UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

R.J. REYNOLDS TOBACCO CO. *et al.*,

Plaintiffs,

v.

UNITED STATES DEPARTMENT OF AGRICULTURE *et al.*,

Defendants.

Civil Action No. 1:14-cv-01388 (KBJ)

REPLY BRIEF IN SUPPORT OF DEFENDANTS' MOTION TO DISMISS

In their opposition, plaintiffs insist that USDA has an obligation to analyze allegations of illicit or smuggled cigarettes and to independently determine those volumes. Yet plaintiffs fail to identify any congressionally-conferred investigative authority or law enforcement power that would enable USDA to meaningfully or reliably ascertain volumes of illicit tobacco products. In light of those limitations, USDA explained at the administrative level that it would refer plaintiffs' report of cigarette smuggling to other federal agencies with tobacco enforcement powers. And if those agencies substantiated plaintiffs' claims and provided the type of reliable and specific data USDA needs to calculate quarterly assessments, USDA would adjust the amount of plaintiffs' assessment due under the Fair and Equitable Tobacco Reform Act ("FETRA").

Plaintiffs' lawsuit challenges the reasonableness of USDA's method for addressing the smuggled cigarette problem. Specifically, plaintiffs contend that not only must USDA definitively determine volumes of smuggled cigarettes, but also USDA must do so independently, without deferring to the expertise and investigatory authority of the Bureau of Alcohol, Tobacco, Firearms and Explosives, the Department of Treasury, or the Department of

Homeland Security. But FETRA does not impose that requirement on USDA. USDA's published regulations similarly reject the imposition of such a broad responsibility upon USDA with respect to determining quarterly volumes of smuggled tobacco products. Accordingly, plaintiffs' legal theory is contrary to law, and their complaint fails to state a claim for relief.

ARGUMENT

I. Plaintiffs Do Not State a Claim for Relief Because It Was Reasonable for USDA to Require Substantiation of Volumes of Allegedly Smuggled Cigarettes.

It is undisputed that neither FETRA nor any other statute confers investigatory or enforcement powers upon USDA with respect to determining volumes of smuggled tobacco products. Rather, USDA's responsibilities under FETRA are to calculate quarterly assessments on manufacturers and importers of tobacco products, *see* 7 U.S.C. § 518d(e)-(h), to collect the quarterly assessments from those manufacturers and importers, *see id.* § 518d(b), and to disburse subsidies to tobacco growers and quota holders, *see id.* § 518c.[1] While those obligations require that USDA perform several complex calculations, FETRA does not impose responsibility for determining the volumes of tobacco products sold or otherwise removed into commerce upon USDA. Instead, FETRA requires that USDA, for the most part, use the information tobacco manufacturers and importers provide to other federal agencies to calculate the quarterly

[1] Contrary to plaintiffs' characterization, USDA does not figuratively place its head in the sand when difficult issues arise in the administration of FETRA. *See* Pls.' Mem. at 22. USDA found a way to reverse engineer the algorithm used by Congress for determining assessments where FETRA was silent on that issue. *See generally Determination of the Administrator of the Farm Service Agency and Executive Vice President of the Commodity Credit Corporation Regarding the Current "Step A" and "Step B" Assessment Methods in the Tobacco Transition Payment Program*, at 5-10, Nov. 16, 2011 (hereafter "the Final Administrative Determination") (available at http://www.fsa.usda.gov/Internet/FSA_File/tobacco_determ_11162011.pdf). USDA also determines market share to the fourth decimal place. *See* 70 Fed. Reg. 72979 (Dec. 8, 2005). And USDA has increased the transparency of its operations over time. *See* Final Administrative Determination at 29. Finally, USDA has ensured the continuity of its calculation methodology despite fluctuations in excise tax rates. *See id.* at 19, 31-40.

assessments. *See id.* § 518d(h)(1); *see also* § 518d(h)(2). USDA is also to use "any other relevant information provided to or obtained by the Secretary.". *Id.* § 518d(g)(1).

