UNITED STATES DISTRICT COURT
DISTRICT OF CONNECTICUT

GRAND RIVER ENTERPRISES SIX NATIONS, LTD.,	)	Civil Action No.
	)	
	)	3:16-CV-01087
Plaintiff,	)	
	)	
v.	)	
	)	
KEVIN B. SULLIVAN, Commissioner of Revenue Services of the State of Connecticut,	)	
	)	
	)	
	)	
Defendant.	)	DECEMBER 21, 2017

PLAINTIFF'S MEMORANDUM IN OPPOSITION TO DEFENDANT KEVIN B. SULLIVAN'S MOTION TO DISMISS SECOND AMENDED COMPLAINT

PLAINTIFF,
GRAND RIVER ENTERPRISES SIX NATIONS, LTD.,

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PRELIMINARY STATEMENT

Plaintiff Grand River Enterprises Six Nations, LTD ("GRE") submits this memorandum of law in opposition to the Motion to Dismiss Second Amended Complaint ("SAC") of the Defendant Commissioner of Revenue Services of the State of Connecticut, Kevin B. Sullivan ("Defendant" or "the Commissioner"). Contrary to the arguments of the Commissioner, GRE has standing and has stated claims for constitutional violation, just as it did in the substantially similar First Amended Complaint.

The Court denied the Commissioner's motion to dismiss the First Amended Complaint ("1st Mot. Dismiss"), *see* ECF No. 65, and aside from the new standing argument, that motion was based on substantially the same arguments presented in the instant motion. GRE refers the Court and incorporates by reference its brief in opposition to the prior motion to dismiss. *See* ECF No. 46. In the interest of completeness and for the Court's convenience, GRE provides the full factual background.

Like the First Amended Complaint, the SAC challenges Conn. Gen. Stat. § 4-28m(a)(3)(C), which imposes requirements on certain tobacco product manufacturers as a condition of having their cigarettes sold in Connecticut. Section 4-28m(a)(3)(C) requires certain foreign cigarette manufacturers to reconcile the number of cigarettes for which excise taxes on their cigarettes have been paid nationwide by independent importers of those products with the number of cigarettes shipped and sold into each State throughout the United States, as reported by those importers under the federal Prevent All Cigarette Trafficking ("PACT") Act, 15 U.S.C. § 375. If a cigarette manufacturer cannot "satisfactorily explain" to the Commissioner why it cannot reconcile these figures within a margin of two and one-half percent, the Commissioner bans the manufacturer's cigarettes from being sold in Connecticut. The Commissioner has twice, in the past two years, advised and threatened GRE that its failure to make the

reconciliation required under § 4-28m(a)(3)(C) will result in GRE's cigarettes being banned from sale in Connecticut.

GRE is a cigarette manufacturer that is covered by § 4-28m and was required to "satisfactorily explain" why it could not reconcile the numbers. In making its annual certification to the Commissioner, GRE first explained that, as a foreign manufacturer, GRE neither pays federal excise tax on its cigarettes that are imported and sold in and throughout the United States, nor is it required to file PACT Act reports for cigarettes sold to United States importers. Unsatisfied, the Commissioner demanded that GRE obtain confidential IRS federal excise tax returns of importers importing GRE's cigarettes into the United States (independent third parties), as well as the PACT Act reports or equivalent State (not Connecticut) reports filed by the importers tracking their shipments to or within any and all States within the United States.

Under reservation, GRE acquiesced to the Commissioner's demands. It requested and was provided federal excise tax returns of several importers that import GRE cigarettes into the United States, as well as the importers' PACT Act reports. GRE did not obtain the federal excise tax returns of importers that import GRE's cigarettes throughout Indian Country (as defined under Federal Law). The PACT Act does not apply to sales and shipments of cigarettes in and among Indian Country. GRE also explained that the PACT Act does not cover intrastate shipments of cigarettes by importers, thus the reconciliation was impossible. Finally, GRE demonstrated that, with respect to shipments made by importers into Connecticut, the number of cigarettes on which excise taxes were paid was consistent with the number reported for PACT Act purposes. In spite of the sound explanation, the Commissioner refused to accept it. He continued to demand that GRE reconcile the number of cigarettes reported for federal excise tax

purposes with the number reported under the PACT Act reports, or else GRE's cigarettes would be banned from sale in Connecticut.

In Count One of the SAC, GRE alleges that § 4-28m(a)(3)(C) violates substantive due process on its face and as applied because the legislation and the Commissioner's enforcement arbitrarily and irrationally requires GRE to reconcile two categories of data that were not intended to be—and in GRE's case, cannot be—reconciled. In Count Two, GRE alleges that § 4-28m(a)(3)(C) is preempted by federal law because it conflicts with the PACT Act, rendering GRE's compliance with state law impossible. In Count Three, GRE alleges that the Commissioner's application of § 4-28m(a)(3)(C) violates the Commerce Clause because it would require out-of-state companies that distribute GRE's products to submit to the Commissioner's regulatory authority by reporting wholly out-of-state activity. In Count Four, GRE asks this Court to construe § 4-28m(a)(3)(C) to avoid the aforementioned constitutional deficiencies and to declare that GRE's explanation regarding its inability to satisfy the reconciliation requirement is sufficient as a matter of law. GRE alleges sufficient facts to support each of these claims.

STATEMENT OF FACTS

I. The Parties

GRE is a Canadian corporation in the business of manufacturing cigarettes. SAC ¶ 11. GRE's Seneca®, Opal®, and Couture® brand cigarettes are approved for sale in Connecticut and have been on Connecticut's approved Tobacco Directory for the past four years. *Id.* ¶ 32. GRE has invested over $1 million to comply with Connecticut's regulatory requirements to earn and retain the right to sell its cigarettes in the State. *Id.* ¶¶ 9, 32.

The Commissioner is charged with licensing cigarette manufacturers in Connecticut and maintaining the Connecticut Tobacco Directory (the "Tobacco Directory" or "Directory"), which lists cigarette brands authorized for sale in Connecticut. *Id.* ¶ 12.

II. Relevant Federal Law Regulating Cigarette Manufacturers

An understanding of GRE's claims requires an overview of two areas of federal law regulating the cigarette industry, as well as how those laws apply to GRE's products. First, all cigarettes that are manufactured in or imported into the United States are subject to an excise tax. *See* 15 U.S.C. § 5701(b). Although GRE is not subject to this excise tax, United States importers of GRE's cigarettes pay an excise tax on each GRE cigarette they import.

Second, the PACT Act, 15 U.S.C. §§ 375–378, is federal legislation regulating the interstate shipment of cigarettes in the United States. As relevant here, the PACT Act requires any person who sells, transfers, or ships cigarettes in interstate commerce to comply with certain registration and reporting requirements. SAC ¶ 25. All such persons must register with the "tobacco tax administrator" of each State into which it ships or advertises cigarettes. 15 U.S.C. § 376(a)(1); SAC ¶ 26. In addition, all such persons must file a monthly report with the "tobacco tax administrator" of each State into which a shipment is made that details, among other things, the cigarette brand and quantity thereof included in each shipment. 15 U.S.C. § 376(a)(2); SAC ¶ 27. The PACT Act's reporting requirements do not apply to a foreign manufacturer's sale of cigarettes that are imported into the United States by third-party importers. Subsequent shipments by importers in interstate commerce (defined in the PACT Act) are subject to the PACT Act's reporting requirements. Thus, the PACT Act does not apply to purely intrastate shipments, nor to shipments within and among Indian Country—either within a single tribal region or from one tribal region to another.[1] 15 U.S.C. § 376(a); SAC ¶¶ 37–39.

[1] Two District Courts in the Second Circuit have so held. *See New York v. Grand River Enters. Six Nations, Ltd.*, 2016 U.S. Dist. LEXIS 117801, at *53–54 (W.D.N.Y. Aug. 30, 2016) and *State of New York v. Mountain Tobacco Co.*, No. 2:12-CV-06276, 2016 WL 3962992, at *8 (E.D.N.Y. July 21, 2016).

Although the PACT Act does not apply to GRE, it does apply to some, but not all, importers of GRE cigarettes. Importers that sell, transfer, or ship GRE cigarettes in interstate commerce as that term is defined in the PACT Act file reports for covered shipments with the States into which they ship, transfer, or sell GRE products. SAC ¶¶ 37–39; ECF No. 38, Ex. B (letter from Leonard Violi to Christine Bacon, Revenue Examiner for the Department of Revenue Services ("DRS"), dated June 21, 2016) (hereinafter "Ex. B").[2] Certain GRE importers, however, distribute GRE cigarettes exclusively within Indian Country and do not file any PACT Act reports. *Id.* Other importers distribute GRE cigarettes interstate as well as in intrastate commerce, and they do not file PACT Act reports for the latter shipments. *Id.* In addition to the many cigarettes shipped within Indian Country, over one million sticks of GRE cigarettes were distributed in intrastate commerce in 2015. SAC ¶ 39. None of the intrastate or Indian Country shipments of GRE cigarettes took place in Connecticut. SAC ¶¶ 38–39; Ex. B.

