Intelligence MEMOS

From: Jeremy Kronick and Rosalie Wyonch

To: Chairs of Canadian Securities Commissions

Date: September 1, 2017

Re: **DON'T STRANGLE THE MARIJUANA BUSINESS IN THE STOCK MARKET**

An unforeseen development has bubbled to the surface in the process of legalizing marijuana in Canada: How to handle Canadian marijuana companies with exposure to the United States. While marijuana is legal in certain US states, it remains illegal federally.

The Toronto Stock Exchange has recently decided to suspend listing new companies with operations south of the border. Furthermore, its parent, the TMX Group Ltd. is asking for help from securities commissions to determine whether the Canadian Depository for Securities Ltd. (CDS) – which it also owns, and clears trades for all Canadian stock exchanges – should continue finalizing trades in these companies. Given the current lack of clarity on the part of the industry's players, job number one is to remove any legal ambiguity and outline a clear policy. We see no reason to prevent these trades from occurring, and believe there are three reasons why this is so.

First, we have clear rules on risk disclosure. Where things get thorny is that despite some marijuana businesses being legal in Canada, they are not in the United States, and the type of exposure to this market matters. If these companies gain directly from sales of marijuana-related products there is a risk they could be shut down, though the Rohrabacher-Farr amendment (passed December 2014) prevents the US Justice Department from spending funds to interfere with the implementation of state medical marijuana laws. There are other risk-based considerations for investors: is marijuana legal in the state(s) where the company operates? Are the companies contributing capital or simply licensing technology? Common amongst all these questions is the theme of investor risk exposure, and for this we have disclosure. If disclosure is appropriate, investors can make their own decisions about the likelihood of any risks.

The second reason these trades should continue is we are discussing legal activities in the market the company is listed in, and there is clearly growing demand for 'pot stock' ownership. The North American legal marijuana market grew 34 percent last year to $6.7 billion, and is projected to grow at a compound annual rate of 27 percent to reach $22.6 billion by 2021. CSE, a small exchange, has almost 50 listings, making up more than half its trading volume. There is also reason to believe US policy vis-à-vis marijuana is starting to shift. For example, the US Department of the Treasury permits banks to work with cannabis businesses as long as they follow the guidelines. Why would we want to stop this growth?

The final reason for these trades to continue is the transparency that arises from public markets. Whether one believes the future of capital is public or private, the rules when companies go public provide increased levels of disclosure and transparency. In a nascent market such as pot, where black markets still exist, this is a good thing.

Recently, one of your commissions, the OSC, approved the prospectus of a marijuana company going public on the CSE. This approval came despite the Canadian company having US exposure. We applaud this move. Others should follow suit.

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