

# Cannabis Securities Law Update: Shareholder Suit Based on Vague Descriptions Of Product Quality Dismissed as Mere Puffery

MAY 29, 2020

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New York court dismisses securities fraud claim alleging that cannabis producer misrepresented that its product is “high-quality” despite shipment containing mold and rubber gloves.

On May 15, 2020, Justice Barry R. Ostrander, presiding in the Commercial Division of the New York Supreme Court, issued an opinion that impacts the developing body of cannabis law, as well as securities fraud law. In the *Matter of Sundial Growers Inc. Securities Litigation*, a putative class of U.S. investors in the Canadian company Sundial Growers, Inc. (“Sundial”) brought a securities fraud complaint against Sundial, its officers and directors, and its underwriters, based on their alleged misrepresentations in the company’s prospectus and registration statement that Sundial was a producer of “high-quality” and “premium” cannabis.

In the company’s securities filings, Sundial represented that it believed its high-quality and premium cannabis would “deliver superior consumer experiences, resulting in strong consumer loyalty and advocacy.” According to the plaintiffs, just weeks later, the media reported that one of Sundial’s customers returned a half ton of cannabis because it contained mold, rubber gloves, and other non-cannabis material. On that basis, the plaintiffs alleged that Sundial’s assertions concerning the “high-quality” of its product was false and Sundial actually produced “low-quality” cannabis.

Justice Ostrander, however, ruled that the plaintiffs had failed to allege an actionable misrepresentation and he granted Sundial’s motion to dismiss their complaint: “Expressions of puffery and corporate optimism are not actionable under the securities laws,” and Sundial’s statements that its product was “premium” and “high-quality” clearly fell into that category because they were opinions that are “not subject to verification.” The court also noted that Sundial expressly disclosed in its securities filings that its business faced substantial risks, including risks concerning failures in its quality control systems.

The court’s decision in *Sundial* has implications beyond securities fraud cases and it demonstrates the precautions that cannabis producers should employ whenever they promote the quality of their product. Indeed, whether cannabis producers are promoting their product to investors or customers, they will be in a stronger position to defend themselves against claims of fraud, or avoid litigation in the first place, if their representations and warranties appear to be “corporate optimism” and general opinion instead of verifiable facts. For example, a company’s claim that its product is “the best” is reasonably understood to be puffery, whereas a claim by a company that its product is “higher quality than all competitors” could conceivably be verified and therefore actionable if untrue.

Benesch has robust cannabis and securities fraud practices, and is uniquely situated to advise your business as it grows and represent its interests when disputes emerge. Benesch's seasoned cannabis attorneys represent companies all over the country, and the firm covers every aspect of the industry's legal needs.

Benesch's attorneys have also helped clients prevail in some of the largest securities fraud actions in the US. For example, Benesch attorneys obtained a complete victory for a defendant in a securities fraud lawsuit alleging over \$20 billion in damages. They also obtained summary judgment in a securities fraud lawsuit seeking over \$2 billion in damages, and persuaded the Eleventh Circuit Court of Appeals to affirm the district court's order.

**For more information, contact a member of Benesch's Cannabis Industry Group.**

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