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Three Ways to Effectively Assess a Legal Cannabis Company To Mitigate Risk

How to scrutinize a legal cannabis company for utmost viability to best ensure your investment, partnership, employment or other engagement doesn't 'go up in smoke.'

By Merilee Kern

With the legal cannabis industry projected to exceed \$50 billion by 2022, according to Cowen & Co., and another report citing that, from just January to September 2017, alone, “cultivation and retail investments tripled to \$718 million” with areas like agricultural technology, infused products, and software attracting copious investor dollars, the future for many stakeholders is decidedly green.¹

Given the extent of near-guaranteed growth and financial upside of the legalized cannabis industry and throngs of sectors related thereto, there's a gold rush mentality prompting people to invest in cannabis stocks, partner with cannabis companies, accept employment opportunities and otherwise “get in the game” and stake their claim as the so-called “wild west of cannabis” unfolds.

Or, “flourish” seems to be a better characterization, given the legal cannabis industry is reported to be the single fastest-growing industry in the United States — one that added more than 64,000 full-time jobs in 2018, bringing the total number of positions for the year to 211,000 — up 44 percent from the prior year, according to a new report from Leafly and Whitney Economics.²

So, it's certainly no surprise that trend-driven, profit-minded companies, entrepreneurs, investors and even job seekers are putting politics and “value

judgments” aside, finding ways to leverage legalized cannabis interests to boost their own bottom lines. However, “given the extent and complexity of issues surrounding safety and security, regulatory and compliance matters, technology and other key concerns that can vary from state to state, there are a number of key factors to examine before formally engaging or investing with a company operating in this space to best protect your interests,” warns Zachary Venegas, CEO of Helix TCS, Inc.³ — the industry's leading provider of integrated operating solutions in the legal cannabis industry.

His publicly traded company (OTCQB:HLIX), which is heavily staffed with military veterans and law enforcement specialists, oversees security and transport, data analytics and compliance-tracking concerns for legal cannabis businesses across the industry spectrum. This as it pertains to producers, manufacturers, distributors, retailers and governments, alike.

According to Venegas, a pioneering executive helping drive cannabis industry maturation, “It's imperative to proceed with extreme caution, as seemingly legitimate purveyors in this space can still be riddled with red flags and hazards that they themselves may or may not be aware of, which are often not apparent to an outsider without proper due diligence. No profit-minded professional would prudently ignore such a market, but one must be mindful that this unique sector is rife with complex legal and regulatory risks.”

To help professionals and businesses at large better navigate what can be a

treacherous field of issues while engaging with a cannabis company, Venegas offers this advice on a few ways to effectively scrutinize a legal cannabis company (whether private sector or publicly traded).

Be skeptical of fast expansion

This can be an indication that a company is prioritizing growth over regulatory compliance, which varies drastically by state. Professionals will understand that an appetite for risk is often a plus, and that companies that play it safe usually aren't the ones to end up making waves.

But, when it comes to the cannabis industry, there's a caveat: according to Venegas, being cautious with regulatory requirements isn't a mistake — it's good management. However inevitable as it might seem, legal cannabis hasn't yet hit mainstream acceptance. Not being methodical in complying with regulations at both the local and federal levels means these businesses are a step away from disaster.

While any number of companies have so far skirted the minefield of regulations without consequence, they may have been lulled into a false sense of security as heavier enforcement is only a matter of time. Early adopter states such as California intend to get tough on illegal pot purveyors. This amid widespread reports that Nicole Elliott, senior adviser on cannabis to Gov. Gavin Newsom, said state funds for enforcement would nearly double in the fiscal year that begins July 1, to \$113 million.⁴

California is also actively driving public information campaigns helping

consumers get “#weedwise” to best ensure their purchases are legal and from properly state-licensed cannabis businesses.⁵ This includes production, manufacturing, retail, delivery, distributors and testing laboratories. Using tools like those the California Bureau of Cannabis Control offers at Capotcheck.com, consumers and industry players, alike, can readily vet an organization.

One other way to evaluate a business on this point is to examine its legal team to the extent possible. Any legitimate business that plans to stay in this particular game must have proper legal advice. If they don't have lawyers, it's highly possible they're not being mindful of this sector's ever-changing legal landscape.

Avoid businesses without foundational advantages

When trying to predict which companies will be around for the long haul, investors should look to Canada, which legalized recreational marijuana in 2018. Nine out of the world's top 10 largest cannabis companies, all Canadian, first had a solid grounding in supplying medical cannabis before branching into recreational products.⁶

“An advantage in infrastructure is huge,” Venegas notes. “We all tend to like the story of the tiny startup blowing up overnight, but the businesses most likely to take advantage of legalization are those who have existing footholds in the industry and the connections to exploit them. A lot of these smaller operations will be squeezed out of the market once legalization is widespread and larger players join in.”

In other words, be wary when engaging companies entering the market — or even currently operating — without

sound infrastructure, though they might seem like good prospects in the existing competitive environment. The only thing constant is change, as the saying goes, so a company must be willing and able to scale, pivot and adapt as needed. Also consider that companies with operations in adjacent industries, such as hydroponics equipment, also have a head start.

A red flag: no executive experience in a heavily regulated industry

A must in any engagement scenario is studying a company's team, but this takes on another level of importance when it comes to cannabis. The mess of varying state regulatory environments, future legal developments and political concerns means any business planning to succeed in the industry will face a set of unique challenges that few other companies will.

Experience is needed to mitigate those challenges and ensure that growth doesn't hit a landmine. Executives or advisors with a background in the medical cannabis industry are the ideal scenario, as this can well prepare a company for future changes across various levels beyond pharma with respect to recreational marijuana and a litany of CBD and hemp-oriented consumer goods.

Even executives or advisors in other industries that comparably navigate stringent regulatory and compliance challenges can be a boon. This might be why tobacco companies are betting big to become major players in the cannabis market.⁷ Even professionals with backgrounds in alcohol, gaming, cryptocurrency and the like may be able to adapt more quickly to the fast-changing environment of the current cannabis market than the norm.

“In my extensive work helping legitimate and legal cannabis operations secure the various resources needed to scale their businesses and capitalize on revenue and other growth opportunities, coupled with my private equity and frontier market launches of multimillion-dollar businesses across three continents, I've seen the good, the bad and the ugly at this point in my career — including how each of these scenarios has impacted the marketplace at large,” notes Venegas. “I'm thrilled to boil some of this key learning down to tips and tools that other professionals and businesses can utilize to keep themselves out of harm's way ... financially, legally and otherwise.”

It would seem that even keeping this bit of baseline wisdom in mind can proffer a make or break difference, helping you avoid getting “burned” by endeavoring into the legal cannabis trade. ■

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¹ <https://cannabiz.media/2017/11/28/2018-marijuana-industry-trends-and-predictions/>

² <https://d3atagt0rnqk7k.cloudfront.net/wp-content/uploads/2019/03/01141121/CANNABIS-JOBS-REPORT-FINAL-2.27.191.pdf>

³ <https://belixtcs.com/>

⁴ <https://tinyurl.com/yxlo5bqs>

⁵ <https://aca5.accela.com/bcc/customization/bcc/cap/licenseSearch.aspx>

⁶ <https://marijuanaindex.com>

⁷ <https://www.marketwatch.com/story/cronos-ceo-says-altria-investment-is-just-the-beginning-2018-12-07>