Those foundational principles guided USDA's resolution of plaintiffs' challenge at the administrative level. There, plaintiffs submitted a report that provided estimates and extrapolations for cigarettes allegedly trafficked illicitly by two entities in New York. USDA determined that it could not meaningfully evaluate plaintiffs' claims as to the volume and timing of smuggled cigarettes, and for that reason, USDA referred the matter to federal law enforcement agencies to substantiate plaintiffs' estimates. *See* Adjudicatory Decision at 5 (copy attached as Ex. 1 to Mot. to Dismiss, ECF No. 10). As part of that administrative process, USDA acknowledged that if plaintiffs' reports were substantiated by those law enforcement agencies – resulting in the kind of precise data USDA could use to calculate quarterly assessments – then USDA would later adjust plaintiffs' FETRA assessments through the "true up" process. *See id.*

In explaining its decision, USDA found that plaintiffs' evidence was "largely based on estimates, approximations, and assumptions, from which neither [plaintiffs] on the Secretary can reliably, much less accurately determine amounts and timing of the tobacco placed into commerce so as to correctly adjust quarterly [plaintiffs'] TTPP assessment levels." *See* Adjudicatory Decision at 5. Plaintiffs do not dispute that finding. *Id.* It was precisely because USDA determined that plaintiffs' evidence was insufficient and would necessarily lead to arbitrary results that USDA determined that absent its substantiation by federal law enforcement agencies, it would not be relevant to the FETRA calculation process. *See id.*

Plaintiffs argue that USDA should have more thoroughly evaluated their consultant's report and reached independent findings regarding the volume and timing of illicit cigarette production. Plaintiffs' principal argument rests on a single clause in 7 U.S.C. § 518d(g)(1) under

which USDA is to consider "any other relevant information provided to or obtained by the Secretary" in making FETRA assessments. *See* Pls.' Mem. at 19-27. Plaintiffs read that clause to require USDA to make definitive determinations regarding allegations as to the volume of smuggled tobacco products – a task that no other federal agency has been able to complete to date – based only on estimates and approximations provided by plaintiffs' consultant. Plaintiffs misconstrue FETRA in several respects.

First and most fundamentally, USDA's obligation to consider "any other relevant information" does not entirely transform USDA's regulatory responsibilities with respect to smuggled tobacco products. *See Whitman v. Am. Trucking Ass'ns, Inc.*, 531 U.S. 457, 468 (2001) ("Congress . . . does not alter the fundamental details of a regulatory scheme in vague terms or ancillary provisions – it does not, one might say, hide elephants in mouseholes."). Nonetheless, plaintiffs advocate just such a result by seeking to place responsibility on USDA – an agency without investigatory or law enforcement powers and that is administering a temporary transitional program – to determine precise volumes of smuggled tobacco products. Rather, when Congress fundamentally alters an agency's statutory responsibilities, it does so through far more direct and plain language. *See, e.g.*, 26 U.S.C. § 5703(d) (imposing a duty on the Secretary of Treasury with respect to excise taxes on tobacco products to "determine the amount of tax which has been omitted to be paid, and to make an assessment therefor against the person liable for the tax"). Thus, USDA's responsibilities under FETRA are best understood as explained in the *Single Stick* decision, which permitted USDA to base its calculations, not on the volumes of all smuggled tobacco products, but based on the materials from other federal agencies. *See Single Stick, Inc. v. Johanns*, 601 F. Supp. 2d 307, 314-15 (D.D.C. 2009), *reversed*

and remanded on other grounds sub nom. Prime Time Intl., Inc. v. Vilsack, 599 F.3d 678 (D.C. Cir. 2010).

In addition, USDA's position is consistent with Supreme Court precedent rejecting expansive readings of federal agencies' regulatory powers in this context. For instance, in *FDA v. Brown & Williamson Tobacco Corp.*, 529 U.S. 120 (2000), the Supreme Court emphasized that "[r]egardless of how serious the problem an administrative agency seeks to address . . . it may not exercise its authority 'in a manner that is inconsistent with the administrative structure that Congress enacted into law.'" *Id.* at 120, 125 (quoting *ETSI Pipeline Project v. Missouri*, 484 U.S. 495, 517 (1988)). In light of that principle, the Supreme Court determined that the FDA could not regulate cigarettes as "drugs" or "devices" under the FDA Act because *inter alia* the FDA had never regulated tobacco products in the past. *See id.* at 144. Much as the FDA had no historical practice of regulating tobacco products, USDA has never independently evaluated or determined volumes of smuggled tobacco products. To the contrary, as USDA explained, it "historically has referred any purported allegations of smuggling, illegal manufacturing, or importing of tobacco products, to an appropriate tobacco enforcement agency." Adjudicatory Decision at 5. Looking ahead as well, it should be remembered that USDA had responsibilities under FETRA for only ten years, which will soon expire, and at that time, USDA will return to having no responsibilities with respect to smuggled cigarettes.

