10 Ways to Reduce Cannabis-Related Litigation Risks

By Michael McCachen and Chris Nyberg

In addition to the regulatory compliance issues that may arise from the production and sale of cannabis, companies operating in this space face many of the traditional legal concerns, including contractual, employment and privacy litigation, as well as intellectual property and product liability issues. The cost, time and effort expended defending litigation can substantially and directly impact an organization's reputation and growth. Below are 10 strategies to minimize the reputational, financial and personnel costs generally associated with litigation.

1 Identify Potential Issues Early

Many class actions and other lawsuits are a result of a failure to identify a potential problem or compliance issue early on. When not addressed immediately, problems may evolve into difficult and costly situations. For example, certain licensed producers in Canada have been named as defendants in class action proceedings brought by customers who are alleging, among other things, that the use of restricted pesticides during the production of cannabis resulted in negative side effects.

While establishing a crisis-control mode for every issue that could result in litigation is not recommended or required, it is beneficial to implement a reporting system that encourages potentially litigious issues to be reviewed early and regularly. The reporting should involve the corporation's in-house or outside counsel, who can render such communications privileged in the event of litigation. This approach will assist to identify issues early and may significantly reduce organizational exposure to litigation risk.

2 Act Quickly to Rectify Identified Issues

The early identification of actionable problems is often of little benefit unless some approach to rectification is implemented that reduces the litigation risk associated with such issues. Seemingly innocuous complaints that have merit can often escalate when the issue is not dealt with proactively (e.g., where complainants perceive that they are being ignored or treated with disrespect). This is especially true in an emerging industry where reputation is one of an organization's most valuable assets.

A company can often rectify the issue and settle with any complainants on a much more favourable basis than if it is not proactive. Canadian courts rarely compensate a successful litigant for more than a fraction of its actual legal costs in presenting or defending a claim through to trial. As a result, it is important to consider cutting losses at an early stage to reduce the impact of a much more significant settlement or judgment down the road. When appropriate, an early settlement may also have the added benefit of allowing the dispute and settlement to be kept confidential.

3 Consider Alternative Dispute Resolution

Litigation is expensive, time-consuming and the outcome is never certain. Adverse publicity often arises immediately while a fully successful defence of a claim may later go unnoticed. Arbitration can be selected as an alternative to litigation by consent or be made mandatory in agreements with counterparties to company contracts. Canadian courts have enforced arbitration provisions in electronic agreements. Such online agreements require a customer to accept the terms of an electronic agreement prior to purchasing a product or using a service. If your organization has an e-commerce platform for the sale of cannabis products, a mandatory arbitration clause may reduce the risk of exposure to class action litigation by requiring that disputes be settled privately by arbitration.

Arbitration should not be chosen blindly, however. Consultation with counsel is warranted first, but it has benefits over court in many instances.

4 The Best Defence Can Be a Strong Offence

The reality of operating a business in Canada is that, for a relatively nominal filing fee, anyone can bring legal proceedings against your organization, including the government. The litigation process often requires the disclosure of confidential documents (which can become available to the public) and the dedication of significant financial and personnel resources. However, the best defence is sometimes a strong offence and there are a number of preliminary applications or motions available to a defendant, which may stop a lawsuit in its tracks.

One such option is an application or motion for security for costs. If granted, the plaintiff will be required to post security for the taxable costs, which are likely to be incurred by the party defending the lawsuit. While the various provincial Rules of Court (and Business Corporations Acts) typically set out the circumstances where security for costs may be ordered (e.g., where the plaintiff resides out of the jurisdiction or has limited assets), many courts are also permitted to order security for costs on a discretionary basis where it is just and reasonable to do so in the circumstances.

Other interim applications or motions include striking out a frivolous claim or summary dismissal of all or part of a claim, which may reduce or entirely dismiss a claim in the early stages. While there is an upfront cost associated with this strategy, if successful, the resources expended would be a fraction of that incurred at trial. Such applications or motions provide a defendant with a number of options to delay or terminate an action and can provide considerable leverage when negotiating the settlement of a claim.

5 Beware That Information May Become Public

One of the biggest concerns raised by organizations facing litigation is the possibility of having to disclose confidential records to the public. A "record" is typically defined broadly and includes both physical and electronic data that is capable of being reproduced visually, by sound or both. All paper documents and electronic records such as emails, text messages and telephone recordings are included. Anything relevant and material to the case must be produced and is available to the court and opposing parties once a lawsuit has been commenced, unless subject to privilege.

