State Attorneys General Powers and Responsibilities

Edited by
Emily Myers
National Association of Attorneys General

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This book is dedicated to Attorneys General and the men and women who work for them in the 56 jurisdictions. They continue to make an important contribution to state govenment and the American legal system. Without them, there would be no book to write.

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This book is a collaborative effort, in which different authors with expertise in each substantive area contribute their time and talent. The principal authors are noted on each chapter, but we would like to thank them again here for their hard work and dedication. Many thanks to the following authors:

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Chapter 22

Tobacco

By Michael Hering, Director and Chief Counsel, Center for Tobacco and Public Health, NAAG

Perhaps the most complex and far-reaching action taken by state attorneys general is their ongoing collective effort to reduce youth smoking. The tobacco litigation begun by a handful of attorneys general in 1994 resulted in a national settlement (the Master Settlement Agreement or MSA), which has recovered more than $126 billion for the states thus far and imposed a number of limits on tobacco company advertising, marketing and promotion. The Supreme Court characterized the MSA as "a landmark agreement,"[1] and the MSA has had far-reaching public health and economic effects. Since the MSA was executed, tobacco usage in the United States has declined substantially, and underage tobacco usage has declined by an even greater percentage, reversing sharp increases that occurred in the 1990s.[2] Enforcement of the provisions of the tobacco settlement continues to be a priority for attorneys general nationwide.

State Claims for Medicaid Reimbursement

In May 1994, the attorney general of Mississippi filed suit in state court seeking reimbursement from tobacco companies for money spent treating

1 *Lorillard Tobacco Co. v. Reilly,* 533 US 525, 533 (2001).

2 Since youth smoking levels peaked in 1996-97, the proportions of students smoking in the month prior to the annual Monitoring the Future survey has fallen by large proportions: 91%, 84%, and 74% in grades 8, 10, and 12, respectively. University of Michigan News Service: Ann Arbor, MI. http://www.monitoringthefuture.org.

illnesses caused by smoking.[3] The lawsuit alleged that the tobacco industry was a cartel that had engaged in negligent and deliberate behavior which was designed to cause and had caused injury and death to persons in Mississippi. The complaint also alleged that the tobacco industry could have developed a safer cigarette but did not; knew that the nicotine in cigarettes was an addictive drug; engaged in a vast advertising campaign designed to increase the number of people addicted to tobacco; unjustly enriched itself from Medicaid funds at the expense of sick and dying tobacco users; targeted groups deemed vulnerable to the tobacco advertising campaign including African-Americans, minors, and low income women; sold a dangerous and defective product; and conspired to fraudulently conceal the dangerous nature of tobacco.

In August of 1994, Minnesota, joined by the state's largest private insurer, filed suit seeking Medicaid reimbursement, but also alleging an antitrust conspiracy and consumer fraud by tobacco companies.[4] Minnesota alleged violations of the antitrust laws through a conspiracy to suppress research and keep safer cigarettes off the market. The complaint also alleged that the tobacco companies promoted the sale and distribution of products known to be harmful and concealed the harmful effects and the addictive qualities of tobacco.

As other states filed suit against the tobacco companies, the theories of recovery included federal Racketeer Influenced Corrupt Organizations (RICO) claims,[5] unfair competition, a variety of fraud allegations, and in two states, Florida and Massachusetts, statutory claims based on the enactment of specific health care cost recovery legislation.[6] The number of states bringing suit also expanded dramatically. By the summer 1997, forty states had sued the tobacco companies.

In June 1997, the states and the major tobacco companies reached a "global settlement" that took the form of a detailed legislative proposal that was presented to Congress as an effort to end the litigation. Under the plan, the tobacco companies would have made settlement payments having an estimated then-present value in 1997 of $368 billion over 25 years. The state health care reimbursement suits would have been settled, and the industry would have been granted immunity from all other forms of class action. Under another provision in the settlement plan, there would have been no punitive damages allowed

3 *Moore v. The American Tobacco Co.,* No. 94-1429 (Chancery Ct. Jackson County, Miss. 1994).

4 *Minnesota v. Philip Morris Inc.,* C1-94-8565 (2d Jud. Dist.).

5 *Texas v. The American Tobacco Co*., No. 5-96CV-91, Complaint (E.D.Tex. Mar. 28 1996).

6 Fla. Stat. § 409.910 *et seq.*; Mass Gen. L. c. 118E (as amended by Stat. 1994, c. 60, § 276 and Stat. 1995, c. 38, § 131).

in individual cases for industry conduct prior to the enactment by Congress of the legislation. A third provision would have capped the total annual liability for awards on future individual claims at $5 billion. When the proposed settlement was presented to Congress, an even more far-reaching legislative proposal emerged, under which the tobacco industry would have made payments valued at $516 billion over twenty-five years. The bill incorporated virtually all of the earlier-negotiated public health provisions but would have eliminated the litigation immunity provisions. This legislation failed to pass, but many of its provisions were incorporated into the eventual settlement of the cases.

The Master Settlement Agreement

After several months of negotiation, forty-six states, the District of Columbia, the Commonwealth of Puerto Rico, American Samoa, Guam, Northern Mariana Islands, and the Virgin Islands (the Settling States) agreed, effective November 23, 1998, to a tobacco settlement proposal that became the MSA. Four states--Florida, Minnesota, Mississippi, and Texas—had settled their cases separately. The tobacco manufacturers that originally settled with the Settling States under the MSA were the four major companies that had been sued: Philip Morris USA Inc., R.J. Reynolds Tobacco Co., Brown & Williamson Tobacco Corp. and Lorillard Tobacco Co.[7] These companies are known as the "Original Participating Manufacturers." (OPMs)[8] Subsequently, more than 40 smaller tobacco product manufacturers have also signed the MSA, and they are known as "Subsequent Participating Manufacturers." (SPMs) Collectively, both groups are referred to as "Participating Manufacturers."[9]

Under the MSA, the Settling States release the Participating Manufacturers from past and future claims for costs incurred due to smoking-related illnesses and death and for other equitable relief.[10] In exchange, the manufacturers agree

7 Liggett Group settled with some states in 1997 and joined in the agreement with the others the next year.

8 Subsequent to signing the MSA, Brown & Williamson Tobacco Corp. and Lorillard Tobacco Co. both merged with R.J. Reynolds Tobacco Co. As a result, there are two remaining OPMs.

