FRANCHISING UNDER THE RADAR IN THE USA AND CANADA: HOW TO ENSURE YOUR CLIENT’S FRANCHISE DREAMS DON’T GO “UP IN SMOKE”

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I. INTRODUCTION

Over the last thirty years, cannabis legalization and the concept of a legal cannabis market have morphed from fringe proposals to a multi-national industry with bipartisan support. In Canada, recreational marijuana use is legal nation-wide,¹ and the market for legal marijuana is expected to generate more than $4 billion (CAD) in sales.² In the United States, thirty-three states have legalized marijuana either for medical or recreational use, a dozen more allow the use of “low tetrahydrocannabinol (THC), high cannabidiol” (CBD) products,³ and the market for medical and recreational use is expected to generate almost $13 billion (USD) in sales.⁴ Industry groups estimate that legalization in the United States at the national level would produce $253 billion (USD) in sales between 2019-2023.

People looking to invest in this industry may want to turn to franchising to develop and provide a business model, operating system and recognizable “brand.” In Canada, franchises have been part of the industry’s development. Conversely in the United States, the patchwork nature of state laws and marijuana’s illegality under federal law make franchising a cannabis business more challenging.

This paper will discuss the current state of Canadian and American cannabis legalization, the Canadian franchise experience, challenges and opportunities for cannabis franchising in the United States, and the legal and ethical challenges to providing legal advice to cannabis clients.

II. A BRIEF SUMMARY OF THE CANNABIS INDUSTRY

For the purposes of this paper, the “cannabis industry” will mean businesses that grow, transport, process, market and sell: (1) cannabis for recreational or medical use; (2) cannabis paraphernalia such as pipes, bud cutters and other products used to consume cannabis; and (3) CBD products derived from the cannabis plant. “Marijuana business” or “Marijuana industry” will refer to a business involved with cannabis that is high in THC and not derived from the hemp plant. “CBD business” will refer to businesses involved with cannabis that is low in THC, high in CBD, and derived from the hemp plant.

The cannabis industry has enormous growth potential. In the United States, almost ten percent of adults, or twenty-four million people, report using marijuana regularly.⁵ In Canada, forty percent of adults living in Ontario and Alberta report using marijuana regularly.⁶ The rise of

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⁵ Id.
recreational marijuana use is so significant that beer makers have expressed concerns about declining sales after marijuana legalization, although the actual effect is unclear. Consumers are also interested in consuming marijuana through edibles, vape pens, and topical oils.

In addition to marijuana products containing THC, the cannabinoid responsible for users feeling “high,” there is also a high demand for CBD products, which contain the cannabinoid, cannabidiol. CBD may be derived from either marijuana or hemp plants, and its advocates claim CBD can be used to treat anxiety, sleep issues, chronic pain, inflammation, and epilepsy. Consumers can purchase CBD-infused drinks, gummies, coffee beans, shampoos, and massage oils. CBD products have been discussed or endorsed by the New York Times, Mandy Moore, Willie Nelson (his company sells CBD infused coffee beans called “Wille’s Blend”), and Good Housekeeping. Although hemp-derived CBD is legal at the federal level, state laws, federal regulations, and inconsistent enforcement still pose significant hurdles to business and individuals attempting to enter the CBD industry.

Other scholars in the area have opined that franchising a marijuana business is “not quite mission impossible” and that “daring entrepreneurs” may “recognize and embrace” the risks of cannabis franchising in order to reap “substantial financial rewards.” Today, franchising a cannabis business is intriguing to many potential franchisors, not just “daring entrepreneurs.” However, the constantly shifting legal and regulatory environment means that any attorney advising a cannabis franchise business must carefully assess all aspects of the franchise system, or their client’s franchise dreams may go up in smoke.

III. FRANCHISING MARIJUANA BUSINESSES IN CANADA

Canada is the second country in the world to legalize recreational marijuana and the first G7 nation to do so. The path to marijuana legalization in Canada has not been without its highs

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10 Id.

11 Williams, supra note 8.

12 Williams, supra note 8.

13 Williams, supra note 8.


16 Id.

and lows, and has been a national issue that has garnered international attention. Although marijuana legalization has been at the forefront of Canadian politics over the past several years, the legal treatment of marijuana use and possession has a much longer history in Canada.

In 1923, Health Minister Henri-Séverin Béland\textsuperscript{18} declared, “There is a new drug in the schedule,”\textsuperscript{19} adding marijuana to the list of prohibited drugs along with heroin and codeine during a review of the Opium and Narcotics Act.\textsuperscript{20} Prior to Béland’s statement, the Canadian government allowed recreational marijuana use and encouraged industrial hemp production.\textsuperscript{21} Notably, the Parliament of Canada did not begin to debate the manufacture, sale, and distribution of medicine containing small amounts of banned drugs until over nine years after marijuana sale and use had been banned in the country.\textsuperscript{22} Following these debates, Parliament legalized the use of certain small quantities of marijuana and hemp for use in medicines.\textsuperscript{23}

In the late 1930s, the depiction of marijuana use in the United States as a life-ruining drug shifted Canadian attitudes toward marijuana. In 1938, the federal government introduced a law prohibiting Canadians from growing marijuana without a permit, and the government ordered that marijuana crops used for scientific and research purposes be destroyed.\textsuperscript{24} A surge of marijuana use in the 1960s prompted the then-Liberal Canadian government to explore non-medical use of drugs. In May 1969, the Government of Canada appointed a Commission of Inquiry into the Non-Medical Use of Drugs, which became known as the “Le Dain Report.” The results of the Le Dain Report, published in 1972, conclusively and controversially stated that there was no science to support criminal sanctions for marijuana possession and recommended decriminalizing simple marijuana possession and cultivation for personal purposes.\textsuperscript{25} Ultimately, the then-current federal government did not accept the Le Dain Report’s recommendations.

In the early 2000s, Canadian courts began to lean toward marijuana depenalization. In \textit{R v. Parker}, the Ontario Court of Appeal struck down the total ban on medical marijuana declaring the ban unconstitutional.\textsuperscript{26} In July 2001, the Government of Canada introduced legislation that permitted the use and possession of dried marijuana for medical purposes to certain authorized individuals. Pursuant to the Marihuana Medical Access Regulations (MMAR), applicants were required to submit a declaration from a licensed physician recommending the use of marijuana as a medical treatment. The MMAR permitted authorized individuals to produce their own marijuana plants, designate someone to produce such plants for them, or apply for Health Canada’s supply of dried marijuana or seeds. Over a decade later, in June 2013, the Government

\textsuperscript{18} Id.
\textsuperscript{19} Id.
\textsuperscript{21} Id.
\textsuperscript{22} Health Canada, supra note 1.
\textsuperscript{23} Health Canada, supra note 1.
\textsuperscript{24} Health Canada, supra note 1.
\textsuperscript{26} \textit{Regina v. Parker} (2000), 49 OR (3d) 481, 188 DLR (4th) 385.
of Canada introduced the Marihuana for Medical Purposes Regulations (MMPR), which opened
the door to the commercial industry and set out a framework for the production and distribution
of marijuana for medical purposes. The MMPR authorized individuals who held a declaration from
an authorized healthcare practitioner to access marijuana cultivated and grown by licensed
commercial growers. In August 2016, the Government of Canada replaced the MMPR with the
Access to Marijuana for Medical Purposes Regulations (ACMPR) as a response to a Canadian
federal court decision released in February 2016, which held that the MMPR was
unconstitutional. Under the ACMPR, a new regime regarding possession, production and use of
medical marijuana was established.

From 2003 to 2015, Canadians witnessed a political ping-pong match as Liberal
governments attempted to introduce depenalization legislation, and Conservative governments
would squash such bills whenever possible. This match ended on October 19, 2015, when the
Liberal government led by Justin Trudeau won a majority government, paving the way for Bill C-
45, An Act respecting cannabis and to amend the Controlled Drugs and Substances Act, the
Criminal Code and other Acts (Cannabis Act). The Liberal Government introduced the Cannabis
Act in April 2017, with the primary purpose to legalize marijuana in Canada. The Cannabis Act received Royal Assent on June 21, 2018, and ninety-five years after Health Minister Béland’s statement, recreational marijuana was legalized across Canada on October 17, 2018.

A. Federal Marijuana Law

The Cannabis Act legalizes and regulates the manufacture, sale and use of marijuana,
providing a strict legal framework for controlling production, distribution, sales, and possession of
marijuana across Canada. The Federal government enacted the Cannabis Act with three goals:
to protect youth from marijuana use, to keep profits out of the illegal market, and to protect public
health and safety by allowing adults to access legal marijuana.

As Canada is a Federal Parliamentary Democracy, both the federal and provincial
governments have jurisdiction over different areas relating to marijuana legalization. The federal
government is responsible for setting countrywide standards, including maximum possession
limits, advertising and packaging requirements, minimum age limit, and home cultivation rules.
As further discussed below, the provincial governments are responsible for the distribution and
wholesaling of marijuana, establishing a retail model, and regulating public consumption.

Pursuant to the Cannabis Act, it is legal for adults over the age of eighteen to possess up
to thirty grams of legal dried marijuana or its equivalent in public. Canadians can buy dried or

27 Allard v. Her Majesty the Queen in Right of Canada, 2014 FC 280.
28 Id.
29 Cannabis Act, SC 2018, c 16.
30 Cannabis Legalization and Regulation, Department of Justice, Government of Canada (Oct. 17, 2018),
31 Supra note 29 at s 7.
32 Supra note 30.
33 Id.
34 Dolgoff, supra note 29 at s 8(1).
fresh marijuana and marijuana oil from a provincially licensed retailer. In provinces without a regulated retail framework, individuals can purchase marijuana online from federally licensed producers. Additionally, Canadians are able to grow up to four marijuana plants per household for personal use, so long as they purchase the seed or seedlings from a licensed distributor or retailer. Marijuana edible, extract and topical products are not yet legal, but the federal government has now released a final draft of amendments to the Cannabis Regulations, set to come into force on October 17, 2019, adding edibles, extracts and topicals as permitted classes of marijuana. While edibles are not available for purchase, Canadians are permitted to make marijuana products, like food or drinks, at home so long as organic solvents are not used to create concentrated products. Notably, medical marijuana will remain accessible for Canadians who have authorization by their healthcare provider.

To achieve the federal government’s goal of protecting youth, the Cannabis Act prescribes an age restriction and limits the manner and method of promoting marijuana. No person may sell or provide marijuana to persons under the age of eighteen. There are two criminal offenses associated with the age restriction. The first consists of giving or selling marijuana to youth, and the second involves using a youth to commit a marijuana related offense. Both criminal offenses have maximum penalties of up to 14 years in jail. Restricting promotion and enticement of marijuana is the other aspect of protecting youth. The Cannabis Act prohibits products that are appealing to youth, including any packaging or labelling that appeal to youth. Furthermore, the Cannabis Act prohibits selling marijuana through self-service displays or vending machines. The only promotion of marijuana available is in narrow circumstances where youth are unable to see the promotion and only via informational or brand preference advertising. Penalties for violating the promotion and enticement prohibitions include a fine of up to five million dollars (CAD) or up to three years in jail.

B. Provincial and Territorial Marijuana Law

As noted above, marijuana regulation is governed by both the provincial and federal governments. For each province, this paper will canvas the provincial law, the governing body, whether the system is private or public, and outline the licensing process if applicable. In addition,
this paper will provide a high-level overview regarding the requirements to open a retail marijuana outlet and what, if any, barriers exist to owning a business or franchise in the province.

1. **British Columbia**

   British Columbia enacted the *Cannabis Control and Licensing Act*, which received Royal Assent on May 31, 2018.\(^46\) In doing so, the Government of British Columbia echoed the intention and spirit of the federal government to introduce legislation to protect youth, promote health and safety, keep marijuana out of the illegal market, keep roads safe, and support economic development.\(^47\) The *Cannabis Control and Licensing Act* provides that the minimum age to purchase, sell, or consume marijuana is nineteen years old. It also permits adults to possess up to thirty grams of dried marijuana or its equivalent in public. Under the *Cannabis Control and Licensing Act*, smoking or vaping of marijuana is prohibited everywhere that tobacco smoking or vaping are prohibited, and is prohibited in vehicles, at playgrounds, sports fields, skate parks, and other places where children commonly gather.\(^48\) Adults are able to grow up to four marijuana plants per household so long as they are not visible from public spaces off the property, unless such household is used as a childcare facility.\(^49\)

   The *Cannabis Control and Licensing Act* also establishes a marijuana retail licensing regime similar to the current licensing regime for liquor. The Liquor Distribution Branch is the wholesale distributor of non-medical marijuana in British Columbia and oversees marijuana retail stores in the province.\(^50\) In conjunction with the *Cannabis Control and Licensing Act*, British Columbia also enacted the *Cannabis Distribution Act*, which establishes the public wholesale distribution monopoly and public retail sales, both in physical stores and online.