Employees should be instructed to assume that all emails and other documents may be subject to the scrutiny of a plaintiff, government agency or court. Where a matter has become identified as a potential litigation risk, implementing controls on the distribution and receipt of emails containing material information is not only prudent but critical for maintaining claims of privilege.

As organizations involved in the production and distribution of cannabis are also dealing with large volumes of sensitive customer information, it is essential that all such information be kept private and secure, and that any disclosure be made only in accordance with the applicable provincial or federal privacy legislation. The proper handling of information is crucial to the early resolution of a complaint, the protection of confidentiality and maintenance of privilege.

6 Keep Proper Documentation

Recognizing that documents may have to be disclosed, it is nevertheless important to keep proper records and implement a document management system. The lack of proper documentation of regulatory compliance, agreements and incidents often creates ammunition for a regulator, complainant or plaintiff to allege a contrary version of events. Carefully written documentation may greatly assist if it becomes necessary to address a complaint that surfaces many months or years after an instigating event. Proper records provide the information necessary to respond to complaints that otherwise may become a proceeding or lawsuit.

It is also important to keep records of all efforts to resolve a complaint. Inadequate follow-up on complaints or threats of litigation may be used by litigants to demonstrate that a proper investigation did not occur, was not comprehensive or was conducted half-heartedly. It is equally important to implement and enforce a document retention and termination policy. The precise time period for document retention can only be determined with knowledge of the business and the applicable legislation.

The production of cannabis is labour-intensive. This will expose producers to employment issues. In many cases, being able to show that a proper investigation of any complaints took place and that proper follow-up steps were taken can forestall litigation before it starts, or reduce damage awards.

7 Manage Points of Interaction

Where a matter has the potential to evolve into litigation, it is important to ensure that the proper person is the point of contact with a complainant or plaintiff and that counsel is informed and involved where appropriate.

It is often the case that the person most involved in the background to a dispute is not the right person to attempt a resolution once the possibility of litigation arises, despite their background knowledge. An independent liaison — whether a member of the management team, legal counsel or otherwise — can often effectively diffuse the situation and come to a settlement.

8 Apply Smart Business Solutions

It will often be the case that a practical settlement is preferable to protracted litigation. Settlement can often be achieved between parties engaged in an ongoing business relationship where the complaint is but one aspect. Additionally, it is usually beneficial to maintain an ongoing relationship with a regulator or local government rather than focusing only on successful litigation. Rolling a small litigation problem into a much larger business deal, or agreeing to a settlement or dismissal of a claim, is often an acceptable way to resolve a dispute.

9 Be Mindful of Government Regulation

In Canada, government regulators have broad jurisdiction to sanction organizations where they believe that applicable statutory or regulatory rules have not been followed, resulting in financial and other consequences. This is especially true in the highly regulated cannabis space, where organizations are open to both criminal and civil risk.

Whether it is an investigation under provincial environmental legislation, the *Competition Act* or other provincial or federal legislation, the mere announcement of an investigation can cause severe harm to an organization's reputation. In addition, such investigations and charges can spawn civil lawsuits. In most cases, investigations are preceded by inquiries or requests for information from a government department. While the purpose of such inquiries may be self-evident in some cases, it is often difficult to predict the full extent of the concerns. As a result, creating the proper context for communication in those circumstances is critical. Moreover, understanding the motive and background behind such an inquiry is key information that should be gathered at the outset.

It is critical to have a strategy and protocols in place beforehand to deal with government regulators, regardless of whether that inquiry appears routine or becomes a formal investigation with charges made. These procedures are best developed directly with legal counsel. How you interact with such regulators may be the difference between a successful outcome and the beginning of an arduous investigation.

10 Know When to Get Help

While parties are often reluctant to contact counsel before litigation is commenced due to cost, doing so can help to contain or resolve the dispute at the early stages. Parties are often concerned that the complexity of their matter will require too much time to explain and often the circumstances are urgent. However, often the contractual, tortious or other legal principles that apply to the complaint or claim are not complex. Although there is no substitute for a formal legal opinion, an early quick review may avoid a dispute escalating into a larger public action.

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