9 The states also entered into a similar settlement covering smokeless tobacco with United States Smokeless Tobacco Company. This settlement is referred to as the STMSA.

10 *See* MSA §§ II(nn), (oo), (pp); MSA §XII.

to pay billions of dollars annually and in perpetuity to the Settling States and to substantially restrict their marketing and promotion of cigarettes.[11]

The Participating Manufacturers' aggregate or total annual settlement payment is distributed among the states pursuant to fixed percentages that were established according to a complicated calculation that generally reflects the population of Medicaid recipients in each state.[12] The MSA places no restrictions on how the states may spend the funds.

In addition to the payments made to the states, the MSA required the Participating Manufacturers each year for ten years to pay $25 million to fund a charitable foundation, the Truth Initiative[13] (Truth), which supports the study of programs to reduce teen smoking and substance abuse and the prevention of diseases associated with tobacco use.[14] Among other activities, Truth carries out a nationwide, sustained advertising and education program to counter youth tobacco use and educate consumers about the cause and prevention of diseases associated with tobacco use. The MSA also required the industry to pay to Truth $1.45 billion to carry out this advertising campaign and educational program.[15]

With regard to tobacco advertising, the MSA bans use of cartoons in the advertising,[16] promotion, packaging or labeling of tobacco products; prohibits targeting youth in advertising, promotions, or marketing;[17] bans industry actions aimed at initiating, maintaining or increasing youth smoking;[18] and requires companies to develop and regularly communicate corporate principles that commit to complying with the MSA and reducing youth smoking.[19]

The MSA also bans outdoor advertising, including billboards, signs and placards in arenas, stadiums, shopping malls, and video game arcades, limits advertising outside retail establishments to 14 square feet, and bans transit advertising of tobacco products.[20] In addition, the MSA bans payments to promote tobacco products in movies, television shows, theater productions or live performances, live or recorded music performances, videos and video games;[21] prohibits

11 *See* MSA §§ III and IX.
12 *See generally* MSA Exhibit A (showing per-state allocation of settlement money.)
13 Formerly known as the American Legacy Foundation.
14 MSA §VI(b).
15 MSA §VI(c).
16 MSA §III(b).
17 MSA §III(a).
18 *Id.*
19 MSA §III(1)
20 MSA §III(d).
21 MSA §III(e).

brand name sponsorship of events with a significant youth audience or team sports (football, basketball, baseball, hockey or soccer);[22] prohibits sponsorship of events where the paid participants or contestants are underage and limits tobacco companies to one brand name sponsorship per year.[23]

In order to foster public awareness of the dangers of smoking and the conduct of the tobacco companies, the MSA required tobacco companies to open and maintain through June 30, 2010, at their expense, a user-friendly and searchable website that included all documents produced in state and other smoking and health related lawsuits, and required the industry to add, at its expense, all documents produced in future civil actions involving smoking and health cases.[24] The documents that had been on these websites have been permanently placed on the website of the University of California at San Francisco.[25]

Under the MSA, the Council for Tobacco Research, the Tobacco Institute, and the Council for Indoor Air Research were disbanded, and all records of those organizations that relate to any lawsuit were preserved. The MSA also gave the states the ability to regulate and oversee any new trade organizations created by the tobacco industry.[26]

The MSA also prohibits tobacco companies from opposing proposed state or local laws or administrative rules that are intended to limit youth access to and consumption of tobacco products. It also prohibits lobbyists from supporting or opposing state, federal or local laws or actions without authorization of the companies.[27]

Because of a concern that tobacco manufacturers that declined to enter into the MSA (known as Non-Participating Manufacturers or NPMs) and thus would not be bound by the marketing and advertising restrictions mentioned above and would not be obligated to make settlement payments, could use such advantages over Participating Manufacturers to derive large short-term profits in the years before liability may arise without ensuring an adequate source of recovery, the MSA provides an incentive for states to require such NPMs to establish a reserve fund to guarantee a source of recovery. This incentive takes the form of a potential reduction in the Participating Manufacturers' aggregate annual settlement payment if they lose market share during a given year. Such reduction can

22 MSA §III(c).
23 *Id.*
24 MSA §IV.
25 *See* https://www.industrydocumentslibrary.ucsf.edu/tobacco/.
26 MSA §§III(o), III(p).
27 MSA §III(m).

occur if (a) there has occurred during the year a Market Share Loss as defined in the MSA, (b) an economic consulting firm chosen by the Original Participating Manufacturers and the states determines that the disadvantages imposed on Participating Manufacturers by the MSA were a significant factor contributing to the Market Share Loss, and (c) some states failed to "diligently enforce" a so-called Model Statute[28] requiring NPMs to make escrow deposits for their cigarette units sold in MSA States. The Model Statute and the potential reduction, known as the "Non-Participating Manufacturer Adjustment," are discussed more fully below.

Legislation

Exhibit T of the MSA contains the language of the Model Statute. The Model Statute requires an NPM either to sign the MSA and become a Participating Manufacturer or to deposit into an escrow account amounts for the NPM's sales in any MSA state as measured by excise taxes collected by the state by means of a tax stamp.[29] This money is returned to the NPM at the end of a 25-year period, provided that no judgment was entered against the NPM, or settlement agreed to between the NPM and a state, in a health-care-costs suit similar to that brought against the major tobacco companies in the 1990's. While the money is in escrow, the NPM collects any interest earned on it. For an NPM that fails to make the requisite escrow deposit for cigarettes sold in a state, the Model Statute authorizes an action to recover the full deposit plus penalties, and for an injunction prohibiting the NPM from selling cigarettes in the state after two knowing violations of the Model Statute.

One area of concern to the states was deficiencies in the Model Statute that hobbled state efforts to require NPMs to make the requisite deposits into the escrow accounts. For example, the Model Statute enables NPMs to sell cigarettes for up to 16 months in a State before the state can bring an action to enforce the Statute. In addition, even where states bring actions and obtain judgments against NPMs, many NPMs are located in foreign countries and it has proven difficult and expensive to obtain service of process or to effect the judgments. To remedy these deficiencies, states enacted "Complementary Legislation," the purpose of which is to make state enforcement of the Model Statutes more effective.