   The licensing authority in British Columbia is the Liquor and Cannabis Regulation Branch (LCRB). This entity is responsible for licensing non-medical marijuana private stores and monitoring the non-medical marijuana retail sector. To apply for a marijuana license, a prospective applicant must apply through the marijuana Licensing Application Portal.\(^51\)

   There are multiple license types available in British Columbia. The first is the Cannabis Retail Store License. With this license, licensees can sell only non-medical marijuana and accessories that are federally approved and purchased through the Liquor Distribution Branch.\(^52\) Licensed retail stores are permitted to operate between 9:00 a.m. and 11:00 p.m. unless the local government or indigenous nation imposes shorter hours.\(^53\) Furthermore, minors are not allowed

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\(^{46}\) *Cannabis Control and Licensing Act*, SBC 2018, c 29.

\(^{47}\) Id.

\(^{48}\) Id. at ss 1, 14, 15, 52 and 61 to 67.

\(^{49}\) Id. at s 56.

\(^{50}\) *Cannabis Distribution Act*, SBC 2018, c 28, s 11.

\(^{51}\) Non-Medical Cannabis Licences, Government of British Columbia (last visited July 30, 2019), [https://www2.gov.bc.ca/gov/content/employment-business/business/liquor-regulation-licensing/cannabis-regulation](https://www2.gov.bc.ca/gov/content/employment-business/business/liquor-regulation-licensing/cannabis-regulation)

\(^{52}\) Cannabis Licensing, Apply for a cannabis licence, Government of British Columbia (last visited July 30, 2019), [https://justice.gov.bc.ca/cannabislicensing/](https://justice.gov.bc.ca/cannabislicensing/).

to enter the retail store for any reason, and customers cannot consume marijuana inside the store. Lastly, under the Cannabis Retail Store License, licensees cannot sell marijuana online and are permitted to sell marijuana only in the licensed store.

The LCRB also issues the license required to operate a Provincially Operated Cannabis Store. These stores are government-run and may operate in-store and online. The LCRB anticipates that in the future it may offer additional licenses, namely: the Cannabis Rural Retail Store License and marijuana Marketing License. The Cannabis Rural Retail Store License may come into effect once regional distribution of retail non-medical marijuana stores is better understood. If rural or remote areas are not adequately serviced by existing stores under the current licensing regime, the LCRB may be authorized to issue this new type of license in response. The Cannabis Marketing License would allow marketers to promote products of licensed federal marijuana producers to licensed marijuana retail stores. Currently in British Columbia, federally licensed marijuana producers are not eligible for a Cannabis Retail Store License.

The application process for obtaining a Cannabis Retail Store License has multiple steps. First, there must be an application evaluation done by the LCRB, then a security screening and financial integrity check. In addition, the local government or indigenous nation must give its recommendation. Once an application is received, the LCRB will notify the local government of the area where the proposed store will be located, and the local government can (1) elect not to make any recommendation, in which case the licensing process would end; or (2) elect to make certain recommendations or comments regarding the application. If the local government makes a recommendation in favor of the application, then the LCRB may continue to review the application to determine whether or not it will issue the license. To be eligible to apply, the applicant must (1) be at least nineteen years old; and (2) be a sole proprietor, partnership, corporation, society, or indigenous nation. An applicant does not have to be a citizen or resident of British Columbia or Canada. Importantly, and in contrast to some U.S. jurisdictions, pursuant to Section 26(4) of the Cannabis Control and Licensing Act, there cannot be a “tied house,” i.e., a personal, financial, or business connection, between a marijuana retail store and a federally licensed marijuana producer. If a personal, financial or business connection exists, the LCRB can restrict a person or retail marijuana store from selling any products associated with that producer.

There are multiple fees involved with the application and renewal process. The first-time application fee includes security screening and financial integrity checks is $7,500 (CAD). If approved, the First Year Licensing Fee is $1,500 (CAD) and each year an annual

57 Supra note 53.
58 Supra note 46 at s 26(4).
Renewal Fee of $1,500 (CAD) is due. Additionally, a security screening renewal fee in an amount to be determined must be paid every two years.\textsuperscript{59}

2. \textbf{Alberta}

The Government of Alberta enacted the \textit{Act to Control and Regulate Cannabis} (ACRC), which received Royal Assent on December 15, 2017. Pursuant to the ACRC, an individual must be eighteen or older to possess, consume, buy, or sell marijuana.\textsuperscript{60} An adult can carry up to thirty grams of dried marijuana or equivalent and may purchase marijuana only from licensed stores. The Government of Alberta has prohibited marijuana consumption in some public places.\textsuperscript{61} In alignment with the federal \textit{Cannabis Act}, adults may grow up to four marijuana plants per household. The Alberta Gaming, Liquor and Cannabis Commission (AGLC) is responsible for regulating the marijuana licensing regime. The AGLC operates an online marijuana store and oversees all private marijuana retailers operating physical stores.\textsuperscript{62}

The AGLC sets the rules regarding who can become a marijuana retailer. The application and licensing process require mandatory background checks for all potential retailers and workers. Provincial regulations\textsuperscript{63} include limiting licenses for any person, business, or organization to fifteen percent of the total number of licenses each year.\textsuperscript{64} The intention of this cap is to protect smaller retailers and allow them to enter the market. All staff at retail marijuana stores must be eighteen or older, must undergo a background check, and complete a four-to-six hour mandatory AGLC training through the “Sell Safe” program.\textsuperscript{65} The rules establish where private marijuana retailers can be located and stipulate that their hours of operation will be the same as liquor stores, from 10:00 a.m. to 2:00 a.m. the following day.\textsuperscript{66}

The application process takes two to four months to complete and consists of background checks, a $400 (CAD) non-refundable application fee for each store location, $700 (CAD) annual license fee, $3,000 (CAD) initial deposit for background checks, and municipal approval.\textsuperscript{67} To operate as a business, the retailer must be incorporated in Alberta or extra-provincially registered in Alberta, and must operate only for the purpose of a retail marijuana store.\textsuperscript{68} Recently, the AGLC


\textsuperscript{61} \textit{Id.}


\textsuperscript{63} \textit{Gaming, Liquor and Cannabis Regulation}, Alta Reg 143/96, made under \textit{Gaming, Liquor and Cannabis Act}, RSA 2000, c G-1.

\textsuperscript{64} \textit{Id.} at s 106.

\textsuperscript{65} \textit{Id.} at s 126.

\textsuperscript{66} \textit{Id.} at s 121.


\textsuperscript{68} \textit{Id.}
lifted the moratorium on new retail license applications and issuing new retail licenses.\textsuperscript{69} To ensure the stability of marijuana supply, the AGLC will issue five licenses on a weekly basis and will continue to monitor the supply to ensure retailers continue to receive adequate inventory.\textsuperscript{70}

3. Saskatchewan

The Government of Saskatchewan enacted the \textit{Cannabis Control Act}, which received Royal Assent on October 17, 2018. The \textit{Cannabis Control Act} prescribes the minimum age to purchase or consume marijuana, which is nineteen years.\textsuperscript{71} Possession is limited to thirty grams per adult in a public space, whereas minors are prohibited from possessing any amount. If a minor is found to have less than five grams of dried marijuana or equivalent, it is a provincial offense and can result in a fine. It is a criminal offense for a minor to possess more than five grams of dried marijuana or equivalent.\textsuperscript{72} The \textit{Cannabis Control Act} also sets a zero tolerance policy for drug-impaired driving and a prohibition on consumption of marijuana by a driver or passenger.\textsuperscript{73} Adults in Saskatchewan can grow up to four plants per household. Importantly, consuming marijuana in public is prohibited under the \textit{Cannabis Control Act}.\textsuperscript{74}

The Saskatchewan Liquor and Gaming Authority (SLGA) is the regulating body who will regulate online sales and private retail stores.\textsuperscript{75} The SLGA is committed to a competitive private model for wholesale/distribution and retail sale of non-medical marijuana.\textsuperscript{76} The only way to purchase marijuana legally in the Province of Saskatchewan is from a licensed retailer.\textsuperscript{77}

The licensing process through the SLGA consists of two types of permits. The first is the Cannabis Retail Store permit, where the primary business activities and sole source of income is the revenue generated by the sale of marijuana product and accessories.\textsuperscript{78} With the Cannabis Retail Store permit, a private retail store can sell to individuals online through delivery or in store pickup. The second permit currently available is the Cannabis Wholesale permit, which is available to businesses that want to engage in wholesale purchase and distribution of marijuana.\textsuperscript{79}

\begin{thebibliography}{9}
\bibitem{70} \textit{Id}.
\bibitem{71} \textit{The Cannabis Control (Saskatchewan) Act}, SS 2018, c C-2.111, ss 1-2(1) and 2-1(1).
\bibitem{72} \textit{Id}.
\bibitem{73} \textit{Id} at s 2-10(1).
\bibitem{74} \textit{Id} at s 2-14.
\bibitem{75} \textit{Id} at s 1-2(1).
\bibitem{76} Cannabis Retailing, Saskatchewan Liquor and Gaming Authority (last visited July 30, 2019), \url{https://www.slga.com/permits-and-licences/cannabis-permits/cannabis-retailing}.
\bibitem{77} \textit{Supra} note 71 at s 2-7(1).
\bibitem{79} \textit{Id}.
\end{thebibliography}
Importantly, in municipalities with more than one Cannabis Retail Store permit, no marijuana retail store permittee will be allowed to control more than fifty percent of the permits in the municipality.  

Before the Cannabis Licensing and Inspections Branch of the SGLA will consider or renew a permit, it must receive a completed application and appropriate fee. Cannabis permit applications require detailed information about the ownership and financing of the business, and personal and corporate information, including criminal background checks of the business’s owners and key individuals. In Saskatchewan, proof of possession is also required. A permit will be issued only for a specified physical premise in legal possession of the applicant. The final step is receiving municipal approval and passing a building inspection. The SGLA stipulates the application processing time to be approximately ninety days. The permit fees vary depending on application type and are generally non-refundable. For a retail permit in a city, the application fee is $2,000 (CAD), and the annual fee is $3,000 (CAD). For a retail permit other than in a city, the application fee is $2,000 (CAD), and the annual permit fee is $1,500 (CAD). The wholesale permit application fee is $2,000 (CAD), and the annual permit fee is $3,000 (CAD). The permit is valid for three years.

The SGLA has stipulated that employees at private marijuana retailers must be nineteen years or older and must complete the “CannaSell SK” training program. The maximum permitted hours of operation are from 8:00 a.m. to 3:00 a.m. the following day. The SGLA also set minimum hours for private marijuana retailers at five days a week for six hours a day. Like most provinces, minors cannot enter the retail store.

