

## **Quinn Emanuel Cannabis Litigation Practice Alert Recent Stock Drop Securities Actions in the Cannabis Industry**

Within the last two years, private litigants have initiated more than a dozen “stock drop” suits against publicly traded companies in the cannabis industry under U.S. securities law. The types of claims are not new: Section 10(b) of the Securities Exchange Act of 1934, and Rule 10b-5 promulgated thereunder, prohibit companies or their officers from making false or misleading statements or omissions in connection with the sale of securities. Sections 11 and 12 of the Securities Act of 1933 generally impose similar requirements with respect to securities offerings. Stock drop actions are those actions that follow from a decline in the price of a security. A shareholder will assert that new information provided by the defendant company or a third-party contradicts prior company statements or reveals they were incomplete. Shareholders further assert that this new information caused a decline in the value of a security, and damage to the shareholder. These litigants will bring suit not only on behalf of themselves, but on behalf of a class of all similarly situated shareholders. Litigants will typically not only bring suit against the company but certain high-ranking corporate representatives as well.

There is nothing new about “stock drop” suits; they represented 214 of the 441 securities class actions filed in 2018 in federal court.<sup>1</sup> However, the uptick in recent years of cannabis companies as defendants in such litigation is new. To provide a better sense of the significance of these kinds of lawsuits, this alert: (1) gathers data on the value, duration, and dispositions of this type of securities case; and (2) surveys “stock drop” cases filed recently against actors in the cannabis industry.

### **Dispositions of Securities Actions**

The following represents a review of publicly available information with respect to “stock drop” securities actions.

- Typical settlement value of securities action settlements: An analysis of securities class actions determined that the average settlement for securities stock drop class actions in 2018 was \$69 million dollars and the median settlement was \$13 million.<sup>2</sup> The difference resulted primarily from a single certain high-value outlier settlement.<sup>3</sup> In 2017, the average settlement amount was \$25 million, and the median settlement was \$6 million.<sup>4</sup> In 2016, also a year with an outlier, high value settlement, the average settlement amount was \$77 million (adjusted for inflation), while the median amount was \$9 million (also inflation adjusted).<sup>5</sup>
- Typical duration of securities actions: Between 2001 and 2014 the majority of securities class actions took two years or more to be resolved, either by settlement or dismissal. The distribution was as follows: 13% of these actions were resolved in less than 1 year; 26% were

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<sup>1</sup> NERA, Recent Trends in Securities Class Action Litigation: 2018 Full-Year Review, Jan. 29, 2019 (the “NERA Report”), at 5, [www.nera.com](http://www.nera.com).

<sup>2</sup> NERA Report at 28, 30.

<sup>3</sup> NERA Report at 28.

<sup>4</sup> NERA Report at 28, 30.

<sup>5</sup> NERA Report at 28, 30.

resolved between 1 and 2 years; 22% were resolved between 2 and 3 years; 14% were resolved between 3 and 4 years; and 25% were resolved after 4 years.<sup>6</sup> For cases filed in 2016, the median resolution time was 2.3 years.<sup>7</sup>

- Motion to dismiss dispositions of securities actions: Between 2014 and 2018, defendants filed motions to dismiss (that is, motions to reject plaintiffs' cases even accepting the truth of their allegations, and before any facts could be developed) in 95% of cases.<sup>8</sup> Courts resolved 77% of these filings; the remaining 23% of motions were not decided, either because of a settlement, plaintiffs' voluntary dismissal, or defendants' decision to withdraw the motion.<sup>9</sup> For those actions where the court did reach a resolution, the court granted 39% of the motions to dismiss.<sup>10</sup>
- Motion for class certification dispositions of securities actions: A significant majority of cases, 73%, are resolved prior to a decision on a motion for class certification (that is, a decision that a plaintiff can represent not only himself or herself, but other similarly-situated shareholders as well).<sup>11</sup> For the cases where a motion for class certification is made, the parties resolved the suit prior to the court's decision on the motion 44% of the time.<sup>12</sup> Courts have granted motions to proceed as a class, either in part or in full, 81% of the time.<sup>13</sup>

## Recent Stock Drop Securities Actions in the Cannabis Industry

A review of public filings reveals at least sixteen "stock drop" securities class actions since 2014 in the cannabis industry: one has settled,<sup>14</sup> and one is in the process of settling;<sup>15</sup> two have been voluntarily dismissed without prejudice; one has been dismissed by stipulation of the plaintiff with prejudice; and the remainder are ongoing. All but three of these actions have been filed in the last two years. The following recently-filed actions represent the range and type of recent "stock drop" securities actions in the cannabis industry.

- *Huang v. CannTrust Holdings Inc. et al.*, No. 1:19-cv-06396-JPO (S.D.N.Y.): CannTrust Holdings, Inc., is a Canadian cannabis producer.<sup>16</sup> According to plaintiffs, beginning with its announcement of third quarter results on November 14, 2018, CannTrust made false and misleading disclosures related to a growing facility, and in particular failed to disclose the regulatory status of the facility.<sup>17</sup> On July 8, 2019, CannTrust announced a report from Health Canada had found the facility non-compliant.<sup>18</sup> The announcement led to a 22% decline in

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<sup>6</sup> NERA Report at 27.