28 MSA § IX(d)(2). The Model Statute is also called the Qualifying Statute or Escrow Statute.
29 MSA, Exhibit T.

Complementary Legislation authorizes a state to maintain a directory of cigarette manufacturers compliant with state law and of their products that are permitted to be stamped and sold in a particular state. The legislation prohibits the placement of cigarette tax stamps on products that are not listed on the directory. All Tobacco Product Manufacturers are required to make specific certifications before a brand can be listed in the directory, but a NPM must also certify that: a) it is registered to do business in the state or has appointed an agent for service of process; b) it maintains a Qualified Escrow Fund with an executed qualified escrow agreement that has been reviewed and approved by the state; c) it is in full compliance with the Model Statute; and d) it identifies the financial institution where it has established such Qualified Escrow Fund and all deposits and withdrawals to/from that fund.

In addition, neither an NPM nor its brands will be listed in the directory unless all escrow deposits for any period have been fully made and all outstanding final judgments for violations of the Model Statutes fully satisfied. The Complementary Legislation also allows the attorney general or other official of a state to request information to verify the accuracy of reported information and permits disclosure of information to other state agencies to facilitate investigation. Criminal and civil penalties, including injunctive relief and designation of product as contraband subject to seizure, forfeiture and destruction are among the penalties that may be imposed.

Under the Model Statute, NPMs are required to make annual escrow deposits. Some states' Complementary Legislation, however, requires NPMs to make quarterly deposits. The Model Statute as originally enacted also contained an unforeseen loophole allowing the early release of escrow funds. An escrow amount required to be deposited in a year could be released earlier than the twenty-five year escrow period to the extent that a tobacco product manufacturer established that the amount was greater than the state's allocable share of the total MSA settlement payment that such manufacturer hypothetically would have been required to make had it been an MSA Participating Manufacturer.[30] This so-called "allocable share release" provision often had the unintended effect of an NPM obtaining releases of the vast majority of its escrow deposits when, for example, the NPM concentrated its sales in a single state or a few states.[31]

30 MSA, Exhibit T.

31 For example, an NPM that sold virtually all of its cigarettes in Missouri could still receive back just under 98 percent of its escrow deposit in Missouri because Missouri's allocable share of the MSA settlement payments is slightly over two percent.

To close this loophole, all but one state have now enacted an amendment to the allocable share release provision. Under the amendment, an NPM can obtain a release of some of its escrow deposit in a state only to the extent that such deposit exceeds what the NPM hypothetically would have paid under the MSA for those same sales in the state.

Challenges to the MSA and Legislation

The MSA and the Model Statutes enacted by the states pursuant to the MSA, as well as the Complementary Legislation and allocable share release amendment, were challenged almost immediately by various parties, including Non-Participating Manufacturers; Subsequent Participating Manufacturers; tobacco importers, wholesalers, distributors and retailers; Native American interests; and individuals. In all decided cases, the suits have been dismissed with prejudice on motions to dismiss or summary judgment has been entered for the state so that the legality of the MSA and the associated statutes has been upheld. There have been no decisions on the merits against the MSA or the statutes.[32]

Challenges to the MSA and related legislation have been in two general categories: (1) those based on various antitrust theories,[33] including violation of the

32 The most recent decisions upholding the legality of the MSA are *Grand River Enters. Six Nations Ltd. v. King*, 2012 U.S. Dist. LEXIS 10802 (S.D.N.Y. Jan. 30, 2012) and *VIBO Corp. v. Conway*, 669 F.3d 675 (6th Cir. Ky. 2012).

33 *Hise v. Philip Morris Inc.*, 46 F. Supp. 2d 1201 (N.D. Okla. 1999), *aff'd mem.*, 208 F.3d 226 (10th Cir.), *cert. den.*, 531 U.S. 959 (2000); *PTI, Inc. v. Philip Morris Inc.*, 100 F. Supp. 2d 1179 (C.D. Cal. 2000); *North American Trading Co. v. National Ass'n of Attys Gen'l*, Civ. Action No. 01-01600 (D.D.C. Sept. 18, 2001), *aff'd*, 2002 U.S. App. LEXIS 24198 (D.C. Cir. Nov. 25, 2002); *A.D. Bedell Wholesale Co., Inc. v. Philip Morris, Inc.*, 263 F.3d 239 (3d Cir. 2001), *cert. den.*, 534 U.S. 1081 (2002); *Forces Action Project, LLC v. State of California*, No. C99-0607MJJ (N.D. Cal. Jan. 15, 2002), *aff'd*, 57 Fed. Appx. 322 (9th Cir. Apr. 17, 2003); (*Mariana v. Fisher*, 226 F. Supp. 2d 575 (M.D. Pa. 2002), *aff'd*, 338 F.3d 189 (3d Cir. 2003), *cert. den. sub nom. Mariana v. Pappert*, 540 U.S. 1179 (2004); *Grand River Enters. Six Nations Ltd. v. Pryor*, 2003 U.S. Dist. LEXIS 16995 (S.D.N.Y. Sep 29, 2003), *vacated*, 2004 U.S. Dist. LEXIS 13373 (S.D.N.Y. Jul. 15, 2004), *rev'd on other grounds*, 425 F.3d 158 (2d Cir. 2005), *cert. den. sub nom. King v. Grand River Enterprises Six Nations Ltd.*, 549 U.S. 951 (2006), *on remand*, 2006 U.S. Dist. LEXIS 44792 (S.D.N.Y.), *aff'd,* 481 F.3d 60 (2d Cir. 2007), *summary judgment granted to defendants*, 783 F. Supp. 2d 516 (S.D.N.Y. 2011), *mot. for recon. den.,* 2012 U.S. Dist. LEXIS 10802 (S.D.N.Y. Jan. 30, 2012); *Freedom Holdings, Inc. v. Spitzer*, 357 F.3d 205, *reh'g den.*, 363 F.3d 149 (2d Cir. 2004), *on remand*, 447 F. Supp. 2d 230 (S.D.N.Y. 2004), *recon. den.*, 2004 U.S. Dist. LEXIS 20078 (S.D.N.Y. Oct. 6, 2004), *aff'd on other grounds*, 408 F.3d 112 (2d Cir. 2005), *on remand*, *Freedom Holdings, Inc. v. Cuomo*, 592 F. Supp. 2d 684) (S.D.N.Y. 2009), *aff'd,* 624