III. The Regulatory Scheme Governing Cigarette Sales in Connecticut

To have its cigarettes sold in Connecticut, a manufacturer is required to comply with various statutory requirements. First, all manufacturers are required to obtain from the Commissioner a cigarette manufacturer's license. Conn. Gen. Stat. § 12-285b. To obtain and retain a license, a manufacturer must pay an annual fee and either (a) be a participant in the Master Settlement Agreement ("MSA") between various tobacco companies and State Attorneys General,[3] or (b) deposit funds annually into an escrow account based on the number of its

[2] GRE inadvertently omitted attaching the exhibits to its Second Amended Complaint. In this memorandum, GRE will cite to exhibits as attached to the First Amended Complaint, which are the same exhibits for the Second Amended Complaint. *See* ECF Nos. 38-1 through 38-4.

[3] The four major tobacco companies in the United States and the Attorneys General of 46 States, including Connecticut, entered into the MSA in 1998. SAC ¶ 15. The enabling legislation to implement the MSA imposes certain requirements on all cigarette manufacturers and grants the Commissioner regulatory authority over said manufacturers.

cigarettes that are sold in Connecticut. Conn. Gen. Stat. § 12-285b; SAC ¶¶ 18–19. Each year, a manufacturer also must certify that it is either a participant in the MSA, or that it is in compliance with its escrow deposit and other obligations set forth in Conn. Gen. Stat. §§ 4-28h to 4-28r. Conn. Gen. Stat. §§ 12-285b(b), 4-28*l*; SAC ¶¶ 18–19. GRE does not participate in the MSA (and is thus referred to as a "Nonparticipating Manufacturer," or "NPM"), and has made all required escrow deposits, totaling hundreds of thousands of dollars over the last four years. SAC ¶¶ 16, 32.

Also, before cigarettes may be sold in Connecticut, a manufacturer's brands must be listed on the Directory. The Connecticut General Assembly, through § 4-28m(a), directed the Commissioner to develop by July 1, 2005 a directory of all tobacco product manufacturers and their brands approved for sale in Connecticut. The statute directs the Commissioner to include all manufacturers that properly certified that they participate in the MSA or have satisfied their escrow obligations. SAC ¶ 20. Initially, the statute also directed the Commissioner not to include any brand of an NPM that either failed to satisfy its escrow deposit obligations, or had an outstanding judgment against it for failure to comply with those obligations. Conn. Gen. Stat. § 4-28m(a)(3) rev. to 2005; SAC ¶ 21. GRE's Seneca®, Opal®, and Couture® brand cigarettes have been listed on the Directory for the past four years. SAC ¶¶ 9, 11, 32.

Effective January 1, 2015, however, the General Assembly amended § 4-28m to add a new condition for an NPM to be listed on the Directory. This provision, set forth in § 4-28m(a)(3)(C), prohibited the Commissioner from including or retaining in the Directory "any brand family of a nonparticipating manufacturer if the commissioner concludes . . . (C) a nonparticipating manufacturer's total nation-wide reported sales of cigarettes on which federal excise tax is paid exceeds the sum of (i) its nation-wide reports under [the PACT Act], as from

time to time amended, or those made by its importer, and (ii) any intrastate sales reports under [the PACT Act], as from time to time amended, by more than five per cent of its total nation-wide sales or one million cigarettes, whichever is less, during any calendar year, unless the nonparticipating manufacturer cures or satisfactorily explains the discrepancy not later than ten days after receiving notice of the discrepancy." SAC ¶ 22. In other words, § 4-28m(a)(3)(C) required NPMs to reconcile on a nationwide basis the number of cigarettes reported for excise tax purposes, *i.e.*, all cigarettes manufactured or imported in a given year, against the number of cigarettes reported for PACT Act purposes, *i.e.*, some, but not necessarily all, cigarettes shipped or sold in the same year. SAC ¶ 24.

Effective October 1, 2017, the General Assembly amended the reconciliation provision. Specifically, § 4-28m(a)(3)(C) now prohibits the Commissioner from including or retaining in the Directory "any brand family of a nonparticipating manufacturer if the commissioner concludes . . . (C) a nonparticipating manufacturer's total nation-wide reported sales of cigarettes on which federal excise tax is paid exceeds the sum of (i) its total interstate sales, as reported under [the PACT Act], as from time to time amended, or those made by its importer, and (ii) its total intrastate sales, by more than two and one-half per cent of its total nation-wide sales during any calendar year, unless the nonparticipating manufacturer cures or satisfactorily explains the discrepancy not later than ten days after receiving notice of the discrepancy." As explained herein, amending the statute to omit reference to the PACT Act does not save the statute. The amended § 4-28m(a)(3)(C) maintains the requirement that GRE, as an NPM, must reconcile the interstate sales of cigarettes reported for excise tax purposes against the total intrastate sales that can only be tabulated through the PACT Act reports.

IV. The Attempt to Revoke GRE's Right to Sell Cigarettes in Connecticut

In April 2016, GRE submitted to the Commissioner its annual certification indicating its compliance with its statutory obligations. SAC ¶ 33. Regarding § 4-28m(a)(3)(C), GRE explained that it compared the number of cigarettes sold in Connecticut for which escrow taxes were paid with the number of cigarettes shipped into Connecticut as reported on the PACT Act reports from its regional importer and that the totals were consistent. On June 16, 2016, the Commissioner requested additional documents and information from GRE, including GRE's "total nationwide cigarette sales and . . . [GRE's] [i]mporter's [Alcohol Tobacco Tax and Trade Bureau ("TTB")] Form 5220.6" reports, "an explanation of how compliance with Conn. Gen. Stat. § 4-28m(a)(3)(C) was verified through [its] records or those of its importers and [an enumeration of the] total national cigarette sales reported on PACT Act reports or those of its [i]mporters." SAC ¶ 34; ECF No. 38, Ex. A (e-mail chain between Ms. Bacon and GRE dated June 16, 2016) (hereinafter "Ex. A"). The Commissioner also notified GRE that "[f]ailure to provide the required documents could result in exclusion from Connecticut's Tobacco Directory, effective July 1, 2016." *Id.*

On June 21, 2016, GRE responded to the Commissioner's request. GRE provided all TTB Forms 5220.6 and PACT Act reports from the importers that file such reports. SAC ¶ 35; Ex. B. GRE also explained that it was impossible to reconcile the number of cigarettes reported for excise tax purposes with the number reported for PACT Act purposes because two of its importers distribute cigarettes entirely within Indian Country and are not required to file PACT Act reports at all, and other of its importers distribute a portion of their cigarettes in intrastate shipments for which they are not required to file PACT Act reports. SAC ¶¶ 37–39; Ex. B. GRE also noted that, pursuant to § 4-28m(a)(3)(C), the Commissioner could not remove GRE

from the Directory because it had "satisfactorily explain[ed]" the discrepancy between its excise tax forms and PACT Act reports. SAC ¶ 41; Ex. B.

Nevertheless, the Commissioner refused to accept GRE's explanation. The Commissioner threatened to remove GRE from the Directory effective July 1, 2016, and initially took the position that GRE was not entitled to a hearing or any other form of due process. SAC ¶¶ 42, 44. On June 29, 2016, GRE filed a Verified Complaint against the Commissioner, alleging that §4-28m(a)(3)(C) and the Commissioner's application of it to GRE violated substantive due process, the Supremacy Clause, and the Commerce Clause. SAC ¶ 43; ECF No. 1. On the same day, GRE field a Motion for Temporary Restraining Order ("TRO"), asking the Court to order the Commissioner to refrain from removing GRE from the Tobacco Directory. ECF No. 3. On July 1, 2016, the Court granted GRE's TRO.

On July 6, 2016, after the Court ordered the Commissioner to refrain from removing GRE from the Directory, the Commissioner notified GRE that it would not include GRE on the Tobacco Directory. SAC ¶ 46; ECF No. 38, Ex. C (letter from Marc Papandrea, Tax Unit Manager at DRS, to Mr. Violi, dated July 6, 2016) (hereinafter "Ex. C"). The Commissioner rejected GRE's explanation for the discrepancy because "the fact that [GRE] chooses to do business with importers who do not file PACT Act forms does not excuse [GRE] from complying with Connecticut law." Ex. C. The Commissioner suggested that GRE either "utilize other importers or . . . require its importers to submit to DRS the documentary equivalent of PACT Act reports." SAC ¶ 48; Ex. C. On September 1, 2016, pursuant to the Commissioner's letter and Conn. Gen. Stat. §§ 4-28m(e) and 12-311, GRE submitted a letter protesting the Commissioner's decision and requesting a hearing. SAC ¶ 53; ECF No. 38, Ex. D (letter from counsel for GRE to Mr. Papandrea, dated Sept. 1, 2016).

