is material information for investors and should be disclosed in the disclosure document applicable to the M&A Transaction. Such disclosure would allow investors to make better informed determinations about the merits of the M&A Transaction in question when exercising their rights.

Board Independence

Staff highlighted that certain Cannabis Issuers had not adequately considered potential conflicts of interests or other factors such as personal and business relationships with other directors or officers before identifying certain directors as independent. Staff also reminded issuers that for the purposes of National Instrument 58-101 – *Disclosure of Corporate Governance Practices* (NI 58-101), independent directors must not have a direct or indirect “material relationship” with the issuer and that the aforementioned conflicts and/or relationships should be carefully considered in this context. Staff also pointed out instances in which the chair of the board and the chief executive officer of several Cannabis Issuers are the same individual, in contradiction to the guidance set out in NI 58-101.

The Guidelines encourage issuers to adopt a written code of business conduct and ethics, which may include provisions stipulating when and how conflicts of interest should be disclosed to other board members as well as to the public and which would address the disclosure of cross directorships and executive officer positions and other ownership interests in the context of M&A Transactions.

Conclusion

With the Guidelines now in place, we expect that Staff will be closely monitoring the disclosure practices of Cannabis Issuers, in particular in the context of M&A Transactions and corporate governance disclosure in the ordinary course. Staff was also careful to mention that while the Guidelines were aimed primarily at Cannabis Issuers, they apply equally to all issuers, and in particular to those operating in emerging growth industries. It would therefore be advisable for all reporting issuers to closely consider addressing conflict of interest

disclosure in advance when implementing or refreshing their written codes of conduct and ethics so that issuers are prepared to make appropriate disclosure when required.

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