Sherman Act[34] and preemption by the Sherman Act[35]; and (2) those alleging that the MSA and the implementing statutes violated a variety of Constitutional provisions, including the Interstate Compact Clause, the Interstate Commerce Clause, the Foreign Commerce Clause, the Indian Commerce Clause, the Supremacy Clause, the First Amendment, the Equal Protection Clause, the Due Process Clause, the prohibition against bills of attainder, the Import-Export clause and the Tenth Amendment.[36]

F.3d 38 (2d Cir. 2010), *cert. den.*, 131 S. Ct. 1810 (2011); *Trident Int'l Corp. v. Kentucky*, 2005 U.S. Dist. LEXIS 20233 (E.D. Ky. Sept. 8, 2005), *recon. den.,* 395 F. Supp. 2d 521 (E.D. Ky 2005), *aff'd*, 467 F.3d 547 (6th Cir. 2006); *S&M Brands, Inc. v. Summers*, 393 F. Supp. 2d 604 (M.D. Tenn. 2005), *aff'd*, 228 Fed. Appx. 560 (6th Cir. Apr 19, 2007); *Sanders v. Lockyer*, 365 F. Supp. 2d 1093 (N.D. Cal. 2005), *aff'd sub.nom. Sanders v. Brown*, 504 F.3d 903 (9th Cir. 2007), *cert. den.*, 533 U.S. 1031 (2008); *Xcaliber Int'l Ltd. v. Edmondson*, 2005 U.S. Dist. LEXIS 26705 (N.D. Okla. May 20, 2005), *recon. den.*, 2005 U.S. Dist. LEXIS 40448 (Aug. 31, 2005), *aff'd sub nom. KT&G Corp. v. Attorney Gen'l of State of Oklahoma*, 535 F.3d 1114 (10th Cir. 2008); *Xcaliber Int'l Ltd. v. Kline*, No. 05-2261, 2006 U.S. Dist. LEXIS 77420 (D.Kan. Feb. 7, 2006), *aff'd sub nom. KT&G Corp. v. Attorney Gen'l of State of Oklahoma*, 535 F.3d 1114 (10th Cir. 2008); *International Tobacco Partners, Ltd. v. Kline*, 475 F. Supp. 2d 1078 (D.Kan. 2007); *Grand River Enters. Six Nations, Ltd. v. Beebe*, 418 F. Supp. 2d 1082 (W.D. Ark. 2006), *aff'd*, 574 F.3d 929 (8th Cir. 2009), *cert. den. sub nom. Grand River Enter. Six Nations, Ltd. v. McDaniel*, 130 S. Ct. 2095 (2010); *Coker v. Foti*, 2006 WL 3307445, 2006 U.S. Dist. LEXIS 82537(W.D. La. Nov. 9, 2006), *aff'd sub nom. S&M Brands, Inc. v. Caldwell*, 614 F.3d 172 (5th Cir. 2010), *cert. den.*, 131 S. Ct. 1601 (2011); *Xcaliber Int'l Ltd. LLC v. Caldwell*, 2006 U.S. Dist. LEXIS 75862 (Oct. 18, 2006), 2009 U.S. Dist. LEXIS 39081 (May 7, 2009), *aff'd*, 612 F.3d 368 (5th Cir. 2010); *International Tobacco Partners, Ltd. v. Beebe*, 420 F. Supp. 2d 989 (W.D. Ark. 2006); *Dos Santos, S.A. v. Beebe*, 418 F. Supp. 2d 1064 (W.D. Ark. 2006); *VIBO Corp., Inc. v. Conway*, 594 F. Supp. 2d 758 (W.D. Ky 2009), *aff'd* 669 F.3d 675 (6th Cir. Ky. 2012).

34 Several courts have rejected antitrust claims on the basis of state action immunity under *Parker v. Brown,* 317 U.S. 341 (1943). *See, e.g.*, *Grand River Enters. Six Nations, Ltd. v. Beebe*, 574 F.3d 929 (8th Cir. 2009), *Sanders v. Brown*, 504 F.3d 903 (9th Cir. 2007); *PTI, Inc. v. Philip Morris, Inc.*, 100 F. Supp. 2d 1179 (C.D. Cal. 2000). The Third Circuit held that state action immunity was not available because the anticompetitive injury resulted from the tobacco companies' conduct after implementation of the MSA, rather than from conduct by the state, and the state's policy to replace competition with regulation, although clearly articulated, was not actively supervised. *A.D. Bedell Wholesale Co., Inc. v. Philip Morris, Inc.*, 263 F.3d 239 (3d Cir. 2001) *cert. den.,* 534 U.S. 1081 (2002). The Third Circuit expressed doubt about this conclusion, but adhered to it in *Mariana v. Fisher*, 338 F.3d 189, 203 (3d Cir. 2003).

35 Regarding antitrust preemption, courts hearing challenges to the MSA and its related legislation have applied the test set forth in *Rice v. Norman Williams Co,*, 458 U.S. 654 (1982), which is that preemption applies only if the statute in question "mandates or authorizes" illegal, anticompetitive behavior in all cases. These courts have uniformly held that neither the MSA nor its related legislation does so. *See, e.g.*, *Freedom Holdings, Inc. v. Cuomo*, 624 F.3d 38 (2d Cir. 2010); *Trident Int'l Corp. v. Kentucky*, 467 F.3d 547 (6th Cir. 2006); *KT&G Corp. v. Attorney Gen'l of State of Oklahoma*, 535 F.3d 1114 (10th Cir. 2008).