On June 23, 2017, the Court denied the Commissioner's Motion to Dismiss. ECF No. 65. With the Commissioner's consent and the Courts' permission, on September 5, 2017, GRE filed its Second Amended Complaint. ECF No. 74. As explained in GRE's motion for leave to file the SAC, the amendments to the complaint were intended to plead additional facts that had occurred since the filing of the First Amended Complaint, including the General Assembly's amendment of the statute at issue. On November 9, 2017, GRE learned that, at least for the coming year, it would be listed in the Directory. ECF No. 82, Ex. A. On November 17, 2017, the Commissioner filed his Second Motion to Dismiss ("2d Mot. Dismiss"). ECF No. 82.

LEGAL STANDARD

A complaint must contain "a short and plain statement of the claim showing that the pleader is entitled to relief." Fed. R. Civ. P. 8(a). "To survive a motion to dismiss, a complaint must contain sufficient factual matter, accepted as true, to 'state a claim to relief that is plausible on its face.'" *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009) (quoting *Bell Atlantic v. Twombley*, 550 U.S. 544 (2007)). In ruling on a motion to dismiss, however, "the duty of a court is merely to assess the legal feasibility of the complaint, not to assay the weight of the evidence which might be offered in support thereof." *DiFolco v. MSNBC Cable L.L.C.*, 622 F.3d 104, 113 (2d Cir. 2010) (internal quotation marks omitted). Thus, "[t]he plausibility standard is not akin to a probability requirement," and "[a] well-pleaded complaint may proceed even if it strikes a savvy judge that actual proof of the facts alleged is improbable, and that a recovery is very remote and unlikely." *Nielsen v. Rabin*, 746 F.3d 58, 62 (2d Cir. 2014) (citations and internal quotation marks omitted). In addition, "[a]lthough a court considering a motion to dismiss for failure to state a claim is limited to the facts stated in the complaint, the complaint includes any written instrument attached to it as an exhibit and any statements or documents incorporated into it by reference." *Paulemon v. Tobin*, 30 F.3d 307, 308–09 (2d Cir. 1994).

ARGUMENT

I. GRE Has Standing.

To have standing, a plaintiff must satisfy three elements: "(1) suffered an injury in fact, (2) that is fairly traceable to the challenged conduct of the defendant, and (3) that is likely to be redressed by a favorable judicial decision." *Spokeo, Inc. v. Robins*, 136 S. Ct. 1540, 1547 (2016) (quoting *Lujan v. Defs. of Wildlife*, 504 U.S. 555, 560 (1992)). The three elements "must be supported . . . with the manner and degree of evidence required at the successive stages of the litigation," and at the pleading stage, "general factual allegations of injury resulting from the defendant's conduct may suffice." *Lujan*, 504 U.S. at 561.

When a defendant makes only a "facial" challenge to standing, the plaintiff bears no evidentiary burden at the pleading stage. *Carter v. HealthPort Techs., LLC*, 822 F.3d 47, 56 (2d Cir. 2016) ("When the Rule 12(b)(1) motion is facial, *i.e.*, based solely on the allegations of the complaint or the complaint and exhibits attached to it . . . the plaintiff has no evidentiary burden."). Furthermore, under a "facial" challenge, district courts must draw all reasonable inferences in the plaintiff's favor and are to "presum[e] that general allegations embrace those specific facts that are necessary to support the claim." *Lujan*, 504 U.S. at 561. Thus, the Court's task with respect to analyzing GRE's standing is to ascertain whether GRE's pleadings allege facts that "affirmatively and plausibly suggest that [GRE] has standing to sue." *Carter*, 822 F.3d at 56 (citations and internal quotation marks omitted).

With respect to the injury-in-fact requirement, the Second Circuit has repeatedly characterized that requirement as a "low threshold." *WC Capital Mgmt., LLC v. UBS Sec., LLC*, 711 F.3d 322, 329 (2d Cir. 2013) (citation omitted). To be sure, the injury must be "concrete and particularized" and "actual or imminent, not conjectural or hypothetical." *Lujan*, 504 U.S. at 560 (internal quotation marks omitted). Nonetheless, an allegation of future injury may suffice if the

threatened injury is "certainly impending," or there is a "substantial risk that the harm will occur." *See Clapper v. Amnesty Int'l USA*, 568 U.S. 398, 414 n.5 (2013).

GRE challenges the statute and the Commissioner and DRS's unconstitutional interpretation of the statute. Specifically, GRE alleges that GRE's property interest in remaining on the Directory and due process rights are conditioned on GRE undertaking certain actions that the Constitution prohibits the Commissioner from demanding of GRE as a condition of maintaining those property rights. GRE also alleges that the Commissioner's interpretation of the statute penalizes GRE if it cannot reconcile two sets of federal reports that are not meant to be reconciled. In doing so, the Commissioner violates GRE's due process rights. These allegations are supported by well-pled factual allegations. *See* SAC ¶¶ 9, 32–39, 41, 50, 58–60. Thus GRE's general factual allegations of injury resulting from the statute and the Commissioner's interpretation of the statute suffice to support the existence of standing. *See Lerman v. Bd. of Elections in City of New York*, 232 F.3d 135, 142 (2d Cir. 2000). At the motion to dismiss stage, the Court is to "presume that general allegations embrace those specific facts that are necessary to support the claim [of standing]." *Id.* (internal quotation marks omitted).

Moreover, the Supreme Court has recognized that economic interests are legally protected interests. *E.g.*, *Clinton v. City of New York*, 524 U.S. 417, 432 (1998). What follows from this recognition is the well-established proposition that economic injury constitutes a particularized and concrete injury-in-fact. *E.g.*, *Carter*, 822 F.3d at 55 ("Any monetary loss suffered by the plaintiff satisfies this element; [e]ven a small financial loss suffices.") (internal quotation marks omitted)). Thus, a plaintiff's general factual allegations of economic injury, which are concrete and particularized, resulting from the defendant's conduct suffices for the purposes of meeting the injury-in-fact requirement.

GRE pleads general factual allegations of concrete, particularized economic injury resulting from the unconstitutional enforcement of the statute. Specifically, GRE expended substantial costs in complying with the Commissioner's demands, which are based on an unconstitutional interpretation of the statue. SAC ¶¶ 9, 32. This form of economic injury—the expenditure of money—meets the low threshold required to meet the injury-in-fact element. *See Vill. of Arlington Heights v. Metro. Hous. Dev. Corp.*, 429 U.S. 252, 262 (1977) (identifying the expenditure of "thousands of dollars" on the plans to support petition for rezoning as valid economic injuries supporting standing); *Anderson Grp., LLC v. City of Saratoga Springs*, 805 F.3d 34, 46 (2d Cir. 2015) (plaintiff's "actual expenditures" used to develop residential project proposal was concrete and particularized economic injury for standing purposes). In addition, banning GRE's products from the Connecticut market under the ostensible authority of the statute at issue demonstrates concrete, particularized economic injury of the highest order. Therefore, GRE sufficiently pleads an economic injury to meet the injury-in-fact requirement.

Also, GRE sufficiently alleges future injury. Although the Commissioner focuses his argument on the potential outcome of future certifications, GRE's future injury are the continued expenditure of money to satisfy the unconstitutional interpretation of the statute. The economic injury, *i.e.*, expending a significant amount of money, in complying with the unconstitutional statute are "certainly impending." *Clapper*, 568 U.S. at 414 n.5. GRE has to submit its certification on a yearly basis. *See* SAC ¶¶ 33, 55.[4] Accordingly, GRE has standing.

[4] Although not addressed—much less challenged—by the Commissioner, GRE satisfies the remaining elements to achieve standing. GRE's economic injury is traceable to the Commissioner's interpretation of § 4-28m(a)(3)(C). *See* SAC ¶¶ 9, 32–36, 55–57. Moreover, a favorable judicial decision, *e.g.*, a declaratory judgment that removal of GRE from the Connecticut Tobacco Directory for alleged non-compliance with § 4-28(a)(3)(C) violates and is barred by either or all of the Due Process Clause, Supremacy Clause, and Commerce Clause, would redress the injury that GRE has suffered.

II. GRE Alleges Sufficient Facts to Support a Claim that § 4-28m(a)(3)(C) Violates Substantive Due Process.

A. GRE has a Constitutionally-Protected Property Interest in Remaining on the Directory.

To state a substantive due process claim under prevailing Second Circuit precedent, a plaintiff must allege that a government action deprived him of a constitutionally-protected property or liberty interest.[5] *See McCaul v. Ardlesy Union Free Sch. Dist.*, 514 F. App'x 1, 3 (2d Cir. 2013); *Mordukhaev v. Daus*, 457 F. App'x. 16, 18 (2d Cir. 2012). A person has a constitutionally-protected property interest in a license or other governmental benefit if he has "a legitimate claim of entitlement to it." *Mordukhaev*, 457 F. App'x. at 19 (quoting *Town of Castle Rock v. Gonzales*, 545 U.S. 748, 756 (2005)). In the context of an application for a license, whether a person has a "legitimate claim of entitlement" depends on the degree of discretion that state law affords the licensing authority. State law gives rise to a constitutionally-protected interest in a license "when the discretion of the issuing agency is so narrowly circumscribed that approval of a proper application is virtually assured." *RRI Realty Corp. v. Inc. Vill. of Southampton*, 870 F.2d 911, 918 (2d Cir. 1989).