The holding in *Gonzales v. Oregon*, 546 U.S. 243 (2006), is also informative here. In that case, the Attorney General through a rule determined "that using controlled substances to assist suicide is not a legitimate medical practice and that dispensing or prescribing them for this purposed is unlawful under the [Controlled Substances Act]." *Id.* at 249. The Supreme Court invalidated that rule, reasoning that "the structure of the CSA . . . conveys unwillingness to cede

medical judgments to an executive official who lacks medical expertise." *Id.* at 266; *see also id.* at 269 (recounting "the Attorney General's lack of expertise in this area"). Just as the Attorney General's regulatory authority was limited by his lack of medical expertise, USDA has no specialized expertise in the area of determining actual volumes of smuggled cigarettes.

Taken together, *Brown and Williamson* and *Gonzales v. Oregon* confirm that federal agencies are not expected to have regulatory responsibilities in areas that they have historically declined to regulate or that are beyond their expertise. Applied here, where the independent evaluation of quarterly volumes of smuggled cigarettes is both beyond USDA's historical regulatory practice and outside of USDA's expertise, plaintiffs' efforts to impute such an obligation to USDA must fail.

USDA's rationale is based on a responsible construction of the scope of its congressionally-delegated powers, and not simply an effort to avoid a difficult task as plaintiffs claim. *See* Pls.' Mem. at 17, 30-31. The limitations inherent in plaintiffs' cases confirm this point. For instance, in *Chamber of Commerce v. SEC*, 412 F.3d 133 (D.C. Cir. 2005), the SEC did not calculate the costs of compliance with a rule issued under the Investment Company Act of 1940, as the SEC was statutorily required to do. *See id.* at 143-44. And in *Cobell v. Salazar*, 573 F.3d 808 (D.C. Cir. 2009), the Department of Interior was sued for not satisfying its statutory obligation to make an accounting of the Native American Trust Fund. *See id.* at 813. The commonality of those cases is that they both involved a clear statutory command on an issue central to an agency's mission. By contrast, neither of those conditions is satisfied here. FETRA provides no clear statutory command for USDA to independently determine quarterly volumes of smuggled tobacco products, nor does USDA have expertise or meaningful authority with respect to the determination of the volumes of smuggled tobacco products.

Finally, plaintiffs argue that USDA's adjudicatory decision denies meaning to the phrase "any other relevant information provided to or obtained by the Secretary" as used in subsection (g)(1). *See* Pls.' Mem. at 25-26. But that is plainly incorrect because the Adjudicatory Decision made clear that USDA would consider other information (beyond that contained in reports and forms) if that information were substantiated by another federal agency. *See* Adjudicatory Decision at 5. As USDA explained, "the information and evidence presented by the Appellants must be substantiated by the U.S. Department of Treasury, the U.S. Department of Homeland Security, or the U.S. Department of Justice (Bureau of Alcohol, Tobacco, and Firearms) as appropriate, before the Secretary can rely upon it when determining individual assessments pursuant to [FETRA]." *Id.*; *cf.* 7 U.S.C. § 518d(h)(1) (requiring in general that USDA rely only upon "the returns and forms . . . that are required to be filed with a Federal agency). Thus, under USDA's determination, as long as other information is substantiated by another federal agency, USDA will use it to calculate FETRA assessments.

II. USDA's Decision Is Consistent with Its Published Regulation.

In its opening brief, USDA noted that its administrative determination was consistent with its own published regulation, 7 C.F.R. § 1463.7(b), which would prevent USDA from considering information regarding smuggled tobacco products that was not reported by another federal tobacco enforcement agency. *See* Mot. at 11-12. Plaintiffs raise two challenges to this argument – one procedural and one substantive. Both fail.

Procedurally, plaintiffs argue that USDA's reference to this regulation violates the rule against post-hoc rationalizations. *See* Pls.' Mem. at 17, 27-28. Plaintiffs first mistake USDA's purpose, which was not to advance a new justification for its administrative decision, but rather to point out that USDA's administrative decision is perfectly consistent with 7 C.F.R.

§ 1463.7(b). Even so, "[i]n administrative law, as in federal civil and criminal litigation, there is a harmless error rule." *PDK Labs Inc. v. DEA*, 362 F.3d 786, 799 (D.C. Cir. 2004). And because plaintiffs have identified no prejudice as a result of USDA relying on a previously published regulation, the Court may consider the regulation as a basis for USDA's determination, as was done in the *Single Stick* litigation, to confirm USDA's limited responsibilities regarding smuggled tobacco products. *See Single Stick*, 601 F. Supp. 2d at 314-15. Practically as well, the only relief that plaintiffs could achieve in this case would be a remand to the agency to reconsider its determination. *See generally Fla. Power & Light Co. v. Lorion*, 470 U.S. 729, 744 (1985) ("If the record before the agency does not support the agency action, if the agency has not considered all relevant factors, or if the reviewing court simply cannot evaluate the challenged agency action on the basis of the record before it, the proper course, except in rare circumstances, is to remand to the agency for additional investigation or explanation."). It serves little purpose to remand this case to USDA simply to announce that under a published it need not consider estimates and extrapolations of smuggled cigarettes unless those are substantiated by another federal agency.[2]