36 *Star Scientific, Inc. v. Beales*, 278 F.3d 339 (4th Cir.), *cert. den. sub nom. Star Scientific, Inc. v.*

Most of these suits have been brought against a single attorney general

Kilgore, 537 U.S. 818 (2002) (due process, equal protection, Commerce Clause, Compact Clause); *Mariana v. Fisher*, 226 F. Supp. 2d 575 (M.D. Pa. 2002), *aff'd on other grounds*, 338 F.3d 189 (3d Cir. 2003), *cert. den. sub nom. Mariana v. Pappert*, 540 U.S. 1179 (2004) (Commerce Clause, Compact Clause); *Grand River Enters. Six Nations Ltd. v. Pryor*, 2003 WL 22232974 (S.D.N.Y. Sep 29, 2003) (Commerce Clause, due process, equal protection, preemption, First Amendment), *vacated in part on other grounds*, 2004 WL 1594869 (S.D.N.Y. Jul. 15, 2004), *rev'd as to Commerce Clause claim*, 425 F.3d 158 (2d Cir. 2005), *rehearing den.* (Jan. 3, 2006), *cert. den. sub nom. King v. Grand River Enterprises Six Nations, Ltd.*, 549 U.S. 951 (2006), *on remand*, 2006 WL 1517603 (S.D.N.Y.) (preliminary injunction *den.*), *aff'd,* 481 F.3d 60 (2d Cir. 2007), *summary judgment granted to defendants*, 783 F. Supp. 2d 516 (S.D.N.Y. 2011); *Freedom Holdings, Inc. v. Spitzer*, 357 F.3d 205, *reh'g den.*, 363 F.3d 149 (2d Cir. 2004), *on remand*, 447 F. Supp. 2d 230 (S.D.N.Y. 2004), *recon. den.*, 2004 WL 2251668 (S.D.N.Y. Oct 06, 2004), *aff'd on other grounds*, 408 F.3d 112 (2d Cir. 2005), *on remand*, *Freedom Holdings, Inc. v. Cuomo*, 592 F. Supp. 2d 684 (S.D.N.Y. 2009), *aff'd,* 624 F.3d 38 (2d Cir. 2010), *cert. den.*, 131 S. Ct. 1810 (2011) (Commerce Clause); *Forces Action Project, LLC v. State of California*, No. C99-0607MJJ (N.D. Cal. Jan. 15, 2002), *aff'd*, 2003 WL 1900848 (9th Cir. Apr. 17, 2003) (No. 02-15336) (motion to amend complaint to add Commerce Clause claim denied on ground of futility); *Coker v. Foti*, 2006 WL 3307445, 2006 U.S. Dist. LEXIS 82537(W.D. La. Nov. 9, 2006), C.A. No. 1372 (W.D. La. Sep. 24, 2009), *aff'd sub nom. S&M Brands, Inc. v. Caldwell*, 614 F.3d 172 (5th Cir. 2010), *cert. den.*, 131 S. Ct. 1601 (2011) (Compact Clause, Commerce Clause, due process); *S&M Brands, Inc. v. Summers*, 393 F. Supp. 2d 604 (M.D. Tenn. 2005), *aff'd*, 228 Fed. Appx. 260 (6th Cir. 2007) (due process, equal protection, First Amendment); *Xcaliber Int'l Ltd., LLC v. Ieyoub*, 377 F. Supp. 2d 567 (E.D.La. 2005), *vacated and remanded*, *Xcaliber Int'l. Ltd., LLC v. Foti*, 442 F.3d 233 (5th Cir. 2006), *on remand*, 2009 U.S. Dist. Lexis 39081 (E.D. La. May 7, 2009), *aff'd*, 612 F.3d 368 (5th Cir. 2010) (First Amendment, due process, equal protection); *International Tobacco Partners, Ltd. v. Kline*, 475 F. Supp. 2d 1078 (D.Kan. 2007) (Commerce Clause); *Xcaliber Int'l Ltd. v. Edmondson*, (C.A. 04-CV-922-EA(C)) (N.D. Okla. Apr. 5, 2005), *aff'd sub nom. KT&G Corp. v. Attorney Gen'l of State of Oklahoma*, 535 F.3d 1114 (10th Cir. 2008) (First Amendment, due process, equal protection, Commerce Clause); *Xcaliber Int'l Ltd. v. Kline*, No. 05-2261, 2006 WL 288705 (D.Kan. July 29, 2005, Feb. 7, 2006), *aff'd sub nom. KT&G Corp. v. Attorney Gen'l of State of Oklahoma*, 535 F.3d 1114 (10th Cir. 2008) (First Amendment, due process, equal protection); *Grand River Enters. Six Nations, Ltd. v. Beebe*, 418 F. Supp. 2d 1082 (W.D. Ark. 2006), *aff'd*, 574 F.3d 929 (8th Cir. 2009) (First Amendment, equal protection, due process, Commerce Clause, preemption), *cert. den.*, 130 S. Ct. 2095 (2010); *International Tobacco Partners, Ltd. v. Beebe*, 420 F. Supp. 2d 989 (W.D. Ark. 2006) (First Amendment, due process, equal protection); *Dos Santos, S.A. v. Beebe*, 418 F. Supp. 2d 1064 (W.D. Ark. 2006) (First Amendment, due process, equal protection, Commerce Clause, preemption); *North American Trading Co. v. National Ass'n of Attys Gen'l*, Civ. Action No. 01-01600 (D.D.C. Sept. 18, 2001), *aff'd on other grounds*, 2002 U.S. App. LEXIS 24198 (D.C. Cir. Nov. 25, 2002) (Commerce Clause); *Star Scientific, Inc. v. Carter*, 2001 WL 1112673 (S.D. Ind. Aug. 20, 2001) (Commerce Clause); *PTI, Inc. v. Philip Morris Inc.*, 100 F. Supp. 2d 1179 (C.D. Cal. 2000) (Compact Clause, Commerce Clause, equal protection, due process, bill of attainder, preemption); *Hise v. Philip Morris Inc.*, 46 F. Supp. 2d 1201 (N.D. Okla. 1999), *aff'd mem.*, 208 F.3d 226 (10th Cir.), *cert. den.*, 531 U.S. 959 (2000) (Compact Clause); *VIBO Corp., Inc. v. Conway*, 594 F. Supp. 2d 758 (W.D. Ky 2009), *aff'd,* 669 F.3d 675 (6th Cir. Ky. 2012) (6th Cir. Jan. 28, 2010) (equal protection, due process, Commerce Clause, Compact Clause).

