

[Securities Regulation Daily Wrap Up, FRAUD AND MANIPULATION—S.D.N.Y.: No showing that trades in Canadian company took place in U.S., \(Aug. 31, 2021\)](#)

Securities Regulation Daily Wrap Up

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By [Rodney F. Tonkovic, J.D.](#)

OTC transactions do not occur on exchanges, and none of the three trades at issue were shown to have occurred in the United States.

A district court dismissed a fraud action against a Canadian cannabis company for lack of any domestic transactions. In this case, the Canadian-based cannabis company operated facilities in the U.S. and its shares were traded over-the-counter in the U.S. via an alternative trading system. The court concluded that there were no transactions on a domestic exchange, since OTC transaction by definition do not occur on an exchange. The complaint also failed to allege that irrevocable liability was incurred in the U.S. for any of the three transactions at issue (*In re iAnthus Capital Holdings, Inc. Securities Litigation*, August 30, 2021, Kaplan, L.).

The action was brought against iAnthus Capital Holdings, Inc., a Canadian corporation operating cannabis cultivation and dispensary facilities in the U.S. The company is based in Canada, organized under Canadian law. Its shares are listed on the Canadian Stock Exchange and also trade over-the-counter in the U.S. on the OTCQX operated by the OTC Markets Group.

Loan default and restructuring. On April 6, 2020, iAnthus announced that it had defaulted on a debt due to its senior secured lender, but this was followed by iAnthus's CEO accepting of a loan from the lender's managing member. In October 2020, a transaction to restructure iAnthus was approved.

Litigation followed, including this consolidated action led by an individual shareholder plus iAnthus's largest shareholder, HI-MED LLC ("Hi-Med"). The complaint alleges that iAnthus and the lender violated the antifraud provisions of the Exchange Act by failing to disclose iAnthus's relationship with the lender and the terms governing its financing by the lender. This undisclosed information allegedly caused the company to default and then put the lender in a position to take over iAnthus. The defendants moved to dismiss on the grounds that the extraterritorial application of the Exchange Act would be improper.

Domestic exchange. The first matter addressed by the court was whether OTCQX qualified as a domestic exchange. At issue was whether the transactions were truly over-the-counter, since such transactions do not occur on an exchange within the meaning of *Morrison*, the court explained. The plaintiffs argued that the securities traded through the SEC-registered OTC Link, but this is an alternative trading system under a separate regulatory regime and as such is specifically exempt from the Exchange Act's definition of "exchange." The transactions in iAnthus's stock accordingly did not qualify as "transactions listed on domestic exchanges" under *Morrison*.

No domestic transactions. Next, there were three transactions at issue in this case: the individual plaintiff's purchase of iAnthus common stock; Hi-Med's receipt of common stock through a transaction between iAnthus and another party; and Hi-Med's purchase of a convertible debenture from iAnthus. First, the plaintiff's purchases were not domestic because he did not show where or how the transactions were made. Even if a purchase through trades in the U.S. over-the-counter market could be inferred, the mere assertion that a transaction took place in the U.S. is insufficient to plead a domestic transaction, since there was no indication of where irrevocable liability was incurred or where title passed. Next, Hi-Med's stock acquisition was not a domestic transaction because it occurred through the merger of foreign entities, which is generally not a domestic transaction—and there was no allegation that irrevocable liability was incurred in the U.S. Finally, regarding Hi-

Med's debenture, the court found that the complaint lacked any facts indicating where the purchase occurred. The court accordingly granted iAnthus's motion to dismiss.

The case is [No. 20-cv-03898](#).

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Companies: Hi-Med LLC; iAnthus Capital Holdings, Inc.; Gotham Green Partners LLC

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