4. **Manitoba**

The Government of Manitoba enacted the *Safe and Responsible Retailing of Cannabis Act*, which received Royal Assent on June 4, 2018, to amend existing laws to create *The Liquor, Gaming and Cannabis Control Act* and the *Cannabis Regulations*. In Manitoba, individuals must be nineteen or older to possess or consume marijuana, and can only buy it from licensed retailers. A proposed addition to *The Liquor, Gaming and Cannabis Control Act* stipulates that adults can carry up to thirty grams of dried marijuana or its equivalent and cannot consume marijuana in public. A key difference in Manitoba’s marijuana legislation from its counterparts is that adults cannot grow marijuana plants at home. The Liquor, Gaming and Cannabis Authority of Manitoba (LGCA) regulates the marijuana industry in the Province of Manitoba. The LGCA

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80 Id. at 10.
81 Id. at 12.
82 Id. at 13.
83 Id. at 14.
84 Id. at 21.
85 Id.
87 Id. at s 101.15.1 [not yet in force].
88 Id. at s 101.15.
oversees a hybrid public/private retail model for non-medical legal marijuana with wholesale distribution through Manitoba Liquor and Lotteries (MLL).\footnote{99}{Id. at s 101.3.}

Licensed private retailers were selected through competitive requests for proposal bidding. In July of 2018, Manitoba released a Request for Pre-Qualification (RPQ) and created a list of potential applicants based on the RPQ. Successful applicants were selected from the list generated by the RPQ, and no avenue currently exists to be added.\footnote{90}{Cannabis Retail Framework Frequently Asked Questions, Government of Manitoba (last visited July 30, 2019), \url{https://www.gov.mb.ca/jec/cannabis/faq.html}.} Successful RPQ applicants had to demonstrate access to $300,000 (CAD) in cash holdings, operating capital to cover three months of initial expenses, and a $50,000 (CAD) letter of credit before operating the retail marijuana store.\footnote{91}{Request for Pre-Qualifications for Cannabis Retail Stores – Phase 2, Government of Manitoba (last visited July 30, 2019), \url{https://www.gov.mb.ca/jec/cannabis/files/cannabis_rfq-201807.pdf}.}

Currently in Manitoba, there is no open market for private retailers, due to a shortage of marijuana supply. In the future, the LGCA will move toward an open market framework where a person or company can enter into a marijuana store agreement through the MLL.\footnote{92}{Supra note 86 at s 101.3.} This open market framework will consist of two licenses. The first type of license is an Age Restricted License, which will be granted for a stand-alone store concept that is similar to the retail store model in other provinces. The second type of license is a Controlled Access License, consisting of a store-within-a-store model, whereby there will be a designated marijuana area; however, no marijuana can be displayed.\footnote{93}{Id. at s 101.4.}

5. **Ontario**

The Government of Ontario enacted the *Cannabis Statute Law Amendment Act*, which amended the *Cannabis Control Act* and received Royal Assent on October 17, 2018. Pursuant to the *Cannabis Control Act*, an individual must be nineteen years or older to buy, use, possess, and grow recreational marijuana.\footnote{94}{Cannabis Control Act, 2017, SO 2017, c 26, Sched 1, s 10.} Adults in Ontario are able to use marijuana in private residences, outdoor public spaces, designated smoking guest rooms, residential vehicles and boats that are not being driven, research and testing facilities, and controlled areas in health care facilities.\footnote{95}{Cannabis laws, Government of Ontario (last visited July 30, 2019), \url{https://www.ontario.ca/page/cannabis-laws}.} Marijuana use is prohibited in indoor common areas, enclosed public places and work places, any place where children gather, and in non-controlled roomed-in health care facilities. Outdoor areas where marijuana use is prohibited include places like restaurant patios, grounds of community recreational facilities, and sheltered outdoor areas.\footnote{96}{Id.} Adults in Ontario can possess a maximum of thirty grams of dried marijuana or equivalent in public at any time and are permitted to grow up to four plants per residence.\footnote{97}{Id.} In order to be permitted to grow plants at home, an
individual must be nineteen years of age or older, they must be only for personal use, and the starting material must be purchased from an Ontario marijuana store or authorized retail store.\textsuperscript{98}

The Ontario government opted for a tightly regulated private retail model. The regulator for privately run recreational marijuana stores is the Alcohol and Gaming Commission of Ontario (AGCO).\textsuperscript{99} The law governing all owners and operators of a marijuana retail store is the \textit{Cannabis License Act, 2018}. The AGCO has set out a comprehensive application process to get a Retail Store Authorization. Before applying for a Retail Store Authorization, applicants must check first with the local municipality to ensure first that the local government has not opted out of having retail marijuana stores and that the physical premises meets municipal requirements for retail stores.\textsuperscript{100} Licensed marijuana retailers can purchase marijuana only from the Ontario Marijuana Store.

Once the AGCO receives a complete Retail Store Authorization, the applicant is notified that they have twenty-four hours to place a placard at the location of the proposed retail store location.\textsuperscript{101} It must be posted for fifteen calendar days to notify the public that a marijuana retail store is proposed for this location. After the public notice period ends, the AGCO provides the applicant with copies of any submissions and has five calendar days to provide written responses to relevant submissions regarding protecting public health and safety, protecting youth and restricting their access to marijuana, and preventing illicit activities in relation to marijuana.\textsuperscript{102}

There are three types of licenses or authorizations available to applicants in Ontario: (1) a Retail Operator License, (2) a Retail Store Authorization, and (3) a cannabis Retail Manager License.\textsuperscript{103} All are valid for a period of two years and will have the option to renew. Applicants must pay a fee when they first apply for a marijuana retail-related license, which is generally non-refundable.\textsuperscript{104} After the two-year period there is also a renewal fee, and the licensee can select a two or four year renewal term for any license type.

On December 13, 2018, the Government of Ontario announced that it would begin taking a phased approach to licensing in the province. During the initial tranche, only twenty-five licenses were made available for issuance. Any operator who obtained a license would be required to be open to the public as of April 1, 2019. Prior to opening to the public, each licensee must have obtained a Retail Operator License and a Retail Store Authorization. On July 3, 2019, the Government of Ontario announced a new lottery process whereby up to fifty additional marijuana retail store licenses will be available to be awarded.\textsuperscript{105} The \textit{Cannabis License Act, 2018} and its

\textsuperscript{98} \textit{Id.}

\textsuperscript{99} \textit{Cannabis Licence Act, 2018}, SO 2018, c 12, Sched 2, s 1(1).

\textsuperscript{100} \textit{Id.} at s 41.


\textsuperscript{102} \textit{Id.}

\textsuperscript{103} \textit{Supra} note 99 at ss 3, 4 and 5.

\textsuperscript{104} \textit{Id.}

\textsuperscript{105} Second allocation of stores – Allocation Lottery, Alcohol and Gaming Commission of Ontario (last visited July 30, 2019), \url{https://www.agco.ca/cannabis/second-allocation-stores-allocation-lottery}. 12
regulations have been amended to allow for this second tranche, whereby the AGCO held an allocation lottery to allow pre-qualified prospective marijuana operators to apply for a Retail Operator License for one of forty-two retail store authorizations in Ontario on August 20, 2019. In addition, the regulations have been amended to allow the AGCO to authorize an additional eight retail store authorizations on First Nations Reserves in Ontario. Unlike the lottery allocation, applications will be accepted on a “first come, first served” basis. Notably, an applicant must receive approval from the applicable First Nations Band Council to operate a cannabis retail store on the subject reserve in order to be eligible to participate in this process.\textsuperscript{106}

6. \textbf{Quebec}

The Government of Quebec enacted the \textit{Cannabis Regulation Act}, which received Royal Assent on June 21, 2018. In Quebec, adults eighteen years or older can possess up to thirty grams of dried marijuana or equivalent in a public space.\textsuperscript{107} The \textit{Cannabis Regulation Act} limits possession in a private residence to 150 grams regardless of the number of persons who live in the residence.\textsuperscript{108} Additionally, an adult cannot possess more than a total of 150 grams of dried marijuana or equivalent in several places. The \textit{Cannabis Regulation Act} also prohibits the cultivation of marijuana for personal use. Marijuana consumption in Quebec is prohibited in alignment with tobacco smoking and vaping laws with the following additional restrictions: on the grounds of health and social services institutions, on the grounds of technical colleges and universities, on bicycle paths, and in bus shelters or shared transportation waiting areas. Like in all provinces, there is zero tolerance for drug-impaired driving.\textsuperscript{109}

To regulate marijuana for recreational purposes, the Quebec government established the Société québécoise du cannabis (SQDC), an offshoot of the province’s liquor board, the Société des alcools du Québec. The SQDC is the only authorized retailer of marijuana in Quebec that can sell in stores or online; thus, there is no licensing process as no private retail system is available.\textsuperscript{110}

7. \textbf{New Brunswick}

The Government of New Brunswick enacted the \textit{Cannabis Management Corporation Act} and the \textit{Cannabis Control Act}, which both received Royal Assent on March 16, 2018.\textsuperscript{111} In New Brunswick, adults nineteen years or older are able to purchase, possess, cultivate, or consume marijuana. An adult may carry up to thirty grams of dried marijuana or equivalent in public. While consumption in public is not permitted, there are no restrictions on how much marijuana can be

\textsuperscript{106} Stores on First Nations Reserves, Cannabis Retail Store Allocation Process for Stores on First Nations Reserves, Alcohol and Gaming Commission of Ontario (last visited July 30, 2019), \url{https://www.agco.ca/cannabis/stores-first-nations-reserves}.

\textsuperscript{107} \textit{Cannabis Regulation Act}, CQLR, c C-5.3, s 4.

\textsuperscript{108} \textit{Id.} at s 7.


\textsuperscript{110} \textit{Id.} at s 25.

\textsuperscript{111} \textit{Cannabis Control Act}, SNB 2018, c 2; \textit{Cannabis Management Corporation Act}, SNB 2018, c 3.
kept at a private residence.\textsuperscript{112} Marijuana kept in a private residence must be secured and inaccessible to minors.

The regulator of marijuana in New Brunswick is NB Liquor, which operates through its subsidiary NB Cannabis. NB Cannabis is the only legal retailer in the province that can sell marijuana in stores and online.\textsuperscript{113} There is only a public system, with no private retailers or licenses available.

8. **Nova Scotia**

The Government of Nova Scotia amended the *Smoke-Free Places Act*, which received Royal Assent on December 13, 2007 and enacted the *Cannabis Control Act*, which received Royal Assent on April 18, 2018. Nova Scotia’s marijuana law allows adults nineteen years or older to possess or buy marijuana.\textsuperscript{114} The *Smoke-Free Places Act*, in conjunction with municipal bylaws, detail where adults can consume marijuana.\textsuperscript{115} Adults in Nova Scotia may possess up to thirty grams of dried marijuana or equivalent in public, with no restrictions on how much marijuana can be kept in a private residence, so long as it is only for personal use.\textsuperscript{116} Additionally, adults are allowed to grow up to four plants per household, but municipalities may implement further restrictions on home cultivation. The rules for transporting marijuana in a car are the same as alcohol; the marijuana must be closed and sealed with the package out of reach of anyone in the vehicle.\textsuperscript{117}

The regulator for marijuana is the Nova Scotia Liquor Corporation (NCLC). The NCLC is the only authorized retailer of marijuana in the province that can sell marijuana in store and online. Nova Scotia’s system is entirely public with no opportunities for private retailers or licenses.\textsuperscript{118}

9. **Newfoundland**

The Government of Newfoundland enacted the *Control and Sale of Cannabis Act*, which received Royal Assent on May 31, 2018. In Newfoundland, the legal age to buy or possess marijuana is nineteen years or older. Adults may possess up thirty grams of dried marijuana or equivalent and may grow up to four plants per household.\textsuperscript{119} Marijuana plants grown in private residences may be grown only indoors or in an adjacent building to the residence, not outdoors.\textsuperscript{120}

\textsuperscript{112} *Id.* at s 12.


\textsuperscript{114} *Cannabis Control Act*, SNS 2018, c 3, s 3.

\textsuperscript{115} *Smoke-free Places Act*, SNS 2002, c 12, ss 5, 5(A), 6 and 7.


\textsuperscript{117} *Id.*

\textsuperscript{118} *Supra* note 114 at s 12.

\textsuperscript{119} *Cannabis Control Act*, SN 2018, c C-4.1, s 64.