In addition, "once the government has granted a business license to an individual, the government cannot 'depriv[e] [the individual of] such an interest . . . without [due process].'"

[5] The Second Circuit has noted that applicants for "licenses required for pursuing a particular occupation" have a "liberty interest in earning a livelihood and are normally not required to show an entitlement to the license they seek in order to state a claim" because "their liberty interest is impaired if their license application is arbitrarily denied." *RRI Realty Corp. v. Inc. Vill. of Southhampton*, 870 F.2d 911, 917 n.4 (2d Cir. 1989). Although some District Courts in the Second Circuit have analyzed substantive due process claims of license applicants without addressing whether the applicants had a protected interest, *e.g.*, *Vizio, Inc. v. Klee*, No. 3:15-CV-00929, 2016 WL 1305116, at *23–28 (D. Conn. Mar. 31, 2016); *Karan v. Adams*, 807 F. Supp. 900, 907–08 (D. Conn. 1992), Second Circuit decisions after *RRI Realty* have said that such an interest is an element of a substantive due process claim. *See McCaul v. Ardsley Union Free Sch. Dist.*, 514 F. App'x 1, 3 (2d Cir. 2013); *Mordukhaev v. Daus*, 457 F. App'x 16, 18 (2d Cir. 2012). GRE sufficiently alleges that it has a constitutionally-protected property interest in remaining on the Directory.

Spinelli v. City of New York, 579 F.3d 160, 169 (2d Cir. 2009) (citation omitted). Thus, when state law provides that a license is subject to renewal and may only be revoked under specific circumstances, a license-holder has a due process interest in retaining her license. *See Jones-Soderman v. Exec. Sec'y of the State Bd. for Psychology of the State Educ. Dep't of the Univ. of the State of N.Y.*, No. 08 CV 4716, 2010 WL 3800908, at *6 (E.D.N.Y. May 21, 2010) ("Where state-issued licenses are subject to renewal according to state regulations and are subject to revocation only for a showing of misconduct, the licensee may have a property interest in the license that requires the protections of the Due Process Clause.").

GRE has a constitutionally-protected interest in retaining its right to have its cigarettes sold in Connecticut and remaining on the State's approved list of tobacco manufacturers and brands. SAC ¶¶ 9, 20, 32. First, the Commissioner is required to issue a manufacturer's license to any manufacturer that meets the statutory requirements and may only revoke that license for failure to comply with applicable laws and regulations. Conn. Gen. Stat. §§ 12-285b, 12-295. GRE alleges, and the Commissioner agrees, that GRE has complied with the statutory requirements and holds a current manufacturer's license. SAC ¶ 9.

Second, GRE is currently listed on the Tobacco Directory and has a right to remain on the Directory unless it fails to comply with specific statutory criteria. Contrary to the Commissioner's contention, GRE does not apply to be listed on the Directory every year. Rather, as GRE alleges and the language of § 4-28m(a)(1) confirms, the Commissioner developed the one and only Directory in 2005. SAC ¶ 20. Nowhere in the statute does it provide that the Commissioner is to publish a *new* list every year. To be sure, the statute directs the Commissioner to "*update* the directory *as necessary* . . . to add or remove a tobacco product manufacturer or brand family to keep the directory current," § 4-28m(a)(1) (emphasis added),

but this directive requires the Commissioner to monitor and update the Directory on an ongoing basis, not to conduct an annual process to publish a new list each year.[6]

Moreover, § 4-28m sets forth in precise terms the requirements for a manufacturer to be listed on the Directory and does not afford the Commissioner discretion to deviate from those requirements. *See* Conn. Gen. Stat. § 4-28m(a)(1) ("[T]he commissioner *shall* develop . . . a directory listing of *all* tobacco product manufacturers that have provided current and accurate certifications conforming to the requirements of section 4-28*l* and *all* brand families that are listed in such certifications," and "*shall* update the directory as necessary in order to correct mistakes and to add or remove a tobacco product manufacturer or brand family to keep the directory current and in conformity with the requirements of sections 4-28k to 4-28r, inclusive.") (emphasis added); Conn. Gen. Stat. § 4-28m(a)(2), (3) ("The commissioner *shall not* include or retain in such directory" manufacturers or brand families that fail to comply with the statutory prerequisites) (emphasis added). This language gives the Commissioner no discretion in deciding which manufacturers to add or remove from the Directory. Instead, the Commissioner's task simple: follow the legislature's instructions to list all manufacturers that comply with the statutory requirements.

Because GRE has constitutional rights protecting commerce in its products with and to Connecticut and additional constitutional rights preventing Connecticut from regulating GRE without due process, GRE has a due process interest in remaining on the Directory (the Directory is the regulatory vehicle through which Connecticut bans commerce in GRE's products in Connecticut). The Commissioner's contention that GRE does not have such an interest because

[6] Whether the Commissioner or DRS perform a *de novo* review after the deadline to submit certification documents is irrelevant. 2d Mot. Dismiss at 10. Nothing in the statute establishes this requirement. Rather, as GRE alleges, the Commissioner's role is to "update as necessary," not to undertake a *de novo* review.

it must satisfy the certification requirements on an annual basis misreads § 4-28m and, in any event, is beside the point. The ultimate inquiry in determining whether a business has a due process interest in a license "turns on whether the issuing authority lacks discretion to deny [the benefit], i.e., is required to issue it upon ascertainment that certain objectively ascertainable criteria have been met." *Mordukhaev*, 457 F. App'x. at 19 (quoting *Natale v. Town of Ridgefield*, 170 F.3d 258, 263 (2d Cir. 1999)). For this reason, the Commissioner is incorrect when he argues that the decision to retain a manufacturer in the Directory "rests within [his] discretion." 2d Mot. Dismiss at 10.

In all of the cases cited by the Commissioner in support of his position, the law or regulation at issue plainly granted the licensing official or agency significant discretion to grant or deny a license application. 2d Mot. Dismiss at 9–11.[7] These cases did not involve application of criteria that violated federal law or the Constitution, nor the unconstitutional application of that criteria. As explained previously, § 4-28m sets forth in detail the requirements for a manufacturer to be listed on the Directory and requires the Commissioner to include a manufacturer that meets the statutory prerequisites. The Commissioner has no discretion to include a manufacturer that does not satisfy the requirements, nor to exclude or remove a

[7] The cases relied on by the Commissioner all emphasized the considerable discretion vested in the licensing authority. *E.g.*, *Harlen Assocs. v. Inc. Vill. of Mineola*, 273 F.3d 494, 503–05 (2d Cir. 2001) (no property interest in special use permit because local law "vests considerable discretion in the [Zoning] Board with respect to granting special use permits"); *Sanitation & Recycling Indus. Inc. v. City of New York*, 107 F.3d 985, 995 (2d Cir. 1997) (no property interest where official "vested with broad discretion to grant or deny a license application"); *Karout v. McBride*, No. 11-cv-1148, 2012 WL 4344314, at *7 (D. Conn. Sept. 21, 2012) (no property interest in special exception permit because zoning board had discretion to deny application "on general considerations such as public health, safety and welfare, which are enumerated in zoning regulations") (citation and internal quotation marks omitted); *Ace Partners, LLC v. Town of E. Hartford*, No. 09-CV-1282, 2011 WL 4572109, at *3 (D. Conn. Sept. 30, 2011) (no property interest in pawn broker license because "the level of discretion conferred . . . by the pawnbroker statute precludes a legitimate claim of entitlement").

manufacturer that meets them. Courts in the Second Circuit have found that statutes containing such mandatory language created constitutionally-protected interests. *E.g.*, *Charry v. Hall*, 709 F.2d 139, 144 (2d Cir. 1983) (applicants had protected interest in sitting for psychology licensure examination because state law granted licensing agencies minimal discretion). This case does not involve the application of a regulatory standard that allows the Commissioner discretion to decide or opine whether the granting of a license is "good" or "bad" for the State, such as those regulatory requirements that might allow a regulator to deny a tax license to an applicant that presents a risk of not paying taxes, or might provide land use boards the discretion to determine what is consistent or best for a neighborhood or zoning district.

Similarly, the Commissioner's argument that GRE's substantive due process claim fails because GRE can seek State administrative and judicial review is unconvincing. *See* 2d Mot. Dismiss at 12. The Commissioner relies on *Yale Auto Parts v. Johnson*, 758 F.2d 54 (2d Cir. 1985), for his argument, but that case is readily distinguishable.