challenging a state's statutes in that state, but some plaintiffs have also sought to sue multiple state attorneys general at once in a single forum. NPM plaintiffs sought to sue 15 attorneys general and the National Association of Attorneys General in the District of Columbia about the states' respective Qualifying and Complementary Statutes, but that attempt was rebuffed for lack of personal jurisdiction over the attorneys general.[37] Another NPM, Grand River Enterprises Six Nations, Ltd., sued 30 out-of-state attorneys general in the Southern District of New York challenging their respective state Statutes. The Second Circuit ruled that there was personal jurisdiction under New York's long-arm statute based on a nexus between the negotiations by the attorneys general with the OPMs in New York City in 1998, which concerned not only the MSA but also the Model Statute eventually adopted in those states, and the lawsuit challenging the Statutes.[38]

An SPM attempted to use the Grand River precedent to file suit against 41 state attorneys general in the Southern District of New York over an alleged antitrust conspiracy. It alleged that the states' refusal to place the NPM's brands on their Complementary Legislation directories and NAAG's refusal to place the brands on its informational List of Participating Manufacturers and Brands were done at the direction of NAAG to exclude the company from the cigarette market.[39] The non-New York attorneys general filed a motion to dismiss based on lack of personal jurisdiction, arguing that the alleged antitrust violation related to the Complementary Legislation, not the negotiation of the MSA in New York. The court agreed and dismissed the claims against the attorneys general and NAAG.[40]

Enforcement of the MSA/STMSA

State attorneys general have brought several cases to enforce the MSA's terms. For example, several states initiated court proceedings to stop R.J. Reynolds Tobacco Co. (RJR) from maintaining outdoor advertising year-round at certain race tracks within the states in connection with NASCAR races. The

37 *North American Trading Co. v. National Ass'n of Attys Gen'l*, Civ. Action No. 01-01600 (D.D.C. Sept. 18, 2001), *aff'd on other grounds*, 2002 U.S. App. LEXIS 24198 (D.C. Cir. Nov. 25, 2002).

38 *Grand River Enters. Six Nations Ltd. v. Pryor*, 425 F.3d 158 (2d Cir. 2005), *reh'g den.* (Jan. 3, 2006), *cert. den.*, 549 U.S. 951 (2006).

39 *Cutting Edge Enter., Inc. v. Nat'l Ass'n of Atty's General*, 481 F. Supp. 2d 241 (S.D.N.Y. 2007).

40 *Id.*

NASCAR racing season extends from February to November, and races are held around the country. The MSA permits outdoor advertising by tobacco companies to be posted at a sponsored event from 90 days before the event until 10 days after. Because NASCAR races continue at various venues throughout the country for more than nine months of the year, RJR argued that the MSA's language referred to the first and last events of RJR's Brand Name Sponsorship series as a whole. The states argued that the MSA referred to the first and last days of events at particular race sites. In the California and Arizona cases, the court agreed that the outdoor advertising must be restricted to 30 days before and 10 days after the race at that site.[41] In the New York case, the court interpreted "initial sponsored event" to mean the first race in the NASCAR Winston Cup Series, and therefore concluded that the signs could remain up for the entire racing season.[42]

Another enforcement action undertaken by the attorney general of California involved the placement of cigarette advertising by RJR in magazines with substantial youth readership (ages 12-17), both in percentage terms and in absolute numbers. The state alleged that the advertising violated §III(a) of the MSA, which prohibits Participating Manufacturers from directly or indirectly targeting youth within any Settling State in their advertising, promotion or marketing of tobacco products. The California Court of Appeal held that the "targeting" of youth required an element of intent by the manufacturer, but found that RJR had such intent because it "knew to a substantial certainty that its advertising was exposed to youth to the same extent it was exposed to young adults."[43] The Court of Appeal upheld the trial court's ruling requiring the company to take specific actions to comply with the terms of the MSA, but reversed its award of sanctions based on nationwide, rather than state-specific, advertising spending. The parties later entered into a settlement setting specific limits on RJR cigarette advertising in magazines.

The attorney general of Ohio brought an enforcement action seeking to stop the distribution of matchbooks printed with cigarette brand logos. The manufacturer argued that because the matchbooks were frequently distributed for free with the purchase of cigarettes, they were not "merchandise" within the meaning of the MSA's prohibition on distribution of merchandise with tobacco product

41 *People ex rel. Lockyer v. R.J. Reynolds Tobacco Co.*, 132 Cal.Rptr.2d 151 (Cal. Ct. App. 4th Dist. 2003); *State ex rel. Goddard v. R.J. Reynolds Tobacco Co.*, 75 P.3d 1075 (Ariz. Ct. App. 2003).

42 *State v. R.J. Reynolds*, 761 N.Y.S.2d 596 (App. Div. 2003).

43 *People ex rel. Lockyer v. R.J. Reynolds Tobacco Co.*, 11 Cal. Rptr. 3d 317 (Cal. App. 4th Dist. 2004).

brand names.[44] The Ohio courts disagreed, finding that the fact that more than 80 percent of matchbooks were distributed for free did not remove them from the category of merchandise. "To find otherwise would eviscerate the ban on marketing and distribution of brand name apparel or other merchandise contained in the MSA."[45]

Two states reached a settlement with a cigarette manufacturer that was violating § III(g) of the MSA by distributing free cigarettes through the mail without first properly verifying the identity and age of recipients and ensuring they wanted to participate in consumer testing and evaluation of cigarettes. The manufacturer agreed to disclose to prospective recipients of free cigarettes that it would mail them only to adults who have given their prior consent to receive the free cigarettes specifically for evaluation or testing purposes. The manufacturer agreed to verify that each person who signs one of its consent forms is indeed an adult, and that it would mail free cigarettes only to persons whose consent forms or consumer evaluation forms are received within the prior 180 days. The manufacturer also agreed to limit the number of packs per mailing, the number of mailings per year, and the size of mailers. The manufacturer must also report on a semiannual basis to the states the number of free cigarettes it mails to persons in each of the states. Finally, the PM agreed to pay $175,000 to be shared between the two states for investigative costs.[46]