\textsuperscript{120} *Id.*
Much like alcohol, marijuana may be consumed in private dwellings or adjacent yards but not in public places, or motor vehicles or boats.\textsuperscript{121}

The regulator, the Newfoundland and Labrador Liquor Corporation (NLC), has set up a mix of public and private retail regimes where adults in Newfoundland may purchase marijuana at stores licensed through the NLC or online through the NLC portal.\textsuperscript{122} Marijuana can be produced only by a federally licensed producer and can be legally sold only to adults by a provincially licensed retailer.\textsuperscript{123}

To open a retail marijuana outlet in Newfoundland, interested applicants were required to submit a proposal during the Request for Proposal for Licensed Cannabis Retailers in February 2018 or May 2018.\textsuperscript{124} Currently, the NLC continues to monitor the retail environment during these early stages of legalization and, if the NLC determines more retail opportunities are necessary, it may post future opportunities for private retailers. Otherwise, there are no current licenses available.\textsuperscript{125}

10. **Prince Edward Island**

The Government of Prince Edward Island enacted the *Cannabis Control Act* (also called *An Act to Respond to the Legalization of Cannabis*), which received Royal Assent on June 12, 2018. Like in most provinces, the law in Prince Edward Island governing marijuana sets the minimum age to purchase, possess and use recreational marijuana at nineteen years.\textsuperscript{126} Adult possession is limited to thirty grams of dried marijuana or equivalent when in public. Marijuana use is restricted to use in private residences. Adults can have up to four marijuana plants in the household. The plants may be grown outdoors so long as they are not accessible to any person not directly invited into the home or any individual under the age of nineteen.\textsuperscript{127} Additionally, the plants may not be visible from public places and must be in a locked enclosure at least 1.52 meters high.\textsuperscript{128}

The marijuana retail system is entirely public, operated by the Prince Edward Island Cannabis Management Corporation (PCMC). The PCMC oversees the operation of four Prince Edward Island marijuana stores and an online platform. The store locations were chosen based on population. Currently there are no opportunities to operate a private retail marijuana outlet.\textsuperscript{129}

\textsuperscript{121} *Id.* at s 75.


\textsuperscript{123} *Id.*

\textsuperscript{124} *Id.*

\textsuperscript{125} *Id.*

\textsuperscript{126} *Cannabis Control Act*, SPEI 2018, c 20, Sched 1, s 7.


\textsuperscript{128} *Id.*

\textsuperscript{129} *Cannabis Management Corporation Act*, SPEI 2018, c 20, Sched 2, s 5.
11. Yukon

The Government of Yukon enacted the *Cannabis Control and Regulation Act*, which received Royal Assent on April 24, 2018 and governs the possession, purchase and sale of marijuana in the Yukon territory.\(^{130}\) Adults who are nineteen years or older are able to possess up to thirty grams of dried marijuana or equivalent and can grow up to four plants her household.\(^{131}\) Adults may purchase marijuana products from a Yukon Liquor Corporation licensed retailer or online from the Yukon Liquor Corporation.\(^{132}\)

The Cannabis Licensing Board governs the issuance of retail marijuana licenses in Yukon.\(^{133}\) To become a licensed cannabis retailer, a prospective applicant must establish that they have not been sentenced to imprisonment for a term of two years or more for specific offenses by submitting a criminal record check.\(^{134}\) There is a Standard Retail License available with two possible sub classes.\(^{135}\) Sub class 1 allows the marijuana retailer to sell other products and substances (like tobacco or alcohol) on the licensed marijuana premises, but not in the designated marijuana area.\(^{136}\) Sub class 2 is more restrictive in that only marijuana and marijuana accessories are to be sold on the licensed premises.\(^{137}\)

For both sub classes, the license period is determined by the Cannabis Licensing Board and begins on the day that the license is issued or renewed and ends on March 31, not more than three years after the date the license was issued or renewed.\(^{138}\) The operating hours for all private retail marijuana stores is 9:00 a.m. to 2:00 a.m. the following day.\(^{139}\) License fees include an initial application fee of $2,050 (CAD), an application fee on renewal of the license of $1,550 (CAD), and an annual license fee of $2,150 (CAD).\(^{140}\)

12. Northwest Territories

The Government of Northwest Territories (NWT) enacted the *Cannabis Legislation and Regulations and Implementations Act* (CLRIA), which received Royal Assent on June 1, 2018.\(^{141}\)

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\(^{130}\) *Cannabis Control and Regulation Act*, SY 2018, c 4, s 1.

\(^{131}\) *Id.* at s 54.

\(^{132}\) *Id.* at s 57.

\(^{133}\) *Id.* at s 21.

\(^{134}\) *Id.* at s 26.

\(^{135}\) *Cannabis Licensing Regulation*, Yuk Reg OIC 2019/43, made under *Cannabis Control and Regulation Act*, SY 2018, c 4.

\(^{136}\) *Id.* at s 2.

\(^{137}\) *Id.*

\(^{138}\) *Id.* at s 3.

\(^{139}\) *Id.* at s 4.

\(^{140}\) *Id.* at s 13.

\(^{141}\) *Cannabis Products Act*, SNWT 2018, c 6, Sched A.
The CLRIA provides that the minimum age to possess or consume marijuana is nineteen years. Adults may possess up to thirty grams of dried marijuana or equivalent and can grow up to four plants per household. Consumption of marijuana is restricted to private property and is not allowed at public events or public spaces used by children.

The Northwest Territories Liquor & Cannabis Commission (NTLCC) is the regulator of marijuana in the province. Adults can buy marijuana at most liquor stores in NWT or online at the NTLCC website. When marijuana was first legalized, there was no private retail licensing option but now an option to apply for a private retail license exists. The CLRIA sets the restrictions and rules for private marijuana retailers. The CLRIA had originally stated that no customers below the age of nineteen were permitted in the store, but the NTLCC confirmed that minors can enter a marijuana store if accompanied by a parent or eligible guardian. In contemplation of minors being allowed to enter the store, all marijuana products must be locked up at all times and available by customer request only. Additionally, all employees will have to undergo specific training on marijuana retail sales.

To be considered as a potential marijuana retail vendor, applicants must submit an expression of interest letter to the Director of the NTLCC. The NTLCC will then conduct an initial community assessment to determine community support and evaluate demand. Once a positive assessment is gathered, a public Request for Proposals (RFP) is released to that community. Notable of this private retail system in NWT is that licensed marijuana vendors enter into a Consignment Agreement with the NTLCC for a period of five years with the option to renew for another five years. It is possible for a licensed marijuana vendor to sell the store and have the Consignment Agreement transferred to the buyer. The buyer must first work with the NTLCC to ensure they qualify to be a designated marijuana vendor. Only after receiving approval can the buyer assume the contract with the NTLCC.

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142 *ld.* at ss 3 and 11.
143 *ld.* at s 34.
146 *ld.* at 6.
147 *ld.* at 21.
148 *ld.* at 9.
149 *ld.* at 4.
150 *ld.*
151 *ld.* at 13.
152 *ld.* at 5.
153 *ld.*
154 *ld.*
Anyone can apply to be designated as a marijuana vendor. Applicants, including owners, directors, shareholders, officers, and investors of the company, must undergo a background check. Importantly, if there is an interest or connection to a federally licensed producer, an applicant may still be considered but these interests must be kept separate. Unlike in some provinces, there is no set cap on the number of marijuana vendors in NWT. The application fee to become a designated marijuana vendor is $1,000 (CAD).

13. Nunavut

The Government of Nunavut enacted the Cannabis Act and Cannabis Statutes Amendments Act, both of which received Royal Assent on June 13, 2018. Together these statutes set the rules for marijuana use, possession, and sale in the province. To consume or possess marijuana, adults must be nineteen years or older and may only purchase marijuana from licensed agents of the Nunavut Liquor and Cannabis Commission (NULC). As in many other provinces, thirty grams is the maximum amount of dried marijuana or equivalent an adult can buy or carry at any time. The consumption of marijuana in public places is restricted, but consumption in private residences or licensed smoke lounges is permitted. Adults may also grow up to four plants per household. There is a zero tolerance policy for driving under the influence of marijuana, and marijuana may not be within reach of anyone in a vehicle.

The NULC regulates the marijuana industry in the territory and sells marijuana online, by phone, or in stores. The Cannabis Act allows the Government of Nunavut to license establishments that sell marijuana, including stores and smoking lounges. As of March 2019, the Government of Nunavut continues to work on the regulations to guide this licensing system.

C. Franchising in Canada

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155 Id. at 2.
156 Id.
157 Id.
158 Id at 4.
159 Cannabis Act, S Nu 2018, c 7; Cannabis Statutes Amendments Act, S Nu 2018, c 8.
162 Id.
163 Id.
164 Id.
165 Supra note 160.
166 Supra note 159 at s 8.
Despite the patchwork of marijuana retail legislation across Canada, franchisors of marijuana retail concepts have established themselves as strong players in the industry. In those provinces that allow privatized marijuana retail sales from brick-and-mortar locations, the franchise business model is an attractive means of identifying operators to scale and develop unit-count. In the provinces of Quebec, New Brunswick, Nova Scotia, and Prince Edward Island, each respective provincial government, through its designated regulatory authority, is the exclusive retailer of recreational marijuana, thereby complicating franchising opportunities. In the balance of the provinces and territories in Canada, three of the most populous of which are detailed below, a regulatory framework that permits private operators to obtain licensure provides fertile ground for franchise expansion.

As in any other franchised business system, a franchisor of a marijuana retail concept can offer to duly licensed franchisees the benefit of being party to a franchise network, brand strength and notoriety, a set of standards and business infrastructure, industry knowledge, and assistance in operating within a regulated retail environment. The marijuana legal, regulatory and business landscape is rapidly growing and evolving, and franchising may provide potential retailers with the most efficient and pragmatic manner to develop and begin operating a retail store given the added complications that accompany the sale of one of the mostly highly regulated consumer products in the country where third party expertise and assistance may be invaluable.

Franchising in the marijuana industry in Canada is not without its challenges. For those provinces where private retail operation is permitted, franchising has not be consistently addressed or considered in the applicable legislation, and as a result franchisors are left to ensure with great care that their business structure and methods of delivering support comply accordingly.

1. **Franchising in Alberta**

The regulations in force in the Province of Alberta provide as follows:

Before issuing a licence the board must be satisfied that its issuance will not result in more than 15% of the total number of issued cannabis licences being held by

(a) one person; or

(b) a group of persons in circumstances where, in the opinion of the board, more than 15% of the total number of issued cannabis licences are or would likely be subject to common control in any material aspect.\(^\text{168}\)

The term “common control” only appears once in the regulations, in the above-quoted section, and is not defined in its enabling statute. Franchisors and their attorneys will grapple with the question as to whether a franchise system could constitute “common control” in the opinion of the governing body. Franchisors can take steps to limit the amount of “control” exercised over their prospective franchisees in an attempt to avoid the application of this provision; however, as this determination is made by the AGLC, it is difficult to predict the outcome. While, at the time of

\(^{168}\) *Gaming, Liquor and Cannabis Regulations, Alta Reg 13/2018, ss 13 and 106.*
this writing, the AGLC has not, to the authors’ knowledge, deemed franchising to be tantamount to “common control,” franchisors may need to revisit their growth strategies in this province should this interpretation be adopted. In the meantime, franchisors of marijuana retail concepts are subject to investigation as part of the AGLC’s review of a franchisee’s application for licensure.

2. **Franchising in British Columbia**

In the Province of British Columbia, the government did not place a cap on the total number of retail licenses to be issued; however, any single applicant or “group of related persons” may not hold more than eight retail store licenses.

The eight retail store cap presumably applies to the franchisor and its network, effectively limiting any system to a maximum of eight stores within the province. The determination as to whether persons are “related parties” for the purposes of this cap is made by the “general manager,” being a regulatory authority. If in the opinion of the general manager, a franchisor, “through an association, financial interest or family or other connection” is “(a) likely have direct or indirect influence over licensees who hold more than 8 retail store licences, (b) likely be able to affect, directly or indirectly, the activities carried out under more than 8 retail store licences, or (c) have the influence referred to in paragraph (a) or the ability to affect activities referred to in paragraph (b) with respect to more than 8 retail store licences,” then this cap will apply.\(^{169}\)

3. **Franchising in Ontario**

In the Province of Ontario, franchisors and their counsel must carefully review the language of their proposed agreements with franchisees, and the extent of their control over the methods of operations of these outlets, so as not to run afoul of the “control-in-fact” prohibitions contained in the legislation. Ontario has specific prohibitions against the involvement of licensed producers of marijuana and their affiliates that could extend to their capacity as franchisors, or partial owners of franchisor. Under the regulations, an “affiliate”\(^ {170}\) is broadly defined and a “licensed producer” means “a person who is authorized by a licence issued under the Cannabis Act (Canada) to produce cannabis for commercial purposes.”\(^ {171}\) Pursuant to the Cannabis License Act, 2018 (Ontario), an applicant and a holder of a Retail Operator Licence may apply for a Retail Store Authorization, subject to the regulations.\(^ {172}\) A licensed producer is subject to certain restrictions in respect of a Retail Store Authorization application, including that “the person and its affiliates, as defined by the regulations, may not between them hold more than one retail store authorization.” Accordingly, a licensed producer (and its affiliates) cannot own or control various retail business in Ontario.