Unlike this instant matter, the plaintiffs in *Yale Auto Parts* were not challenging the constitutionality of the statute at issue in that case. Rather, they challenged the defendants' denial of a certificate of location approval sought from the Zoning Board of Appeals. 758 F.2d at 55. Thus the *Yale Auto Parts* plaintiffs, unlike GRE, did not have a license and had no property interest protected by the Due Process Clause. *Id.* at 60. Here, GRE alleges that once it was placed on the Directory, it was conferred a property interest. Furthermore, *Yale Auto Parts* neither considered the issue of a Connecticut statute applying criteria that violates federal law or the Constitution, nor the unconstitutional application of the criteria. Thus, whether administrative and judicial redress is available to GRE is of no moment. GRE is challenging the

constitutionality of the statute and its application. In essence, the entire process—even with access to "[S]tate administrative and judicial fora"—is unconstitutional.

In summary, GRE has a constitutionally-protected property interest in remaining on the Directory. Once listed on the Directory, GRE has a right to be listed because the Commissioner has no discretion to grant a cigarette manufacturer's license and is prohibited from revoking that right unless the manufacturer fails to comply with statutory requirements. *See* SAC ¶¶ 9, 11, 23, 32, 58. Accepting the factual allegations as true, GRE meets the plausibility standard by alleging facts that it has a cognizable property interest in remaining on the Tobacco Directory.

B. GRE Alleges Sufficient Facts to Support a Claim that § 4-28m(a)(3)(C) is Not Rationally Related to a Legitimate State Interest.

The United States and Connecticut Constitutions both prohibit the government from depriving a person of "life, liberty, or property, without due process of law." U.S. Const. amend. XIV, § 1; Conn. Const. art. I, §§ 8, 10. The constitutional guarantees of due process "cover a substantive sphere as well, barring certain government actions regardless of the fairness of the procedures used to implement them." *Vizio, Inc. v. Klee*, No. 3:15-CV-00929, 2016 WL 1305116, at *23 (D. Conn. Mar. 31, 2016) (citation omitted). Under both the United States and Connecticut Constitutions, economic regulation is subject to the rational basis test, which requires that "legislation be supported by a legitimate legislative purpose furthered by a rational means." *Id.* (citation omitted). "A state deprives a candidate for licensure of substantive due process if the state imposes licensure requirements that have no rational connection with the candidate's fitness or capacity to practice in the profession." *Karan v. Adams*, 807 F. Supp. 900, 907 (D. Conn. 1992) (citation omitted).

Although rational basis review is deferential, courts in the Second Circuit, as well as the Supreme Court, have made clear that the test "is not a toothless one" and that a challenged

statute "must rationally advance a reasonable and identifiable governmental objective." *N.Y. State Motor Truck Ass'n v. Pataki*, No. 03 CV 2386, 2004 WL 2937803, at *10 (S.D.N.Y. Dec. 17, 2004); *accord Romer v. Evans*, 517 U.S. 620, 632 (1996) (under rational basis test, "[courts] insist on knowing the relation between the classification adopted and the object to be attained"); *Barletta v. Rilling*, 973 F. Supp. 2d 132, 136 (D. Conn. 2013) ("[R]ational basis review must mean something beyond absolute deference to the legislature; otherwise it is not review at all."). A statute fails the rational basis test when its "relationship to an asserted goal is so attenuated as to render [the statute] arbitrary and irrational." *Barletta*, 973 F. Supp. 2d at 136 (citation and internal quotation marks omitted).

The reconciliation requirement in § 4-28m(a)(3)(C) has no rational relationship with a legitimate State interest. The Commissioner contends that the purpose of the provision is to ensure that certain cigarettes of manufacturers licensed to sell their products in Connecticut are not being diverted into the illicit market, with the ultimate goal being to "reduce state tax evasion[,] increase compliance with the State's escrow statute . . . and protect Connecticut residents from the many adverse public health effects [caused by the availability of] artificially underpriced[] cigarettes." 2d Mot. Dismiss at 14. Irrespective of whether these are legitimate interest, § 4-28m(a)(3)(C) is an irrational and arbitrary means of effecting these interests because the inability to reconcile the numbers in question is a result of the requirements of federal law and has no bearing on whether the manufacturer's cigarettes were diverted to the illicit market.

Indeed, the fact that the legislation is only applicable to some, but not the majority of, manufacturers whose cigarettes are sold in Connecticut, defeats the State's claims. If tax evasion and artificial pricing were legitimate State concerns, then the new legislation would apply to all manufacturers, not just those that have not joined the MSA. If compliance with the State's

escrow laws is the State's interests, then reconciliation of the sales in Connecticut and the escrow paid for those sales would be the means to the furthering that interest—a reconciliation that GRE has demonstrated to the penny and the very last cigarette sold in Connecticut. Requiring GRE, then, to prove that the exact number of cigarettes that its importers have imported throughout the United States (based on federal excise tax returns) matches the number of cigarettes those importers reported, in effect, on their federal PACT Act reports through the United States (within two and one-half percent) is irrational, impossible (as a matter of law) and a completely arbitrary means of promotion GRE's compliance with its escrow obligations in Connecticut. There is no connection between what the Commissioner is requiring GRE to reconcile and GRE's compliance with its escrow obligations in Connecticut. Consequently, the Commissioner's motion fails completely to demonstrate such a connection.

Section 4-28m(a)(3)(C) requires certain cigarette manufacturers—those who have not joined the MSA—each year to reconcile, within two and one-half percent, "the total nation-wide reported sales of cigarettes on which federal excise tax is paid" and the total number of cigarettes reported, in effect, on the manufacturers or its importer's PACT Act forms. Excise taxes are paid on *all* cigarettes "manufactured in or imported into the United States." 26 U.S.C. § 5701(b). The PACT Act requires reporting of only interstate cigarette sales. 15 U.S.C. § 376(a)(2). The necessary assumptions underlying § 4-28m(a)(3)(C) are that all of the cigarettes manufactured or imported by a manufacturer in a given year should also be shipped and sold in a covered shipment for PACT Act purposes in the same year and that any difference between the two numbers somehow adversely affects the State. These assumptions are belied by both the PACT Act and basic economic realities, rendering the statute arbitrary and irrational.

The excise tax forms of GRE's importers account for all GRE cigarettes imported into the United States. SAC ¶ 37. The importers' PACT Act forms, however, do not reflect all GRE cigarettes shipped or sold in the United States. SAC ¶ 27. Because the PACT Act only requires reporting of cigarettes shipped in "interstate commerce," certain sales and shipments are exempt from the reporting requirements. Under the PACT Act, "'interstate commerce' means commerce between a State and any place outside the State, commerce between a State and any Indian country in the State, or commerce between points in the same State but through any place outside the State or through any Indian country." Thus, purely intrastate shipments and shipments within Indian Country do not fall within the PACT Act's definition of "interstate commerce." As GRE explained to the Commissioner, well over one million of its cigarettes are sold in intrastate shipments and shipments within Indian Country, and none of those shipments take place in Connecticut. SAC ¶¶ 37–39. Because the PACT Act exempts these shipments from its reach, GRE cannot reconcile the number of cigarettes reported on its importers' excise tax forms with the number reported on their PACT Act forms as required by § 4-28m(a)(3)(C). SAC ¶¶ 37–39, 50. It is arbitrary and irrational to condition the right of cigarette manufacturers to sell or have their products sold in Connecticut on the ability to reconcile two numbers that cannot be reconciled due to the requirements of federal law, especially given that the exempt shipments have no nexus to Connecticut.[8]

Although the Commissioner now says that sales in Indian Country will be exempt from enforcement, he has not explained how this exemption will work under the statutory formula. To

[8] An additional reason why the legislation and the Commissioner's enforcement are preempted and unconstitutional is the PACT Act's express limitation that the information required to be reported under the PACT Act can only be used for the purposes of enforcement of the PACT Act itself, not any other State or federal law, which the Commissioner is purporting to do. *See* 15 U.S.C. § 376(c).

exclude Indian Country sales from the equation, the Commissioner necessarily will need to know how many GRE cigarettes were sold in Indian Country. Thus, it appears that for the Commissioner to "exempt" Indian Country sales from enforcement, GRE will be required to report to the Commissioner the exact information that the Commissioner is purporting to exempt. If true, this is not an exemption at all, but simply a roundabout way of compelling GRE to provide information that the Commissioner appears to concede the State has no authority to require in the first place. In any event, whether the Commissioner will in fact be able to exempt Indian Country sales from enforcement is a factual issue that will need to be vetted in discovery, rendering a motion to dismiss inappropriate. In addition, the Commissioner still maintains that GRE must provide PACT Act reports for wholly intrastate sales, which, as discussed previously, also prevents GRE from complying with the statute because those sales are not required to be reported under the PACT Act.