The attorney general of Vermont sued RJR over its marketing of "Eclipse" brand cigarettes with several express and implied health claims, including the claim that Eclipse "is a cigarette that may present less risk of cancer, chronic bronchitis, and possibly emphysema." Vermont alleged that these claims violate § III(r) of the MSA: "No Participating Manufacturer may make any material misrepresentation of fact regarding the health consequences of using any Tobacco Product, including any tobacco additives, filters, paper or other ingredients." Vermont further alleged that the claims violate its Consumer Fraud Act, which prohibits unfair or deceptive acts or practices in the course of trade or commerce. Under such laws, as under the FTC Act, marketers may not make "health claims" about their products unless they have substantiation for those claims on file. After lengthy pre-trial proceedings and a trial involving extensive expert testimony and the participation of attorneys from several other attorney general offices, the trial

44 MSA § III(f).

45 *State ex rel. Petro v. R.J. Reynolds Tobacco Co.*, 787 N.E.2d 717 (Ohio Ct. App. 2003), *aff'd,* 820 N.E.2d 910 (Ohio 2004).

46 Press Release, Office of the Attorney General of California, "Attorney General Reaches Settlement with R.J. Reynolds Over Free Cigarette Mailings," Jan. 5, 2001.

court ruled that certain of the claims for Eclipse violate the Vermont Consumer Fraud Act as well as MSA § III(r), which the court held embodies the same standards as the Consumer Fraud Act.[47] The court later assessed a civil penalty of $8,328,000 against RJR and entered a permanent injunction against its making similar misrepresentations in the future.[48]

Three states sued a cigarette manufacturer for MSA violations due to the manufacturer's advertising campaign that targeted youth smokers in violation of § III(a) of the MSA and other provisions of the MSA. The campaign included special edition cigarette packs, retail displays and point-of-sale merchandise portraying self-described "urban Hip-Hop culture" appealing to youth. The ad campaign featured these hip-hop themed cigarettes, displays, and radios in numerous convenience stores, drug stores, gas stations and other retail locations, despite knowledge that three-fourths of teenagers shop at convenience stores at least once a week, and teens are more likely than adults to be influenced by promotional pieces in such stores. Further, hip-hop themed cigarette ads and CDs and CD-ROMs appeared in magazines with high youth readership. Accordingly, there was significant youth exposure to these cigarette packs and displays. One of the suing states obtained a Temporary Restraining Order, which led to a settlement with the manufacturer and all three suing states whereby the manufacturer agreed to stop the specific ad campaign.[49]

In another case involving tobacco targeted at youth, RJR was selling cigarettes in sweet and alcohol-named flavors and appealing to youth through packaging and advertising schemes also attractive to youth. Following an extensive investigation by a multi-state group of attorneys general into RJR's marketing, promotion and advertising of many of its flavored cigarettes, forty-one states signed a settlement agreement wherein RJR agreed to specific marketing restrictions limiting the characterizations, descriptors and names of their cigarettes in their marketing and promotions outside of adult-only facilities. The goal of these limits was to cease use of names attracting youth, specifically names indicating sweet or alcoholic cigarette flavors.[50]

States have also initiated several actions against cigarette manufacturers for failing to report some of their U.S. cigarette sales to the Independent Auditor

47 *State of Vermont v. R.J. Reynolds Tobacco Co.*, 2010 Vt. Super. LEXIS 11 (Mar. 10, 2010).

48 2013 Vt. Super. LEXIS 15 (June 3, 2013).

49 Press Release, Office of the Attorney General of Maryland, "Landmark Settlement of "Kool Mixx" Tobacco Lawsuits," Oct. 6, 2004.

50 Press Release, Office of the Attorney General of Illinois, "39 Attorneys General and R.J. Reynolds Reach Historic Settlement to End Its Sale of Flavored Cigarettes," Oct 11, 2006.

under the MSA, resulting in these manufacturers paying substantially less than they owed under the MSA. Two of those cases resulted in recoupment of the underpayments by the states.[51] In a third case the SPM filed for bankruptcy and ultimately went out of business.[52]

Emerging Issues

Non-Participating Manufacturer Adjustment

As discussed above, the MSA's Non-Participating Manufacturer Adjustment allows Participating Manufacturers potentially to reduce their settlement payments due in a year if they lose market share during the preceding year.[53] An NPM Adjustment can be applied to reduce a settlement payment only if during a given year (a) there has occurred a Market Share Loss as defined in the MSA, (b) an economic consulting firm determines that the disadvantages imposed on Participating Manufacturers by the MSA were a significant factor contributing to the Market Share Loss, and (c) one or more states failed to "diligently enforce" their Model Statutes.[54]

The NPM Adjustment is first calculated as a percentage equal to three times the percentage of the Manufacturers' Market Share Loss. That percentage trebled is then applied to the Participating Manufacturers' aggregate settlement payment to come up with the dollar amount of the NPM Adjustment. That amount is then divided among those states, if any, that are determined not have "diligently enforced" their Model Statutes during the year in which the Market Share Loss occurred.

As noted earlier, the Participating Manufacturers' aggregate MSA settlement payment is distributed annually among the states pursuant to a formula established in Exhibit A to the MSA. Each state's distribution percentage is known as its "Allocable Share." For a state found to have "diligently enforced" its Model Statute during the year, what might have otherwise been its Allocable

51 *State of Missouri ex rel. Nixon v American Tobacco Co and Premier Manufacturing, Inc.*, No. 972-1465, Div. 19 (Cir. Ct. St. Louis City, 22nd Jud. Cir. Mo., June 24, 2003); *State of Iowa ex rel. Miller v. R.J. Reynolds Tobacco Co. and Tobacco & Candy International, Inc.*, No. CL 000 71048 (Dist. Ct. Polk Cty, Iowa).

52 *In re Alliance Tobacco Corp.*, Case No. 03-11030 (Bankruptcy Ct. W.D. Ky).

53 MSA §IX(d)

54 MSA §IX(d)(2).

Share of the NPM Adjustment had it been found "non-diligent" is reallocated to those states in fact found "non-diligent." Because of this reallocation provision, a "non-diligent" state can have its distribution of an annual settlement payment reduced by more than the state's Allocable Share of the NPM Adjustment and, indeed, such state can potentially lose its entire distribution or share of the MSA settlement payment in a year.