In the second allocation lottery conducted in Ontario in August 2019, any “holder of a cultivation, processing or nursery licence issued by Health Canada under the Cannabis Act

\(^ {169}\) Cannabis Licensing Regulation, BC Reg 202/2018, s 6, made under Cannabis Control and Licensing Act, SBC 2018, c 29.

\(^ {170}\) General, O Reg 468/18, s 2, made under Cannabis Licence Act, 2018, SO 2018, c 12, Sched 2.

\(^ {171}\) Id. at s 1.

\(^ {172}\) Supra note 99 at s 4.
(federal)” was not permitted to submit an expression of interest application under the Cannabis Retail Store Allocation Lottery Rules published by the AGCO. Any franchisor which is a holder of such licensure or falls within the definition of “affiliate” would not have been able to submit an expression of interest in the latest lottery held in Ontario and would be subject to the one-store cap set out above. While there can be a strong nexus between licensed producers and franchisors (or licensed producers as franchisors), there are legal bounds to such structures. The Government of Ontario has taken specific steps to curb the potential monopoly of licensed producers of the market by way of vertical ownership. These steps have left room for the franchise model, where the parameters of control are carefully addressed.

One of the elements of the test for an “affiliate” under the Regulations is whether one person exercises “control in fact” over the licensed retail store. Generally, a franchisee is not an affiliate of its franchisor, but rather it is an independent business owner-operator which has been issued a license to use certain marks and a set of system standards owned by the franchisor. While there are certain controls in place to ensure the compliance with such system standards, the franchisor does not control the day-to-day operations of the franchisee’s business. In fact, the definition of “franchise” under Ontario’s franchise legislation contemplates that a franchisor will exercise significant control over or offer significant assistance to its franchisees in connection with the franchisee’s method of operation (including building design and furnishings, locations, business organization, marketing techniques or training). Control over a franchisee’s actual day-to-day operations is generally outside the scope of the franchise relationship.

Under the subject regulations, a “person is deemed to be an affiliate of another person if the other person, or a group of persons or entities acting jointly or in concert with the other person, has any direct or indirect influence that, if exercised, would result in control in fact of that person.” The phrase “control in fact” has not been defined in the enabling legislation or the regulations; however, control in fact has traditionally been interpreted as relating to a party’s ability to control the corporate governance and ownership interests of another party, which is materially different than the hallmark of the franchise relationship. Canadian franchise attorneys have argued that because a franchisor does not exercise ‘control in fact’ but only control over the “method of operation” over an independently owned franchise outlet, there is room for licensed producers of marijuana to act in the capacity of franchisors.

4. Advertising

On the federal level, the Cannabis Act strictly regulates the promotion, packaging and labelling of marijuana and marijuana accessories and services related to marijuana. Other than the inclusion of one brand element, prescribed packaging cannot be altered so as to


175 Id.


177 Cannabis Regulations, SOR/2018-144 at s. 130(9)
differentiate one system’s offering from another’s. In order to comply with these restrictions, traditional advertising approaches and certain brand standards must be revisited by the franchisor. Under the traditional franchising model, franchisors would encourage local advertising and may have permitted franchisees to prepare their own advertising materials. When franchising in the marijuana industry, franchisors should revise their franchise agreements to reflect strong directions regarding advertising, marketing, and promotion.

5. **Site Selection and Leasing**

In addition to the legislative and licensing hurdles, traditional territory determination, site selection, and leasing models may not apply to the marijuana retail franchise industry. Local governments and municipalities have various levels of influence in the licensing process across Canada, which can result in the stalling or termination of the licensing process for an applicant. While franchisors are familiar with the old adage “location, location, location,” finding a suitable location for a marijuana retail unit will be markedly more difficult as there are zoning and local regulations that must be complied with, landlords who are likely to charge additional deposits (which will affect the franchisee’s initial cash flow), and additional build-out costs to adhere to security requirements.

Similarly, under a traditional franchise agreement, the franchisor often retains the powerful remedy to assume the business operations (and potentially the lease) of the franchisee in the event of a default. But in the marijuana retail context, the operator of a store must be authorized by the appropriate provincial body as described above. As a result, a franchisor cannot simply seize the inventory of the franchisee, exercise step-in rights to manage the store, or take an assignment of the lease for the purposes of operating the franchised business. As the franchisee’s marijuana retail licenses are not automatically transferable, the franchisor will likely be required to apply under the then-current provincial framework to obtain its own licensure.

Both the process of qualifying a location and territory as well as the premises-related rights under the franchise agreement should be reviewed carefully to ensure that the franchisor is able to exercise its discretion and rights in accordance with applicable law. Furthermore, if the prospective franchisee must submit evidence of its right to possession to a specific premises as part of its application process, as was the case in the Province of Ontario during the second allocation lottery, then franchisors and franchisees may find themselves in a difficult scenario regarding the timing of the signing of the franchise agreement, lease agreements, and disclosure.

6. **The Evolving Experience of Canadian Franchisors**

Ultimately, franchisors are experts in the retail industry and marijuana represents a new market of retail goods. Franchisees could benefit greatly from this expertise and brand notoriety, particularly those without previous retail experience. As operator licences are not transferable in most provinces at this time and there are significant regulatory hurdles to transfer in other provinces, if a party wishes to operate under a particular cannabis brand umbrella, the best or only option would be to become a licensee (or franchisee) of such system.

Franchisors are left to find the balance between establishing controls through the operative agreement which do not overstep any regulatory prohibitions from the perspective of the applicable governing body and the practical need to have enforceable rights and remedies as
against a franchisee which allow the franchisor to effectively manage its system. Like franchise law in Canada, marijuana control and licensing laws are governed at the provincial level. A franchisor who wishes to franchise across Canada, in such provinces which permit private retail, will be tasked with navigating the nuances of each province’s regulatory regime. And these regulatory regimes are changing and evolving in unprecedented manners. Any franchisor in this space must be able to react and adapt to the changing landscape and ensure that its franchise agreement ascribes to it sufficient flexibility to allows the system to do the same.

While marijuana retailing is heavily regulated, and there are certain legal hurdles that franchisors are required to jump over in order to gain access to this space, many franchisors in Canada have done so already, and this trend does not appear to be slowing down.

IV. FRANCHISING CANNABIS BUSINESSES IN THE UNITED STATES

A. The History of Cannabis Law in the United States

Prior to the early twentieth century, people could legally grow and consume cannabis in the United States. George Washington grew hemp at Mount Vernon. Between 1850 and 1942, physicians and pharmacists used cannabis to treat a wide range of ailments, and marijuana was recognized in the United States Pharmacopoeia, the official list of recognized medicinal drugs. In 1910s, the recreational use of marijuana started to become more popular. Unfortunately, marijuana critics deployed racist stereotypes and fear to promote laws making the growth, possession, and consumption of marijuana illegal. In 1913, California passed the first law prohibiting the recreational use of marijuana and, by 1936, recreational marijuana use was illegal in 48 states. In 1937, the federal government limited medical marijuana use through the Marihuana Tax Act, which imposed a registration tax and substantial record keeping requirements on individuals and business offering marijuana for medical use.

In 1970, Congress sounded the death knell for legal marijuana use when it enacted the Controlled Substances Act (CSA). Under the CSA, cannabis is classified as a Schedule I

180 Id.
182 Id. at 51–52 (explaining that Harry Anslinger, the director of the Federal Bureau of Narcotics claimed that “50 percent of violent crimes committed in districts occupied by Mexicans, Greeks, Turks, Filipinos, Spaniards, Latin Americans, and [African-Americans] may be traced to the roots of marihuana” and that “Marihuana causes white women to seek sexual relations with [African-Americans].”); William Randolph Hearst also used his vast media empire to extoll the dangers of marijuana use and praised Mussolini’s and Hitler’s efforts to eliminate its use.
184 Id.
drug. Schedule I is the highest level of classification and reserved for the most hazardous drugs with “high abuse potential and no acceptable medical use.” Accordingly, the cultivation, possession, sale and use of marijuana in any form, for any reason is prohibited.

In 1996, California, the first state to make recreational marijuana use illegal, legalized (at the state level) medical marijuana use in the Compassionate Use Act, which removed criminal penalties for the use, possession, and cultivation of medical marijuana. As of the spring of 2019, ten states and the District of Columbia have legalized marijuana for recreational use (although Vermont and the District of Columbia do not permit marijuana to be sold commercially). Thirty-three states have legalized marijuana for medical use. Twelve more states have legalized “low THC, high cannabidiol” (CBD) products for limited medical use or as a legal defense to criminal charges. Only Idaho, South Dakota, Nebraska, and Kansas completely prohibit cannabis use.

Legalization at the state level does not negate the CSA. The United States Supreme Court has repeatedly held that the federal government has the power to criminalize and enforce all marijuana-related conduct, even in states that have legalized its growth, possession, and use in some form.

Because marijuana use is legal in virtually every state in some form, and the legal marijuana industry generates more than $10.4 billion dollars (USD) in sales, $632 million (USD) in taxes, and employs more than 250,000 people, legal commentators note that it “appears unlikely that the federal government could realistically stamp out marijuana sales.”

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186 Id.
188 21 USC § 812.
190 Supra note 3.
192 Supra note 3.
193 Id.
194 See United States v. Oakland Cannabis Buyer’s Collective, 532 U.S. 483 (2001) (holding that medical necessity is not a defense to federal drug charges even when California had legalized the medical use of cannabis because the CSA classified cannabis as having no medical benefits); Gonzales v. Raich, 545 U.S. 1 (2005) (congress may criminalize the production and use of homegrown marijuana under the commerce clause even it was legal for medical use in the state in which it was grown). See also Sam Kamin, The Battle of the Bulge: The Surprising Last Stand Against State Marijuana Legalization, 45 J. OF FEDERALISM 427 (2015).
196 Id.
197 Id.
Understanding the federal approach to marijuana businesses is challenging. In 2013, the Attorney General for the Obama administration issued a memorandum (the Cole II Memo) which stated that the Justice Department is “committed to using its limited . . . resources to address the most significant threats” and listed eight key federal law enforcement priorities including preventing the sale of distribution of marijuana to minors and to states where marijuana is not legal; preventing bad actors from using state authorized marijuana activity as a pretext for other illegal activities; preventing the revenue from marijuana sales from going to illegal enterprises; preventing the use of violence firearms in marijuana industry; preventing the growth and use of marijuana on federal land and federal properties; and preventing drugged driving and other public health concerns.\(^\text{198}\) The Cole II Memo indicated that a marijuana business that strictly complied with state laws and refrained from the listed behavior would not be an enforcement priority.

In 2018, Attorney General Jeff Sessions withdrew the Cole II Memo and issued new guidance that discussed the CSA, money laundering statutes, and banking laws, and stated that “prosecutors should follow well-established principles that govern all federal prosecutions” when “deciding which marijuana activities to prosecute under these laws with the Department’s finite resources.” Attorney General William Barr further muddied the issue when he stated in his 2019 confirmation hearing that while he “did not support the wholesale legalization of marijuana” he did not intend to prosecute “parties who have complied with state law in reliance on the Cole Memorandum.”\(^\text{199}\) But Attorney General Barr has not issued any formal guidance rescinding the Sessions memorandum or reinstating the Cole II memo. Given the sheer size of the marijuana industry in the United States, it is unlikely that the Justice Department will attempt to eliminate the industry through criminal prosecution. But advocates for legalization continue to pursue federal legalization.

B. Challenges to Marijuana Franchises

Despite significant in-roads having been made in numerous states, marijuana remains illegal under federal law.\(^\text{200}\) Conversely, federal law recently removed hemp from Schedule I controlled substances, thus opening the door for hemp-based CBD as a viable commercial product.\(^\text{201}\) Nonetheless, there still remain significant disparities between federal and state law for low THC hemp. Finally, each state has complex laws and regulations regarding marijuana businesses. Many of these state law and regulations contradict similar laws in other states.