That the reconciliation requirement is wholly arbitrary is apparent from the Commissioner's explanation of the economic theory behind the formula. He notes that the formula is based on "a form of economic analysis, called trade gap analysis," which "works by comparing the totals of two independent sources of numerical data that are generated at different points in the marketing chain." 1st Mot. Dismiss at 5.[9] According to the Commissioner, "[a]ny difference between the two totals reflects the probable diversion of cigarettes to an illegal market while in transit . . . . " *Id.* The report cited by the Commissioner in support of this theory, however, makes plain that this formula relies on the underlying assumption that, absent diversion to the illegal market, the data points to be compared should be identical. Specifically, the report

[9] In his second Motion to Dismiss, ECF No. 82, the Commissioner stated that his "explanation of the applicable statutory framework" was set forth in the Defendant's Memorandum in Support of Motion to Dismiss.

notes that trade gap analysis, which traditionally is used to estimate the size of the global or national illicit market, "compare[s] the total recorded exports and the total recorded imports; the difference reflects diversion to illegal markets while in transit." ECF No. 42, Ex. B, Nat'l Research Council & Inst. of Med., *Understanding the U.S. Illicit Tobacco Market: Characteristics, Policy Context, and Lessons from International Experiences* (2015), at 78 (hereinafter "*Understanding the U.S. Illicit Tobacco Market*"). Comparing exports to imports on a national or global level is a proverbial apples-to-apples comparison because all products that are exported from one place should be imported into another. But Connecticut's use of two data points that are inconsistent due to the requirements of federal law is akin to comparing apples-to-oranges and renders the statute arbitrary and irrational.[10]

It may be reasonable to rely on trade gap analysis to estimate the size of the national or global illegal cigarette trade for purposes of determining whether legislative action is appropriate or effective. Here, however, the state is relying on a fundamentally flawed version of the analysis to deny GRE the right to do business in the State. There simply is no basis to conclude that a discrepancy between the number of cigarettes reported for excise tax purposes and the number reported for PACT Act purposes reflects the "probable diversion of cigarettes to an illegal market."[11] 1st Mot. Dismiss at 5.

[10] In fact, the report cited by the Commissioner concedes that, even with respect to data points that should be identical, "there are almost always other, nonillicit, reasons for different sources to yield different results, and researchers typically have to make assumptions about unknown factors to produce estimates of the size and growth of the illicit market." *Understanding the U.S. Illicit Tobacco Market*, at 78.

[11] Even if the discrepancy suggested that some cigarettes were diverted to the illegal market somewhere in the country—a point that GRE contests—Connecticut only has a legitimate interest in preventing illegal cigarettes sales in Connecticut. As noted previously, GRE submitted documentation to show that there was no discrepancy with respect to Connecticut sales. Ex. B.

Also, the Commissioner is not entitled to dismissal of this action merely by offering a superficially plausible (yet patently flawed) explanation of the relationship between the statutory formula and the State's interest in preventing illegal cigarette sales. Although the rational basis test does not require that the legislature's chosen means be supported by empirical evidence, dismissal of a substantive due process claim is not appropriate where a plaintiff alleges that those means are demonstrably irrational. *E.g., Dias v. City & Cty. of Denver*, 567 F.3d 1169, 1183–84 (10th Cir. 2009) (where plaintiffs alleged that evidence would demonstrate that pit bull ban would not improve public safety, plaintiffs must be afforded opportunity to "marshal enough evidence to prevail on the merits of their claim that the Ordinance is irrational"); *N.Y. State Motor Truck Ass'n*, 2004 WL 2937803, at *10–11 (denying motion to dismiss equal protection claim under rational basis standard where record countered proffered rationales for statute barring transportation of 800 cigarettes or less by any person other than common or contract carrier); *cf. Bass Plating Co. v. Town of Windsor*, 639 F. Supp. 873, 879–80 (D. Conn. 1986) (town's requirement that hydroxide waste contain no more that 70 percent water not reasonably related to interest in preventing waste from entering ground water and insuring that waste could be handled efficiently because evidence established that 50 percent water content was sufficient to accomplish objectives). Because GRE alleges that the PACT Act renders the formula set forth in § 4-28m(a)(3)(C) arbitrary and the explanation proffered by the Commissioner is flatly contradicted by his own sources, the second motion to dismiss must be denied.

To the extent the Commissioner may contend that the provision in § 4-28m(a)(3)(C) allowing manufacturers to "satisfactorily explain[] the discrepancy" cures the arbitrariness of the statutory formula, his interpretation of that provision renders it equally arbitrary. In response to GRE's detailed explanation that it could not reconcile the discrepancy because a significant

number of its cigarettes are sold in transactions not subject to the PACT Act, SAC ¶¶ 35–37; Ex. B, the Commissioner offered GRE the following ultimatum: either use importers who file PACT Act reports for all shipments throughout the country, or require importers to "submit to [the Commissioner] the documentary equivalent of PACT Act reports." SAC ¶ 48; Ex. C. In other words, the Commissioner's view is that GRE can only "satisfactorily explain[] the discrepancy" by (1) refraining from using distributors who sell products in intrastate or Indian Country sales, thus losing out on a sizeable—and entirely legal—segment of the market, or (2) requiring independent third parties over whom GRE exercises no control and with whom GRE has no affiliation to report to the Commissioner details about sales that occur entirely outside of Connecticut. SAC ¶ 41.

This is no fix for a fundamentally flawed and irrational statute. As GRE informed the Commissioner, forty percent of its importers' sales are not subject to the PACT Act reporting requirements, and none of those importers sell cigarettes in Connecticut. SAC ¶ 35; Ex. B. Requiring GRE to either sacrifice a significant number of legal sales or be at the mercy of the internal record-keeping practices of independent, out-of-state third parties who are not subject to regulation in Connecticut is an arbitrary and illegitimate enforcement of State law. GRE's right to have its products sold in Connecticut cannot be conditioned on the conduct of unrelated out-of-state third parties. *Cf. Pilchen v. City of Auburn*, 728 F. Supp. 2d 192, 202 (N.D.N.Y. 2010) (city's refusal to reconnect renter's water until landlord paid water bill violated due process because forcing renter to assume landlord's debt was not rational means of collecting delinquent bill). Thus, the Commissioner's motion to dismiss GRE's due process claim must be denied.

III. Conn. Gen. Stat. § 4-28m(a)(3) Violates the Supremacy Clause Because it Conflicts with the PACT Act.

The Supremacy Clause restricts the power of states to adopt policies that conflict with federal laws. U.S. Const. art. VI, cl. 2. When a federal statute does not contain an express preemption provision, State law nevertheless must yield to federal law if Congress has evinced an intent that federal law is to occupy the field, or if there is an actual conflict between state and federal law. *United States v. Locke*, 529 U.S. 89, 115 (2000). An "actual conflict" between state and federal law occurs when a state law "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress," or when "it is impossible for a private party to comply with both state and federal law." *Id.* at 109.

The reconciliation requirement of § 4-28m(a)(3)(C) is preempted by the PACT Act because it is impossible for GRE to comply with both statutes. *See PLIVA, Inc. v. Mensing*, 564 U.S. 604, 618 (2011) ("We have held that state and federal law conflict where it is impossible for a private party to comply with both state and federal requirements.") (internal quotation marks omitted)). As discussed previously, § 4-28m(a)(3)(C) purports to require cigarette manufacturers to reconcile within two and one-half percent of cigarettes reported for federal excise tax purposes with the number reported, in effect, under the PACT Act. SAC ¶¶ 2–4, 22–24. The PACT Act, on the other hand, makes this reconciliation impossible in certain circumstances because certain sales and shipments of cigarettes are exempt from the reporting requirements. SAC ¶¶ 37–39, 50. It is beyond question that Connecticut has no authority to force GRE or any other manufacturer to comply with a reporting requirement that Congress expressly exempted.

GRE has fully satisfied its national reporting requirements under the PACT Act and that its importers ship in exempted shipments well over the five percent or one million stick allowance, thus making it impossible for GRE to comply with both § 4-28m(a)(3)(C) and the

PACT Act. SAC ¶ 37–39; Ex. B. A motion to dismiss must be denied where a plaintiff alleges sufficient facts to support a finding that it is impossible for it to comply with both state and federal law. *See Bradley v. Fontaine Trailer Co.*, No. 3:06-CV-62, 2009 WL 763548, at *5 (D. Conn. Mar. 20, 2009) (denying motion to strike preemption defense of state law claim that auto accident was caused by defective lighting because "it is possible for defendant to proffer evidence that . . . [it] cannot meet both the federal requirements and remedy whatever defect plaintiffs suggest the tractor trailer had"). Thus, the Commissioner's motion must be denied because GRE is in compliance with its national reporting requirements dictated by Congress, and the state cannot engraft onto the PACT Act additional requirements that Congress expressly excluded from the Act's reach. In addition, the statute at issue requires reconciling using "intrastate sales," which in effect are reported under the PACT Act. The PACT Act, however, only applies in "interstate commerce," which excludes the precise sales §4-28m(a)(3)(C) requires to be reconciled.