<sup>7</sup> NERA Report at 26.

<sup>8</sup> NERA Report at 19, 20.

<sup>9</sup> NERA Report at 20.

<sup>10</sup> NERA Report at 20.

<sup>11</sup> NERA Report at 21.

<sup>12</sup> NERA Report at 21.

<sup>13</sup> NERA Report at 21.

<sup>14</sup> *In re Medbox*, No. 2:15-CV-00426-BRO (C.D. Cal.) Dkt. 88-3 (proposing settlement of \$1.85 million dollars); Dkt. 114 (granting final approval).

<sup>15</sup> *In re Namaste Technologies*, No. 1:18-CV-10839-GHW (S.D.N.Y.) Dkt. 45-1 (proposing settlement of \$2.75 million dollars); Dkt. 66 (ordering settlement hearing for March 11, 2020).

<sup>16</sup> 1:19-cv-06396-JPO (S.D.N.Y.), Dkt. 1 ("CannTrust Complaint") ¶ 2.

<sup>17</sup> CannTrust Complaint ¶¶ 17-22; 23.

<sup>18</sup> CannTrust Complaint ¶ 24.

CannTrust's stock.<sup>19</sup> Plaintiff filed its action on July 10, 2019; the parties are currently engaged in motion practice with respect to consolidating similar actions, appointing lead counsel, and appointing class counsel.<sup>20</sup>

- *In re Curaleaf Holdings Inc. Security Litigation*, No. 1:19-cv-04486-BMC (E.D.N.Y.): Curaleaf, a Canadian company headquartered in Massachusetts, acts as an “integrated medical and wellness operator.”<sup>21</sup> According to plaintiffs, Curaleaf made certain statements about a CBD product and suggested, for example, that it could be used as a dietary supplement.<sup>22</sup> These statements in turn prompted a warning letter from the FDA on July 22, 2019, which in turn led to a 7% decrease in the value of Curaleaf stock.<sup>23</sup> Plaintiffs filed their complaint on August 5, 2019.<sup>24</sup> Certain procedural matters followed, including consolidation of a number of suits with similar allegations, and also motions related to the appointment of class counsel.<sup>25</sup>
- *Hammond v. Greenlane Holdings, Inc., et al.*, No. 9:19-cv-81259-RKA (S.D. Fl.): Greenlane is a distributor of vaping products, including CBD products.<sup>26</sup> According to plaintiffs, in preparation for its IPO, Greenlane made certain misrepresentations about the prospects of the e-cigarette business.<sup>27</sup> These statements did not reflect the company's full knowledge of future regulatory actions that would be undertaken, in particular, by the city of San Francisco.<sup>28</sup> The complaint alleges that an adverse regulatory announcement precipitated a 17% hit to Greenlane's stock price and that Greenlane's stock has fallen 68% from its IPO.<sup>29</sup> The action was filed September 11, 2019, and the parties are currently briefing motions to appoint lead plaintiff and lead counsel.<sup>30</sup>
- *Huang v. Sundial Growers Inc., et al.*, No. 1:19-cv-08913-ALC (S.D.N.Y.): Sundial is a Canadian cannabis producer and marketer.<sup>31</sup> Plaintiff alleges that Sundial made certain misrepresentations with respect to the quality of its cannabis products as well as other allegedly misleading statements.<sup>32</sup> The complaint was filed on September 25, 2019.<sup>33</sup>

## Key Takeaways

Public cannabis companies are increasingly being sued in shareholder securities class actions. The public data on securities class actions indicates there are a wide range of possible outcomes, but many securities cases settle for significant sums and last for years.

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<sup>19</sup> CannTrust Complaint ¶ 4.

<sup>20</sup> CannTrust Dkt. 1, 40, 65, 67, 69, 70, 71.

<sup>21</sup> 1:19-cv-04486-BMC (E.D.N.Y.) (“Curaleaf Complaint”) ¶ 7.

<sup>22</sup> Curaleaf Complaint ¶¶ 16-19, 20.

<sup>23</sup> Curaleaf Complaint ¶¶ 21-23.

<sup>24</sup> Curaleaf Dkt. 1.

<sup>25</sup> *E.g.*, Curaleaf Dkt. 36.

<sup>26</sup> 9:19-cv-81259-RKA (S.D. Fl.) (“Greenlane Complaint”) ¶ 2.

<sup>27</sup> Greenlane Complaint ¶¶ 36-43.

<sup>28</sup> Greenlane Complaint ¶¶ 43, 44-45.

<sup>29</sup> Greenlane Complaint ¶¶ 46, 48.

<sup>30</sup> Greenlane Dkt. 1, 26, 28.

<sup>31</sup> 1:19-cv-08913-ALC (S.D.N.Y.) (“Sundial Complaint”) ¶ 9.

<sup>32</sup> Sundial Complaint ¶¶ 34-35.

<sup>33</sup> Sundial Dkt. 1.

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If you have any questions about the material in this memo, or if you would like a copy of any of the materials mentioned in it, please do not hesitate to reach out to:

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