The legal uncertainty and status of cannabis in the various states presents numerous practical and legal challenges for the unwary franchisor and its franchise owners in the traditional franchise model of business. These challenges affect all aspects of the franchise system,


including the areas of: (1) ownership; (2) regulatory matters specific to the industry; (3) royalty fees; (4) banking; (5) trademarks; (6) sourcing and distribution; and (7) enforcement. Although a few companies appear to offer marijuana franchises, the authors were unable to identify any operational marijuana franchises or any active franchise registrations in any state that makes registrations available online.

1. **Ownership**

   a. **The Franchisor**

      As an initial matter, a company considering franchising should be located in a state where the marijuana product is legal under state law. Then, depending on whether the marijuana product is legal under federal law (hemp) or not (marijuana), the company should consider limiting its franchise offerings to the state in which it is located in order to avoid interstate commerce.\(^\text{202}\) In doing so, a company theoretically could have up to 23 FDDs and up to 23 separate franchise entities (as of the writing of this paper, 23 states have approved the sale of marijuana in some form) that would also offer franchises.

   b. **Affiliates**

      If a franchisor is launching a 23-state franchise initiative at the onset, it would need to list the 22 affiliates that offer franchises in each FDD.\(^\text{203}\) If the franchisor takes a one at a time approach and establishes new affiliates as it launches into new states, it will have to amend each FDD when a new affiliate is introduced. Franchisors will need exceptional organizational and tracking skills to maintain and update these FDDs (and run these separate franchise entities).

2. **Laws or Regulations Specific to the Industry**

   Another affected area in the franchise system is the disclosure of laws or regulations specific to the industry. While federal law recently removed hemp (defined as marijuana with less than 0.3% THC on a dry weight basis) from Schedule I controlled substances, thus opening the door for hemp-based CBD as a viable commercial product,\(^\text{204}\) there still remain significant disparities between federal and state law for low THC, hemp-based marijuana. Each state has complex laws and regulations regarding marijuana businesses. Many of these state laws and regulations contradict similar laws and regulations in other states.

   Item 1 of the FDD calls for the disclosure of any laws that apply the franchised business specifically.\(^\text{205}\) Here, the franchisor must describe the federal law pertaining to marijuana and list

\(^{202}\) Please note that, whether legal under state or local law, the possession, use, distribution or sale marijuana are all federal crimes. This article is not intended to give any legal advice, or offer any opinions concerning the legality of franchising in a marijuana or other cannabis related business.


\(^{205}\) Id.
each state’s applicable marijuana laws. Similarly, there may also be additional marijuana laws or local regulations in the various cities and counties. Certain towns or counties may prohibit the sale of marijuana even though it is legal statewide. In Colorado, which is known for its “legalized” recreational marijuana dispensaries, the majority of smaller towns and cities still ban retail marijuana at the local level.\textsuperscript{206} This may also raise franchise territory issues.

Franchisors should also describe the licensing process and the availability of marijuana licenses in the state. Franchisees may be restricted from operating a certain type of franchise (retail or manufacturing) depending on the licenses they obtain and state specific laws.

3. \textbf{Royalty Issues}

Royalty payments, which of course are fundamental to the franchise system, present another area of risk to the franchisor.\textsuperscript{207} Even in states that have legalized marijuana, there are often licensing requirements to the sale of the marijuana product. In such circumstances, indirect revenues through the receipt of royalty payments by an unlicensed entity (the franchisor) may represent a legal grey area, or may be outright illegal. And it certainly could be precarious for a company to obtain a royalty based on the sale of a product that is currently illegal to possess, manufacture, or sell in the franchisor’s home state. State laws are going to be playing catch-up in this area, and it may be some time before there is any real clarity in the marketplace. But in Washington state, the legislature recently passed a law removing royalty and licensing agreements relating to the use of intellectual property from the definition of “true parties in interest” of a licensed marijuana business (and the vetting process otherwise applicable to investors and financiers of a marijuana business), so long as those royalty or licensing agreements are disclosed to the state licensing board and the royalty fee is no greater than an amount equal to ten percent of the licensed marijuana business’s gross sales of the product.\textsuperscript{208} The effect of this new state law will be to exempt a franchisor from also having to qualify for a cannabis business license.\textsuperscript{209} Other states may eventually follow.

4. \textbf{Banking}

Banking also presents a challenge to a franchised marijuana practice because marijuana businesses often lack access to capital and financial products from banks. While no federal law expressly prohibits marijuana businesses from having bank accounts, the Department of Treasury has released guidance to banks that provides for burdensome due diligence and reporting requirements before a bank should consider allowing a marijuana business access to its accounts or other banking services.\textsuperscript{210} Notably, banks that violate law can lose their Federal Deposit


\textsuperscript{207} The FTC Rule defines a franchise as any continuing commercial relationship or arrangement that, among other things, includes that “as a condition of obtaining or commencing operation of the franchise, the franchisee makes a required payment or commits to make a required payment to the franchisor or its affiliate.” See 16 CFR § 436.1(h).


\textsuperscript{209} Ibid.

\textsuperscript{210} Supra note 195 at 29.
Insurance Corporation (FDIC) deposit insurance, and may even be subject to criminal penalties in some cases.\textsuperscript{211} 

As a result, many marijuana businesses report difficulty securing financing and credit products to start or expand their businesses, and in establishing accounts to manage cash flow and business expenses. Most large banks will not work with marijuana companies. This has led most marijuana businesses to operate on a cash basis.\textsuperscript{212} A cash-only business model poses a huge challenge to the franchisor’s ability to collect fees from the franchisee. Will the franchisor require payments in cash from the franchisee? What protections will the franchisor have against underreporting? Even if a franchisor is able to find a financial institution that will work with marijuana businesses, it must also plan for the possibility that either the franchisor or the franchisee may lose this banking option at any time. The franchisor should include multiple payment options and notification requirements. The franchisor should also seek out a point-of-sale system suited for cash operations.

Banking practices are fluid in nature and likely will adapt over time. It is notable, however, that even after the passage of the 2018 U.S. Farm Bill, the newly legal hemp industry continues to face barriers with obtaining banking and financial services.\textsuperscript{213} This has led to a recent rare bipartisan effort to end discrimination faced by lawful hemp producers in the banking and financial services industry.\textsuperscript{214}

5. Trademark

Federal trademarks are allowed only for goods and services lawfully used in commerce.\textsuperscript{215} Because of this requirement, franchisors are unable to obtain federal registrations for the retail sale of marijuana. Franchisors will have to look to state trademark laws and common law to protect their trademark rights. This could be problematic in establishing a 23-state brand because most states require that a trademark be in use before obtaining these rights.\textsuperscript{216} Additionally, some marijuana licenses require that the trademark be owned by the license holder. Franchisors should prepare multiple brand strategies to provide flexibility in those states where their primary trademark is not available. Franchisors should include a trademark assignment provision in their franchise agreements, assigning all rights and goodwill in the trademark back to the franchisor upon the expiration or termination of the franchise agreement.

\textsuperscript{211} Id.
\textsuperscript{212} Id.
\textsuperscript{213} Id.
\textsuperscript{214} In April 2019, U.S. Senators Ron Wyden (D-OR) and Senate Majority Leader Mitch McConnell (R-KY) sent letters to four federal banking and financial regulatory institutions, including the Federal Deposit Insurance Corporation (FDIC), the Office of the Comptroller of the Currency (OCC), the Federal Reserve System, and the Farm Credit Administration (FCA). The letters generally presented that the hemp industry “continues to face challenges with regulatory uncertainty as federal agencies work to implement this significant change in federal law,” and urged the regulatory bodies to “offer guidance to ease any concerns” banks may have regarding engaging with or providing services to hemp businesses. See McConnell-Wyden Letters to FDIC, OCC, Federal Reserve, and FCA (last visited July 30, 2019), https://senmcconnell.app.box.com/s/6383dmky9nklo9kvp33rkcdayc4mnnkk.
\textsuperscript{215} 15 USC § 1127.
6. **Sourcing and Transportation**

One of the key elements of a franchise system is the uniform mix of proprietary products from approved suppliers. Unfortunately, because marijuana products are regulated entirely at the state level, and cannot legally be transported across state lines, establishing a common “menu” of products, and ensuring a consistent and adequate supply, will be challenging for franchisors and franchisees.

Several states require marijuana businesses to test the THC and CBD levels in their products as well as for contaminants such as mold and pesticides. Some states such as Alaska and California require that the testing be performed by third party laboratories.\(^{217}\) Maryland law requires that third party laboratories get state approval.\(^{218}\) Massachusetts requires all laboratories either to be accredited by specific third party organizations or have state approval or accreditation.\(^{219}\) Finally, some states like Arizona and Rhode Island have no current regulations for the testing of marijuana products.\(^{220}\) Each state created its own testing standards. Some states like Washington test for THC content while others, like New Jersey, test only for the presence of contaminants.\(^{221}\) Testing requirements vary widely and are subject to change. For example, in 2019, the Washington state legislature transferred oversight of independent marijuana testing from the Liquor Control Board to the Department of Ecology.\(^{222}\)

In addition to regulating the content of marijuana products, many states also regulate the appearance of marijuana products and their packaging. States are most concerned with products or packaging that might appeal to children. For example, in Washington, state regulations limit the color of the text and background on packaging, and marijuana businesses must select any additional colors from a list of sixteen colors.\(^{223}\) Packaging may use no more than three colors.\(^{224}\) Washington law also regulates the shapes of edibles.\(^{225}\) Shapes that would appeal to children such as stars, hearts or gummi bears are all prohibited.\(^{226}\)

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\(^{218}\) *Id.*

\(^{219}\) *Id.*

\(^{220}\) *Id.*

\(^{221}\) *Id.*


\(^{224}\) *Id.*

\(^{225}\) *Id.*

\(^{226}\) *Id.*
Finally, marijuana businesses cannot legally transport product across state lines.\footnote{227} The penalty for a first-time offense is up to five years in prison and a fine of up to a million dollars.\footnote{228} Even states that have legalized marijuana still forbid transporting it across state lines.\footnote{229} Oregon, Nevada, and California law all forbid interstate transportation.\footnote{230} In Nevada, transporting marijuana across state lines is a felony and subject to two to ten years in prison and a $10,000.\footnote{231} Marijuana businesses also need to be aware that federal regulations give U.S. Customs and Border Protection the authority to operate within 100 miles of any U.S. external entry, including coastline.\footnote{232} This means that marijuana business in all of Florida, and significant parts of Washington, Oregon, and California could be subject to federal enforcement. One marijuana attorney reported that a client was transporting marijuana in Washington State near the U.S. Canadian border when they encountered U.S. Customs enforcement officers. The client was not charged but “had everything seized.”\footnote{233}

7. **Enforcement**

Another challenge that potentially faces franchisors is the dispute resolution mechanism to enforce the franchise agreement. Despite recent significant in-roads with respect to using the court system for business disputes involving marijuana businesses, the possession, use, distribution, and sale of high-THC marijuana or marijuana remain illegal under federal law.\footnote{234} Accordingly, neither federal nor state courts provide an ideal forum for disputes arising under the franchise agreement. For marijuana businesses, franchisors instead would likely rely on extrajudicial methods, such as arbitration clauses, to confidentially resolve any disputes outside the courtroom. Arbitration proceedings are based on contract and are almost always private proceedings, and formal pleadings, motions, witness testimony and other data can be kept confidential by explicit agreement of the parties.\footnote{235}

To do so, the franchisor would have to ensure that the franchise agreement contains a precise alternative dispute resolution (ADR) clause requiring arbitration of “any” disputes arising out of or related to the franchise agreement or relationship. The franchise agreement should also make confidentiality in arbitration an explicit requirement in the agreement. For example, the franchisor would be well-advised to include provisions such as the following:

\begin{itemize}
\item \footnote{227} 21 USC § 812.
\item \footnote{229} *Id.*
\item \footnote{230} *Id.*
\item \footnote{231} *Id.*
\item \footnote{232} *Id.*
\item \footnote{233} *Id.*
\item \footnote{235} American Bar Association, *AAA Statement of Ethical Principles* (last visited July 30, 2019), \url{https://www adr.org/StatementofEthicalPrinciples}.  
\end{itemize}
• The parties agree, and the arbitrator shall issue an order providing, that all pleadings, motions, discovery responses, depositions, witness testimony, and all documents or data exchanged or filed in relation to the arbitration be kept strictly confidential;

• The parties agree, and the arbitrator shall issue an order providing, that any award issued by the arbitrator shall remain confidential and be entered under seal in a court of competent jurisdiction; and

• The parties agree that any party may seek a separate order from a court of competent jurisdiction enforcing the arbitrator’s order protecting the disclosure of the proceedings and all testimony and evidence in the arbitration, provided that such motion and responses thereto shall be filed under seal.