Moreover, although courts generally operate under an assumption that State laws relating to a "field which the States have traditionally occupied" are not preempted "unless that was the clear and manifest purpose of Congress," that assumption does not apply where a State regulates in an area not typically within its powers. *Locke*, 529 U.S. at 107–08 (maritime law); *see also New York SMSA Ltd. v. Town of Clarkstown*, 612 F.3d 97, 104 (2d Cir. 2010) (telecommunications); *State Farm Bank, FSB v. Burke*, 445 F. Supp. 207, 216 (D. Conn. 2006) (federal savings banks). A State law that conflicts with a federal one is especially ripe to be struck down on preemption grounds where the State is attempting to regulate conduct at the outer reaches of its powers. *Cf. Locke*, 529 U.S. at 115–16 (State law requiring vessels operating in State waters to report casualties regardless of where they occur preempted by federal law

requiring Coast Guard to prescribe regulations regarding reporting of marine casualties in part because State law "affect[ed] a vessel operator's out-of-state obligations and conduct, where a State's jurisdiction and authority are most in doubt"). Section 4-28m(a)(3)(C) is particularly susceptible to a preemption challenge because it is an attempt to regulate conduct that occurs wholly outside of Connecticut and within Indian Country, both areas that are well beyond the outer reaches of the State's authority. The State's attempt to add to the reporting requirements as dictated by Congress impermissibly increases GRE's burden with respect to conduct that is not within the State's power to regulate.

The Commissioner also continues to rely on 15 U.S.C. § 376a to support his argument that the PACT Act does not preempt State activity. That statute provides that "[w]ith respect to *delivery sales* into a specific State and place, each *delivery seller* shall comply with . . . all state, local, tribal, and other laws generally applicable to sales of cigarettes or smokeless tobacco as if the *delivery sales* occurred entirely within the specific state and place . . . . " 15 U.S.C. § 376a(a)(3) (emphasis added). By its terms, that statute applies only to "delivery sales," which are other-than-in-person sales whereby a seller delivers products directly to the consumer, and only to such sales that are conducted by "delivery sellers," which are persons who make "delivery sales." 15 U.S.C. § 375(5), (6). The reporting statute at issue here is 15 U.S.C. § 376—not § 376**a**—and applies to all sellers of cigarettes and smokeless tobacco. Unlike the "delivery sales" statute, 15 U.S.C. § 376 does not reference any requirement that such sellers comply with State law. Moreover, nowhere else in the PACT Act is there an expression of congressional intent to allow states to regulate commerce occurring wholly in other States. The Commissioner's argument to the contrary is unfounded.

In addition, although the Commissioner is correct in stating that federal courts presume that federal statutes do not preempt State law, *see Bond v. United States*, 134 S. Ct. 2077, 2088 (2014), it is equally true that "[a] failure to provide for preemption expressly may reflect nothing more than the settled character of implied preemption doctrine that courts will dependably apply, and in any event, the existence of conflict cognizable under the Supremacy clause does not depend on express congressional recognition that federal and state law may conflict." *Crosby v. Nat'l Foreign Trade Council*, 530 U.S. 363, 387–88. Therefore, the absence of an express preemption clause in the PACT Act does not defeat GRE's Supremacy Clause claim.

Finally, the Commissioner is incorrect in arguing that preemption is precluded merely because achieving the stated goals of the PACT Act "necessarily requires coordinated efforts by all levels of government." 2d Mot. Dismiss at 19. Although GRE recognizes that the State's goals may be consistent with the policy Congress sought to achieve via the PACT Act, GRE alleges that § 4-28m(a)(3)(C) is not a "coordinated effort" because it conflicts with the federal scheme. As the Supreme Court has recognized, a State law that conflicts with federal law is not sheltered from the Supremacy Clause simply because the State and federal statutes share the same goal. "The fact of a common end hardly neutralizes conflicting means." *Crosby*, 530 U.S. at 379. It is one thing to say that a State may impose more stringent requirements than the federal government with respect to in-state conduct when those requirements do not conflict with a federal statute. *E.g.*, *Wyeth v. Levine*, 555 U.S. 555, 568–69 (2009) (Food and Drug Administration's approval of warning label did not preclude state tort claim based on failure to warn that drug was not safe for use in particular application). It is quite another to say that a State may require out-of-state actors to comply with a federal law when Congress itself has expressly chosen to exempt those same actors from the statute's reach.

IV. Conn. Gen. Stat. § 4-28m(a)(3)(C) is an Extraterritorial Regulation in Violation of the Commerce Clause.

The Commerce Clause provides that "Congress shall have Power . . . [t]o regulate Commerce with foreign Nations and among the several States." U.S. Const. art. I, § 8, cl. 3. In addition to limiting the federal government's authority to regulate intrastate commerce, the Commerce Clause "has long been recognized as a self-executing limitation on the power of the States to enact laws imposing substantial burdens on such commerce." *S.-Cent. Timber Dev., Inc. v. Wunnicke*, 467 U.S. 82, 87 (1984). The Supreme Court has recognized three ways in which a State law may violate the dormant Commerce Clause.

In *Healy v. Beer Inst., Inc.*, 491 U.S. 324, 336 (1989), the Supreme Court explained that "the Commerce Clause . . . precludes the application of a state statute to commerce that takes place wholly outside of the State's borders, whether or not the commerce has effects within the State . . . [In addition, a] statute that directly controls commerce occurring wholly outside the boundaries of a State exceeds the inherent limits of the enacting State's authority and is invalid regardless of whether the statute's extraterritorial reach was intended by the legislature. The critical inquiry is whether the practical effect of the regulation is to control conduct beyond the boundaries of the State." (citation omitted) (internal quotation marks omitted). Pertinent to this case is the prohibition on "extraterritorial" regulation, which forbids Sate laws that regulate conduct outside its borders.

Although *Healy* considered a law controlling prices outside Connecticut, the rule the Court in *Healy* articulated was not limited—as the Commissioner argues—to those circumstances. *See* 2d Mot. Dismiss at 24–25. Instead, the Supreme Court noted that, "at a minimum," its Commerce Clause jurisprudence stood for several "propositions," including the prohibition of a State imposing its law extraterritorially. *Healy*, 491 U.S. at 335 (citing *Edgar v.*

MITE Corp., 457 U.S. 624, 642–43 (1982)). Thus, in relying on *Mite Corp.*, the scope of the *Healy* rule can be placed in proper context.

As explained by the Supreme Court, *Mite Corp.* "significantly illuminates the contours of the constitutional prohibition on extraterritorial legislation." *Id.*, 333 n.9. *Mite Corp.*, unlike *Healy*, was not a price control case. Rather, the court in *Mite Corp.* "struck down the Illinois Business Takeover Act, which required that a takeover offer for a target company having a specified connection to Illinois be registered with the Secretary of State and mandated that such an offer was not to become effective for 20 days, during which time the offer would be subject to administrative evaluation." *Id.* As in *Healy*, *Mite Corp.* scrutinized the practical effects of the Illinois law to conclude that it violated the Commerce Clause. *Mite Corp.*, 457 U.S. at 643. Thus, the Commissioner unnecessarily limits the application of *Healy*.[12]

Moreover, the prohibition on extraterritorial control of commerce is a strict one. A state law that has the "practical effect of regulating commerce that takes place wholly outside of its borders" is "*per se* invalid," regardless of "whether . . . the statute's extraterritorial scope was intended by the lawmakers." *Eric M. Berman, P.C. v. City of New York*, 895 F. Supp. 2d 453, 474, 476–77 (E.D.N.Y. 2012), *vacated in part on other grounds*, 796 F.3d 171 (2d Cir. 2015).

[12] In *Vizio, Inc. v. Klee*, 226 F. Supp. 3d 88 (D. Conn. 2016), the plaintiff was allowed to re-plead its dormant Commerce Clause claim that was based on the extraterritoriality prong. *Id.* at 97. Specifically, the Court permitted the plaintiff to plead that a certain aspect of the challenged statute "operate[d] to directly control the interstate price of [the plaintiff's] televisions." *Id.* In discussing *Healy*, the court determined that the *Healy* "language emphasize[d] that, in order for a statute to actually violate the dormant Commerce Clause under the extraterritoriality theory, it must directly control interstate prices." *Id.* at 100. To the extent that the court in *Vizio* attempted to limit the application of *Healy* purely to cases about price control, GRE contends that this is incorrect. As noted previously, the Supreme Court, through its reliance on *Mite Corp.*, has not limited the *Healy* rule only to those cases. *See Healy*, 491 U.S. at 333 n.9.