Attorney-Client Privilege and Common Interest Doctrine

Several tribunals have recognized that an attorney-client relationship exists between NAAG and its member attorneys general as well as their states. This relationship has been held to confer a privileged status on communications between NAAG counsel and the attorneys general and their counsel.

In the Grand River litigation in the Southern District of New York, discussed above, the plaintiffs sought discovery of various communications between NAAG counsel and the staffs of the 31 defendant attorneys general. The district court, affirming a decision by the magistrate judge, accepted the defendants' argument that such communications were not discoverable because an attorney-client relationship existed between NAAG and the recipients of the communications, and the communications at issue related to legal advice.[55] Based on its review of the documents, the court concluded that "the state attorneys general and the National Association of Attorneys General are generally the attorneys and the states and their relevant agencies are the clients. It does appear, though, that in some instance the attorneys general also acted as clients."[56] The magistrate judge had previously ruled that the states, by virtue of their being parties to the MSA, held a common interest that protected against a waiver of privilege notwithstanding their having shared privileged communications with each other.[57]

In *Tobaccoville USA, Inc. v. McMaster,*[58] a dispute arose over whether certain communications between the South Carolina attorney general and NAAG were entitled to attorney-client privilege. The South Carolina Supreme Court held:

55 *Grand River Enters. Six Nations Ltd. v. King*, 2009 U.S. Dist. LEXIS 2045 (S.D.N.Y. Jan. 12, 2009), *aff'g Grand River Enterprises Six Nations, Ltd. v. King*, 2008 U.S. Dist. LEXIS 112748 (S.D.N.Y. April 18, 2008).

56 *Id*. at *55.

57 2008 U.S. Dist. LEXIS 112748 at *54. The district court held that the plaintiff had "effectively conceded" its common interest objections by not raising them before the court. 2009 U.S. Dist. LEXIS 2045 at *53.

58 692 S.E.2d 526, 530 (S.C. 2010)

> While the relationship the AG has with the NAAG is not the traditional attorney-client relationship envisioned in *Doster,* we nonetheless find that these communications may be covered by the attorney-client privilege. As the ALC noted, the AG has not "retained" the NAAG attorneys in this matter or with respect to the disputed documents. However, the AG is a paid member of the NAAG, and NAAG staff attorneys are available to provide legal advice relating to the MSA and tobacco regulation and enforcement. . . . Thus we hold that the attorney-client privilege may apply to this very narrow factual scenario because the AG, as a paid member, has solicited the NAAG attorneys for legal advice and consultation on matters relating to the tobacco litigation, the MSA, subsequent enforcement of the MSA, and tobacco regulation.

The Court remanded the matter for a determination whether the documents in question did in fact relate to legal advice. (The matter was settled before such a determination could be made.) The Court further held that the documents were not protected by the work-product doctrine because they were not created because of the prospect of litigation.[59] Finally, the Court recognized and applied the common interest doctrine, holding:

> [T]he AG has a common interest with the other settling state attorneys general in matters relating to the MSA and tobacco regulation and litigation. The settling state attorneys general and the NAAG are working together to have uniform tobacco regulations and enforcement of the MSA. Accordingly, if the documents were privileged and thus exempt from production, that privilege was not waived when the AG shared the information with other state attorneys general.[60]

An arbitration panel, in the context of the "Non-Participating Manufacturer Adjustment", described above, addressed a motion by a group of states for an order protecting against disclosure and use in the arbitration of certain documents containing or reflecting communications between NAAG and those states relating to enforcement of the MSA and the states' Model Statutes. In granting the motion, the panel first determined that an attorney-client relationship exists between NAAG and the states. The panel noted that "[t]he MSA specifically

59 692 S.E.2d at 530.

60 387 S.C. at 296, 692 S.E.2d at 531.

assigned the NAAG the obligation to 'provide coordination and facilitation for the implementation and enforcement of this Agreement on behalf of the Attorneys General of the Settling States.'"[61] The panel also observed that "The NAAG Constitution contemplates a confidential relationship between staff and the attorneys general."[62] Despite the lack of an explicit reference to NAAG or its staff as "attorneys" for the states, the panel held:

> [T]hese documents taken in totality express a mutual intent that the NAAG lawyers provide legal services for the States. The fact is that "NAAG staff" referred to in the documents are attorneys, that a confidential relationship is contemplated, and that the attorneys at the NAAG may act as the States' agent when so directed. Further, when an attorney supports the efforts of the states to "enforce" and "defend" a complex agreement like the MSA, they are providing legal services.[63]

Turning to the documents at issue, the arbitration panel ruled that several of the documents contained communications entitled to privilege. It further ruled that to the extent that certain presentations made by NAAG staff at conferences "provided legal advice, they will be privileged and shielded from both discovery and admissibility," but "to the extent that they provide general training regarding compliance with the MSA, without containing legal advice or revealing client confidences, they will not be protected by the attorney-client privilege. . . ." [64] The panel also found that documents containing strategizing and advice relating to the NPM Adjustment Proceedings themselves were entitled to work-product protection because, at the time the documents were created, the states anticipated that such Proceedings would likely take place, but that the case for such protection was weak because the PMs were already aware of the strategy and advice contained in the documents.[65] Finally, the panel relied on the common interest doctrine in rejecting the PMs' arguments that the states had waived privilege and

61 *In the 2003 NPM Adjustment Proceedings, Order re: Protective Order* (Jan. 18, 2011), at 7 (citing MSA § VIII(a)).

62 *Id.* (citing NAAG Constitution, Article II.2.). The panel also referred to the statement on the NAAG website that "The mission of the NAAG Tobacco Project is "to provide highly qualified and experienced attorneys and support staff to preserve the MSA and to maximize its value to the Settling States by supporting their efforts to enforce, defend and improve the agreement."

63 *Id.*

64 *Id.* at 12.

65 *Id.* at 12-15.

work-product protection by sharing protected documents with states that have open records laws and with states not party to the MSA.[66]

Bankruptcy

Some Participating and Non-Participating Manufacturers have sought bankruptcy protection, and the states have actively participated in the bankruptcy proceedings, occasionally as the bankrupt's largest creditors. These cases are discussed in Chapter 20.

66 *Id*. at 17-19.