Of course, the parties must recognize that these contractual steps offer only a limited assurance of confidentiality. Courts may seal a judicial proceeding to confirm an arbitration award, but are not compelled to do so. Instead, courts may engage in a balancing test, weighing the public interest in disclosure of the information on the one hand and the parties' interest in maintaining the confidentiality of the information on the other. As one might expect, the results of such a balancing test are frequently uneven.

Nevertheless, an order from the arbitrator or arbitration panel requiring that the proceeding be private and confidential based on the explicit terms of the arbitration agreement between the parties can be key in preventing future disclosure. Indeed, courts have relied on such orders to block access to arbitration information or material. To further ensure that such procedures are followed, the parties might also consider including a liquidated damage provision for breach of any of the above procedures. Taking these steps will dramatically increase the probability that private arbitration proceedings will remain private.

A recent case illustrates the importance of drafting an effective and enforceable ADR clause. In Atkinson v. Rose, the Washington court of appeals found that the parties to an agreement to run a marijuana retail business were not bound to arbitrate their dispute because the ADR clause explicitly applied only to a “deadlock,” which the agreement defined as the parties’ failure to “reach an agreement” following “negotiations.” Concluding that the parties had not engaged in “negotiations” necessary to reach such a “deadlock,” the court refused to enforce the

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238 Compare Jessup v. Luther, 277 F.3d 926, 928 (7th Cir. 2002) (holding that although settlement agreements and arbitration awards generally are private, a document is presumptively public once it is filed in court record), with City of Newark v. Law Dep’t of City of New York, 754 NYS2d 141, 144 (N.Y. Sup. 2002) (deferring to arbitration order that specifically mandated arbitration proceedings remain private and confidential); and Health Plan Inc. v. BJC Health Sys. Inc., 30 S.W.3d 198, 203-04 (Mo. Ct. App. 2000) (deferring to arbitration confidentiality order just at it would “any other arbitration award,” which was signed by both parties and the arbitration panel).

239 City of Newark, 754 NYS2d at 144; Health Plan Inc., 30 S.W.3d at 203-04.

ADR clause and remanded the dispute back to the trial court.\textsuperscript{241} A clearer and more comprehensive ADR clause easily could have avoided such a result.

One notable shortcoming to the arbitration process is in the resolution of non-compete obligations under the franchise agreement. While the relevant arbitration rules usually allow an arbitrator to grant a temporary injunction or enter some sort of preliminary relief, a company that wishes to obtain such relief must first select an arbitrator and then schedule a hearing. These steps can result in a loss of precious time—sometimes days or weeks during which the franchisee or its owner, manager, or other employee can violate the agreement causing irreparable harm to the franchisor.\textsuperscript{242} In contrast, the same franchisor generally could obtain a temporary restraining order in court the same day it files a suit to enforce the non-compete agreement.

C. \textbf{CBD Challenges}

The 2018 Farm Bill legalized the production of hemp, a variety of the marijuana plant that is rich in CBD but generally contains less than .3 percent THC.\textsuperscript{243} CBD products are popular and have significant growth potential. Chris Burggraeve, a former Coca-Cola and InBev executive, called CBD “the new avocado toast.”\textsuperscript{244} Both Martha Stewart\textsuperscript{245} and Willie Nelson\textsuperscript{246} market their own branded CBD products. The CBD industry may be appealing to franchisors either as a new franchise system or as additional products to be sold within an existing system. In either scenario, franchisors or franchisees interested in CBD products will face significant hurdles.

Ironically, unlike marijuana, CBD’s illegality under state law poses the most significant problem to the franchise model. In states like Texas, state police have raided businesses selling CBD. In one case, the state police confiscated $50,000 (USD) of CBD inventory, employee cell phones and cash.\textsuperscript{247} Neither the business owner nor the employees were arrested. People selling CBD products have also been arrested in Ohio and Nebraska.\textsuperscript{248} Enforcement may vary from state-to-state or city-to-city. Additionally, there is no current police field test that is capable of distinguishing between CBD derived from hemp and marijuana.\textsuperscript{249}

\begin{flushright}
\textsuperscript{241} \textit{Id. at} *5. \\
\textsuperscript{244} \textit{Supra} note 8. \\
\textsuperscript{245} Emily Price, \textit{Martha Stewart is launching her own CBD line}, Forbes (Feb. 28, 2019), https://www.forbes.com/sites/emilyprice/2019/02/28/martha-stewart-is-launching-her-own-cbd-line/#f4a290bdabd2. \\
\textsuperscript{246} \textit{Supra} note 8. \\
\textsuperscript{248} \textit{Supra} note 243. \\
\textsuperscript{249} Frank Green, \textit{As Virginia’s Industrial Hemp Markets Take Off, Police Have No Quick Way to Tell If It’s Marijuana}, Richmond Times Dispatch (May 17, 2019), https://www.richmond.com/news/virginia/as-virginia-s-industrial-hemp-market-takes-off-police-have/article_07abeeff-d888-5e2d-90bd-5ba569a754e6.html.
\end{flushright}
Like marijuana businesses, businesses selling CBD products will face significant challenges moving products across state lines. For example, while hemp is now legal under federal law, Idaho’s marijuana statute outlaws the possession of a marijuana plant with any detectable amount of THC.\textsuperscript{250} This discrepancy came as an unpleasant surprise to an Oregon truck driver who now faces fifteen years in prison after he was arrested outside Boise with eighty-four hemp plants in his truck.\textsuperscript{251}

CBD-based franchises would also face unique challenges in terms of what products they can sell. Although the 2018 Farm Bill legalized CBD-based products, and the Food and Drug Administration approved a CBD-based prescription medication, the FDA maintains that “adding CBD oil to food products is the same as adding a prescription drug.”\textsuperscript{252} Additionally, under the Food, Drug and Cosmetics Act (FDCA) any substance that is intentionally added to food is subject to FDA pre-market approval unless the substance is generally recognized as safe, which CBD is not. In December of 2018, the FDA issued guidance stating that it remains unlawful under the FDCA to “introduce or deliver for introduction into interstate commerce any food to which CBD or THC has been added.”\textsuperscript{253} Federal guidelines also prohibit the addition of CBD to alcoholic beverages.\textsuperscript{254} In April of 2019, the U.S. Alcohol and Tobacco and Trade Bureau guidance stating that it would not currently approve the use of CBD in the formulation of beer, wine, or liquor.\textsuperscript{255}

The regulatory landscape at the state level is equally confused. California, Georgia, and New York City have all banned CBD from foods. In Washington, a café owner was able to serve CBD infused “wellness” lattes for two weeks before the health department intervened and prohibited the sale.\textsuperscript{256} On the other end of the spectrum, the Colorado Department of Public Health and the Environment issued guidance stating that “all parts of the industrial hemp plant is allowed as a food ingredient,”\textsuperscript{257} and the Missouri Division of Alcohol and Tobacco Control issued an industry circular that states the division “has no authority” to regulate the use of CBD oil that has no THC content.\textsuperscript{258}


\textsuperscript{251}Id.

\textsuperscript{252}Supra note 242.


\textsuperscript{255}Id.


\textsuperscript{257}Industrial Hemp Policy, Colorado Department of Public Health and Environment (last visited July 30, 2019), https://drive.google.com/file/d/15jUlZ0wMrSoejP0wxY4uSLBBHNUF4u9V/view.

It may be slightly easier to obtain trademark registration for a CBD-based product or franchise than a marijuana-based one. In May 2019, the USPTO issued an examination guide intended to clarify the status of marks for CBD-based goods. As discussed above, the USPTO will not license goods that cannot be used lawfully in commerce. In its examination guide, the USPTO identified the CSA, the FDCA, and the 2018 Farm Bill laws it would analyze to determine if a CBD-related mark will be eligible for registration. In light of the Farm Bill removing hemp from the CSA, the USPTO stated that “for all applications filed on or after December 20, 2018” the Farm Bill may remove the CSA as a ground for refusal for registration but only if the goods are derived from “hemp.” However, the USPTO noted that application for CBD goods would still be subject to the “lawful use” requirement under the FDCA. Accordingly, the current position of the USPTO is that “registration of marks for foods, beverages and dietary supplements, or pet treats containing CBD will still be refused as unlawful under the FDCA” regardless of the source from which the CBD is derived.

V. CONCERNS FOR ATTORNEYS WORKING WITH CANNABIS CLIENTS

Attorneys advising marijuana clients on the legal implications of franchising should also be aware that working with marijuana clients poses unique legal and ethical challenges for their law practice. Strictly speaking, marijuana cultivation, possession, and consumption is illegal under federal law. Ethics rules prohibit attorneys from assisting their clients in committing crimes, so under a strict reading of the rules and the law, attorneys should not advise marijuana clients. In reality, criminal prosecution of marijuana attorneys is rare and state bar associations are split as to whether or not advising a marijuana client violates the rules of professional responsibility. Attorneys advising marijuana clients operate on the frontiers of a developing industry. An attorney advising a client wanting to franchise a marijuana business (that by its nature is likely to cross state lines and invoke federal law) must carefully consider the legal, ethical, and practical aspects of their representation.

A. Criminal Concerns


261 Supra note 259.

262 Id.

263 Id.

264 Id.

265 The authors could only locate two instances in which an attorney advising marijuana businesses was arrested and prosecuted. In both cases, the charges were ultimately dismissed. See Jeff McDonald, In Criminal Case Against Medical-Pot Lawyer, Judge Voids Attorney-Client Privilege, SAN DIEGO UNION-TRIB. (June 16, 2017), https://www.sandiegouniontribune.com/news/courts/sd-me-medwest-charges-20170615-story.html; Eric Gorski, Feds: Four Men Diverted Columbian Cash to Colorado Marijuana Business, DENVER POST (Apr. 28, 2014), https://www.denverpost.com/2014/04/28/feds-four-men-diverted-columbian-cash-to-colorado-marijuana-business/.

266 Anna El-Zein, Caught in a Haze: Ethical Issues for Attorneys Advising on Marijuana, 82 Mo. L. Rev. 1171 (2017).
An attorney advising a marijuana client exposes themselves to two kinds of liability: (1) accomplice liability under the CSA; and (2) liability under the Money Laundering Act. Under the Money Laundering Act, the government does not need to prove an individual acted with the intent to promote criminal activity, only that the transaction involved proceeds of “some unlawful activity” and that the recipient had knowledge or was willfully blind to that fact. In at least two cases, attorneys working with marijuana clients in states that have legalized marijuana have been arrested and charged with criminal offenses for their legal work. In both cases, the charges were ultimately dropped but the attorneys were subject to sweeping searches of their homes and offices and, in one case, civil forfeiture.

In 2013, Colorado marijuana attorney David Furtado was charged with money laundering and attempting to deposit proceeds from an illegal transaction into a bank. Mr. Furtado was involved in the operation of a medical marijuana dispensary. As a result of the investigation, the state of Colorado revoked the license of the dispensary in 2014. Although prosecutors ultimately dismissed the five felony charges against him, federal authorities confiscated $450,000 dollars (USD) found in Mr. Furtado’s trunk and seized a warehouse owned by the dispensary. Similarly, in California, marijuana attorney Jessica McElfresh was arrested and charged with multiple felonies. Prosecutors alleged that McElfresh was aware that her clients, who owned a medical marijuana dispensary, were producing hash oil and helped them hide illegal acts from investigators. Although the San Diego Prosecutor’s Office dropped the charges, investigators conducted searches at her office and home and seized ten million megabytes of data related to her work for the dispensary and other marijuana clients.

The authors of this paper were unable to locate any incidences of marijuana attorneys who were convicted on criminal charges for their work on behalf of legal marijuana businesses. However, even an unsuccessful prosecution could have significant financial and ethical implications such as civil asset forfeiture and the loss of confidential client information.