In evaluating whether Connecticut's statute runs afoul of the extraterritorial prong of the dormant Commerce Clause, "[t]he critical inquiry is whether the practical effect of the regulation is to control conduct beyond the boundaries of the State." *Healy*, 491 U.S. at 336 (citations and internal quotation marks omitted). Here, GRE alleges sufficient facts to establish that § 4-28m(a)(3)(C) violates the Commerce Clause because the statute has the practical effect to regulate commerce occurring wholly outside of Connecticut. In particular, § 4-28m(a)(3)(C) purports to require manufacturers to reconcile on a "nation-wide" basis the number of cigarettes reported for excise tax purposes and the number of cigarettes reported, in effect, under the PACT Act. The statute does not limit its reach to cigarettes that are imported into, shipped from, or sold in Connecticut, but instead requires manufacturers to report all of its cigarettes sold across the country. In GRE's case, this means that importers of GRE cigarettes that conduct their business entirely outside of Connecticut would be required to report all of their sales of GRE cigarettes to the Commissioner. SAC ¶¶ 38, 39, 40, 50.

Indeed, the Commissioner has confirmed that he interprets the statute to authorize him to engage in extraterritorial regulation. In response to GRE's letter explaining that it was impossible to reconcile the number of cigarettes reported on its importers' excise tax forms with those reported on the importers' PACT Act forms, the Commissioner told GRE that, if it wanted to continue selling cigarettes in Connecticut, its only two options were to use importers that file PACT Act forms for all sales, or to require its importers to report all of their sales to the Commissioner. SAC ¶ 48; Ex. C. Put differently, as the Commissioner interprets § 4-28m(a)(3)(C), GRE can only sell cigarettes in Connecticut if it either refrains from selling them to importers who conduct their business exclusively within the boundaries of another State, or

requires such out-of-state importers to submit to the Commissioner's regulatory authority. This is an impermissible Hobson's choice that the Commerce Clause does not permit.

As an initial matter, Connecticut does not have the authority to prohibit GRE from doing business with companies that conduct their operations entirely outside of Connecticut, which would be the natural result of the Commissioner's first alternative. Because the PACT Act exempts reporting of transactions that occur either wholly intrastate or within Indian Country, the only way to refrain from using importers that do not file PACT Act forms would be to cease doing business with companies that engage in purely intrastate or within Indian Country transactions. This "stop-selling" rationale would render the Commerce Clause meaningless because States could merely interpret statutes to force cigarette manufacturers into a Hobson's choice. The "stop-selling" notion cannot withstand a modicum of scrutiny.

The Commerce Clause flatly prohibits Connecticut from applying a "state statute to commerce that takes place wholly outside of the State's borders," or from "directly control[ling] commerce occurring wholly outsides the boundaries of [the] State." *Healy*, 491 U.S. at 336. "Quite simply, if [a] transaction is consummated out of state, a state may not regulate it without violating the dormant Commerce Clause." *Eric M. Berman, P.C.*, 895 F. Supp. 2d at 483. Therefore, the Commissioner's first alternative is not just an attempt to regulate out-of-state commerce; it is an attempt to prohibit it. Put simply, the Commissioner cannot condition GRE's right have its products sold in Connecticut on a requirement that is cease doing business elsewhere or with other companies that do business elsewhere completely within the law of those other States and federal law.

The Commissioner's second alternative is equally offensive to the Commerce Clause because it would require out-of-state companies to submit to Connecticut's regulatory authority

by reporting their sales to the Commissioner. Courts in the Second Circuit have struck down on Commerce Clause grounds similar attempts to impose reporting requirements on out-of-state businesses. In *Motor Vehicle Mfrs. Ass'n of U.S., Inc. v. Abrams*, 720 F. Supp. 284 (S.D.N.Y. 1989), the court addressed a Commerce Clause challenge to various provisions of New York's Lemon Law statute. Of particular relevance to this case was a provision that required auto dealers that received notice of a warranty-covered defect to report that defect to manufacturers within seven days. *Id.* at 287–88. The Attorney General of New York interpreted the provision to apply to out-of-state auto dealers dealing with customers from New York. *Id.* at 288. The court struck down this provision as an extraterritorial regulation because "[i]nnocuous as it [was], this requirement nonetheless ha[d] the effect of 'regulat[ing] commerce in other States,' *Brown-Forman* [*Distillers Corp. v. New York State Liquor Auth.*], 476 U.S. [573,] 580, 106 S. Ct. [2080,] 2085, [1986], in violation of the Commerce Clause." *Id.* The court further noted that the dealers' contractual relationship with the manufacturers requiring them to provide warranty service was "of no moment" and that New York's attempt to regulate out-of-state dealers was "per se in violation of the Commerce Clause." *Id.*

The Commissioner's attempt to require out-of-state businesses to report their sales to Connecticut is even more egregious than the New York law struck down in *Abrams*. The practical effect of the Commissioner's reporting requirement pursuant to § 4-28m(a)(3)(C) that is levied on out-of-sate businesses is to control conduct outside the boundaries of Connecticut. *See MITE Corp.*, 457 U.S. at 643 (1982) ("The limits on a State's power to enact substantive legislation are similar to the limits on the jurisdiction of state courts. In either case, 'any attempt directly to assert extraterritorial jurisdiction over persons or property would offend sister States and exceed the inherent limits of the State's power.'") (quotation omitted)). Unlike *Abrams*, in

which the New York Attorney General's interpretation at least limited the statute's application to auto dealers doing business with people from New York, the Commissioner is attempting to regulate companies that have no connection to Connecticut. This is an impermissible extraterritorial regulation under the Commerce Clause. It is also irrelevant to the analysis that GRE conducts other, unrelated business in Connecticut because "the in-state presence of one party to the transaction cannot be used as justification to regulate the other party." *Eric M. Berman, P.C.*, 895 F. Supp. 2d at 483 (New York City law regulating debt collection agencies, defined to include buyers of debt who collect debt in NYC directly or through services of another, would violate Commerce Clause as applied to out-of-state debt buyers who do not directly engage in in-state collection activities and whose contracts with third-party collectors were consummated out-of-state).

It is also no answer to say that the statute puts the onus on GRE, as opposed to the out-of-state importers, because the information that the Commissioner seeks relates to transactions that occur wholly outside of Connecticut and have no nexus with the State. SAC ¶¶ 38, 39, 41, 50. Connecticut cannot assert itself as a regulator of the cigarette industry across the country. Other States are free to require—or not to require—manufacturers and distributors to track and report the number of cigarettes sold in their own States. Connecticut has no authority to override those decisions merely because it has made a different policy choice. Based on the allegations in the SAC and adhering to *Healy*'s standard that the "critical inquiry is whether the practical effect of the regulation is to control conduct beyond the boundaries of the State," 491 U.S. at 336, the Commissioner's application of § 4-28m(a)(3)(C) is a naked attempt to "regulate commerce that takes place wholly outside of [Connecticut]'s borders" in violation of the Commerce Clause. *Mite Corp.*, 457 U.S. at 642–43.

V. GRE States a Claim for a Declaratory Judgment that It has Complied with § 4-28m(a)(3)(C).

In Count Four of the Complaint, GRE seeks a declaratory judgment that it has complied with § 4-28m(a)(3)(C) because, if the statute is not struck in its entirety, GRE's explanation regarding the "discrepancy" between the number of cigarettes reported for federal excise tax purposes and the number reported for PACT Act purposes must be deemed "satisfactory" as a matter of federal law. The Commissioner moves to dismiss this claim because GRE received confirmation of its compliance for the 2016–2017 certification year and the 2017–2018 certification year. 2d Mot. Dismiss at 26.

Despite having been granted confirmation of its compliance, it does not render GRE's claim seeking declaratory judgment moot because the offensive conduct is "capable of repetition, yet evading review." *See Murphy v. Hunt*, 455 U.S. 478, 482 (1982) (per curiam) (citation and internal quotation marks omitted). This court may exercise jurisdiction over this action if "'(1) the challenged action [is] in its duration too short to be fully litigated prior to its cessation or expiration, and (2) there [is] a reasonable expectation that the same complaining party would be subjected to the same action again.'" *Id.* (quoting *Weinstein v. Bradford*, 423 U.S. 147, 149 (1975) (per curiam)). Here, the challenge to the Commissioner's unconstitutional interpretation of § 4-28m(a)(3)(C) is too short to be fully litigated before GRE is force to submit to another round of annual certification. Also, there is little doubt that the GRE would be subjected to the same action by the same Defendant. Nonetheless, this Court can avoid striking down the statute by declaring that GRE's explanation is sufficient as a matter of law.

CONCLUSION

For the foregoing reasons, GRE respectfully requests that the Court deny the Commissioner's Motion to Dismiss the Second Amended Complaint.

PLAINTIFF,
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CERTIFICATION

I hereby certify that on this 21st day of December, 2017, the foregoing was filed electronically and served by mail on anyone unable to accept electronic filing. Notice of this filing will be sent by e-mail to all parties by operation of the Court's electronic filing system. Parties may access this filing through the Court's CM/ECF system.

/s/ Rosendo Garza, Jr.
Rosendo Garza, Jr. (ct30053)