[2] Plaintiffs raise an additional procedural challenge, namely that by not submitting an administrative record, USDA did not comply with Local Rule 7(n). That argument misapplies Local Rule 7(n) in three respects. First, Rule 7(n) does not require filing an administrative record with a dispositive motion, but merely a certified *list* of the contents of the administrative record. *See* D.D.C. Civ. R. 7(n)(1). Second, Rule 7(n) applies to "cases involving the judicial review of administrative agency actions," but at this stage of the proceedings, all that is presented is a challenge to the sufficiency of plaintiffs' complaint. *Id.* To read the rule otherwise would require a certified list of the contents of the administrative record for dispositive motions claiming defective service or improper venue. Third, even if Rule 7(n) were to apply here, it has been substantially complied with. That rule ultimately requires "an appendix containing copies of those portions of the administrative record that are cited or otherwise relied upon in any memorandum in support of or in opposition to any dispositive motion," and "[c]ounsel shall not burden the appendix with excess material from the administrative record that does not relate to the issues raised in the motion or opposition." *Id.* And here, USDA included the only part of the administrative record that it relied upon (the Adjudicatory Decision).

Plaintiffs also dispute the substantive meaning of USDA's regulation, arguing that the regulation does not prevent USDA from considering materials, such as plaintiffs' report, that have not been submitted to tobacco enforcement agencies. *See* Pls.' Mem. at 27-28. But that contention profits plaintiffs nothing – USDA has already announced that it will consider data on smuggled cigarettes as long as those figures are substantiated by another federal agency. Plaintiffs' argument is also at odds with the *Single Stick* holding, which determined that it was permissible for USDA to base its calculations, not on the volumes of all smuggled tobacco products, but based on the materials from other federal agencies. *See Single Stick*, 601 F. Supp. 2d at 314-15.[3] Consistent with that holding, USDA referred plaintiffs' report to other federal agencies for substantiation. If substantiated, USDA would adjust plaintiffs' quarterly assessments, but if not, then as the Court held in *Single Stick*, USDA is not required to take further action. *See id.* at 315 (giving controlling deference to USDA's interpretation that FETRA did not require "inclusion of all smuggled or unlawfully imported [tobacco products] in calculating volume of domestic sales").

III. The APA Claim in Count 2 Should Be Dismissed.

Plaintiffs make minimal efforts to defend their second count (a claim under the APA). In fact, plaintiffs argue only in a footnote that their APA claim in Count 2 is an alternative theory of relief that should be permitted. *See* Pls.' Mem. at 24 n.3. Arguments in footnotes are disfavored

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[3] Plaintiffs do not challenge the correctness of the *Single Stick* holding, *see* Pls.' Mem. at 23, specifically that it was permissible for USDA to not include all smuggled or unlawfully imported tobacco products in its FETRA calculations. *See Single Stick, Inc.*, at 314-15. Plaintiffs do, however, misread that decision in significant manner because the Court in *Single Stick* never required USDA to consider "other relevant information" presented by manufacturers and importers to USDA, as plaintiffs' mistakenly assert, nor could that court have done so. That issue was not presented because Single Stick had not submitted any information on smuggled tobacco products for USDA's consideration. *Cf. Single Stick, Inc.*, at 314-15.

and are not entitled to any weight in this Circuit. *See Hutchins v. District of Columbia*, 188 F.3d 531, 539 n.3 (D.C. Cir. 1999) (en banc) (explaining that a court "need not consider cursory arguments made only in a footnote"). Plaintiffs' argument is also incorrect substantively. USDA explained that no relief is available under the APA when another adequate remedy at law exists. *See* 5 U.S.C. § 704; *Bowen v. Massachusetts*, 487 U.S. 879, 903 (1988). Here, plaintiffs admit that they have an adequate remedy under FETRA (the refund of their alleged over-assessments), *see* Pls.' Mem. at 24 n.3, and by law the APA cannot serve as an alternative argument. Count 2 of plaintiffs' complaint should be dismissed on that basis.

CONCLUSION

For the foregoing reasons, as well as those presented in the Motion to Dismiss, ECF No. 10, plaintiffs' complaint should be dismissed for failure to state a claim for relief.

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Respectfully Submitted,

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