270 Supra note 265.
271 Id.
273 Id.
274 Id.
275 McDonald, supra note 265.
276 Id.
277 Id.
B. **Ethical Concerns**

The model rules of professional conduct prohibit attorneys from advising or assisting clients in illegal conduct. An attorney advising a marijuana franchise would likely be asked to advise clients on questions regarding production and distribution of a controlled substance as well as banking and other financial arrangements for a marijuana business, all of which are illegal under multiple federal statutes. Can an attorney advise marijuana clients without risking their bar license? It depends on the state bar association.

1. **Marijuana Friendly States**

Several states offer a safe harbor to attorneys who advise marijuana clients so long as the attorney (1) reasonably believes the client’s conduct to be legal under state law and (2) warns the clients of the potential legal implications under federal law. States as socially and politically diverse as Alaska, California, Colorado, Connecticut, Florida, Hawaii, Illinois, Nevada, Maine, Minnesota, Massachusetts, Michigan, New Jersey, New York, Oregon, Ohio, Pennsylvania, Rhode Island, and Washington have either adopted or are likely to adopt this safe harbor approach, although both the Connecticut and the Nevada Bar Association currently discourage attorneys from working with clients in the cannabis industry. These state bar associations who have approved “safe harbor” rules rely on the Cole II Memo, which identifies conduct that is in “clear and unambiguous compliance with state law” as a low priority for federal enforcement. Despite the fact that Attorney General Sessions withdrew the Cole II Memo in January of 2018, no state bar association has withdrawn its safe harbor opinion.

In addition to providing safe harbor ethical opinions, state bar associations in Michigan, Pennsylvania, New York, Oregon, and Washington have marijuana law committees, and several states offer continuing legal education on issues related to providing legal services to marijuana businesses.

2. **Marijuana Hostile States**

Other state bar associations have taken a strict compliance approach and have issued opinions prohibiting attorneys from advising clients on conduct that violates federal law. This approach focuses on the status of marijuana under federal law, not the federal enforcement guidance encompassed in the Cole II Memo. For example, The Connecticut Bar Association allows attorneys to advise clients on the “requirements” of the medical marijuana statute but emphasizes that lawyers may not “assist clients” in violating federal criminal law and that “lawyers should carefully assess where the line is and not cross it.” Other bar associations have been

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280 El-Zein, supra note 266.


more explicit. The New Hampshire Bar Association states that “lawyers cannot provide legal services that would assist a client in the operation of a medical marijuana facility.” 283 The Nevada Bar Association advises attorneys that, while marijuana is legal under state law, advising marijuana businesses “may trigger discipline proceedings.” 284

3. Best Practices

Any attorney considering advising a client on a marijuana franchise should locate and carefully review the ethics opinion of their state bar association. Attorneys, particularly attorneys working in states such as Louisiana where marijuana is legal in some form but the bar association has not yet issued ethical guidance, should be particularly careful and should inform marijuana clients that their representation may be terminated if the bar association issues an ethics opinion that prohibits certain legal services.

C. Practical Concerns

Ironically, while the implications of advising a marijuana client remain murky, the demand for legal services is skyrocketing. As more states move toward some form of legalization, more business and individuals are seeking legal guidance. The following section offers practical guidance for a lawyer working with marijuana clients.

1. Protect your Client

An attorney advising a marijuana client must go beyond merely informing their client that marijuana is illegal under federal law. They must also carefully explain the implications of its continuing illegality and stress the need for near-perfect compliance with all other state and federal laws. At a minimum, an attorney advising a client seeking to sell or purchase a marijuana franchise should inform their client of: (1) the risk of criminal liability for themselves for other parties’ actions, including financial transactions; (2) the limited legal protections available to marijuana businesses; and (3) limitations on legal representation.

Courts and law enforcement may be more likely to impose liability on a marijuana franchisor for the bad acts of a franchisee than they might on a conventional franchisor. The CSA imposes broad liability for any individual “aiding or abetting” a marijuana business, even if the “aiding” business is perfectly legal. 285 A tangential connection to a marijuana business such as renting a building, advertising, or providing accounting services can be enough to expose a client to liability. Similarly, state legalization does not negate liability under the Money Laundering Act for transactions related to the proceeds of criminal activity and attempts to avoid reporting requirements such as keeping deposits below $10,000 (USD) can trigger independent criminal liability. Under Section 280E of the Internal Revenue Code, marijuana businesses are prohibited


from making certain business deductions. Generally, franchisors are not held liable for the acts for franchisees but, given the CSA and the broad language of the Cole II Memo, a franchisor could face criminal liability or civil seizure of assets based on a franchisee’s misconduct. An attorney advising a marijuana client should emphasize this risk and (1) encourage the franchisor to conduct through background checks of prospective franchisees; (2) design and implement a comprehensive policy regarding all financial transactions, especially those between the franchisee and franchisor; and (3) zealously monitor and aggressively enforce system compliance including all legal obligations.

A marijuana franchise system will not have the same legal protections as a conventional franchise. For example, it likely will not be able to obtain federal trademark protection for most aspects of its intellectual property. An attorney working with a marijuana business must advise their clients that a trademark associated (and the USPTO defines associated broadly) with marijuana will be unable to obtain federal registration. A hemp-based business may be able to obtain federal registration but the USPTO has stated that it will consider hemp’s “lawfulness” under the 2018 Farm Bill but will also consider “lawful use issues under the Federal Food Drug and Cosmetic Act.” Additionally, bankruptcy courts have held that a marijuana business may not seek bankruptcy protections or have required marijuana businesses to cease marijuana operations to maintain their bankruptcy petition.

An attorney advising a marijuana client should educate their client on the limits on the legal representation they can provide. An attorney working with marijuana clients should consider whether a change in guidance from the Justice Department or a bar association would lead them to limit or stop working with marijuana clients. They should inform any marijuana clients about those circumstances and explain that a change in the law or the ethical guidance from the bar association may lead them to terminate the attorney client relationship. Additionally, communications between an attorney and a marijuana client may not enjoy the same level of protection under attorney-client privilege. In the McElfresh case, investigators seized the business records and communications of the attorney, and the trial court later held that some communications were not protected by privilege under the crime-fraud exception. The seized communications were not only communications between McElfresh and the clients that were charged in the investigation but also McElfresh’s other marijuana clients. An attorney working with a marijuana business should advise their clients that privilege may not apply to their communications and that their attorney could be called as witness if they are prosecuted.

2. Protect Yourself

In addition to advising their clients, an attorney working with marijuana businesses must be aware that advising clients in violating federal law also poses significant risk to their own legal

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288 See In re McGinnis, 453 B.R. 770 (Bankr. D. Or. 2011) (Chapter 13 plan denied); In re Arenas, 514 B.R. 887 (Bankr. D. Colo. 2014) (grounds to dismiss were that the plan would have required the trustee’s administration of illegal assets); In re Johnson, 532 B.R. 53 (Bankr. W.D. Mich. 2015) (debtor enjoined from operating his medical marijuana business during pendency of the matter).

practice. Careful client selection and detailed record-keeping may mitigate those risk. Attorneys should also ask whether a malpractice claim from a marijuana client would be covered by malpractice insurance.

Both the Cole II Memo and other exemptions for lawful marijuana businesses require strict compliance with state and certain federal laws. While most attorneys are accustomed to advising clients on how to stay out of jail, attorneys advising a marijuana business are relying on their clients’ ability to strictly comply with legal and accounting requirements to keep themselves and their attorneys out of jail. A wise practitioner will be cautious to select marijuana clients who will not expose them to unnecessary risk by either being careless regarding such laws and guidelines or actively working to subvert them.

Attorneys working with marijuana businesses should draft detailed engagement letters that (1) explicitly state that marijuana is illegal under federal law and provide detailed information about relevant statutes; (2) outline the specific aspects of marijuana businesses that are legal under the state laws of the state in which the client will be operating; (3) specifies the aspects of the marijuana business for which they will and will not provide guidance, (4) informs the clients that their communications may not be privileged; and (5) lists the circumstances under which the attorney will terminate the representation, including the client’s conduct and a change in the legal or ethical landscape. Even safe harbor states require attorneys to advise marijuana clients that marijuana is illegal under federal law, and a detailed engagement letter ensures that it will be in writing.

When advising a marijuana client, careful documentation and record keeping is essential. While criminal investigations and prosecutions of marijuana businesses and their service providers are rare, they do occur, and careful documentation regarding what services an attorney provided and how they were paid for may limit an attorney’s exposure. An attorney working with marijuana and non-marijuana clients may want to consider segregating the business and financial record keeping for each type of client.

Finally, an attorney advising a marijuana client should carefully review their malpractice insurance policy. There are a handful of companies that will provide professional liability insurance for lawyers advising marijuana clients, but most insurance providers are reluctant to provide coverage.290 In the general insurance context, some courts have rejected the denial of coverage for “illegal or contraband” acts or property, such as a federal trial court in Colorado that refused to enforce a “contraband” exclusion against a medical marijuana dispensary because the term “contraband” was ambiguous when the “contraband,” marijuana, was legal under state law.291 But other courts have taken the opposite approach. A Michigan federal court enforced an “illegal acts” exclusion in a case where the commercial landlord had its insurance claim denied because its tenants had used the property for a grow operation without the landlord’s knowledge, based solely the fact that such conduct was illegal under federal law.292 An attorney advising marijuana clients should carefully consider whether or not to inform their malpractice provider that they are advising such clients. If they choose not to seek affirmative guidance from their carrier, they may discover that they are not covered through a denial letter.


VI. CONCLUSION

The rapidly growing cannabis market and increasing number of states moving toward some form of marijuana legalization offer incredible potential to prospective franchisors, investors and franchisees. But because of the conflicting state and federal laws related to key aspects of cannabis businesses, an attorney advising a cannabis franchise must take a comprehensive and creative approach to advising their client. A marijuana franchise would need to adapt the traditional franchise model by offering more flexibility in terms of the products the system sells or how the products look, but it may require more franchisor involvement and monitoring of business transactions. Because of conflicting state regulations, a marijuana franchise is much less likely to rely on a standardized set of goods, trade materials, or marketing practices. Conversely, because law enforcement views any involvement in a bad actor marijuana business as the basis for criminal liability or civil forfeiture, an attorney advising a marijuana franchisor should stress the need for careful monitoring and greater involvement in how the franchised business is operated, especially as it relates to financial transactions. This additional franchisor involvement may give rise to an additional risk of vicarious or joint liability in some cases. A CBD franchise could more closely follow the traditional franchise model but would need to include workarounds for conflicting state laws, food and drug administration rules and transportation challenges.
Biographies

Mike Drumm is an attorney with Drumm Law and its founder. Before founding Drumm Law, Mike wore a suit and tie every day and worked at a large national law firm (he is grateful that he no longer has to wear the “lawyer costume” every day). He is most proud of being a father of three and of hearing “you don’t remind me of a lawyer” when he meets people. Mike is continually recognized as a Franchise Times magazine Legal Eagle and 1851 Franchise Legal Player and is a designated Certified Franchise Executive by the International Franchise Association. He has also received commendation from Super Lawyers. Mike has given presentations on intellectual property, distribution, and franchise law across the country. Mike attended law school at the University of Texas and a semester at University College London (he visited 15 countries while “studying”). Mike obtained a BSBA in Business Management from the University of Missouri-Columbia. He is admitted to the state bars of Texas and Colorado.

Caroline Fichter is a partner with the Bundy law firm in Washington State. She focuses her practice on representing franchisees, franchisors and other small business owners. Caroline helps clients in all stages of the franchise relationship, including reviewing the franchise agreement, negotiating changes to the franchise agreement, helping franchisees sell or close their franchise, and fighting for wronged franchisees in litigation. Her published works include “Don’t Tread on Me: A Defense of State Franchise Regulation” (Franchise Law Journal, Summer 2018) and “Surviving the Tempest: Franchisees in the Brave New World of Joint Employers and $15 Now” (Franchise Law Journal (Spring 2016), as well as multiple articles in the Franchise Lawyer. She received the 2016 Chair’s Award for Substantial Written Work or Presentation. She is the chair of the American Bar Association Forum on Franchising Litigation and Alternative Dispute Resolution Committee. Caroline is licensed in Oregon and Washington. She graduated Cum Laude from Seattle University School of Law and from Washington State University with a Bachelor of Arts in Political Science.