

# 17-1993(L)

17-2107, 17-2111 (XAP)

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## United States Court of Appeals for the Second Circuit

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THE STATE OF NEW YORK, THE CITY OF NEW YORK,

*Plaintiffs–Appellees–Cross-Appellants,*

v.

UNITED PARCEL SERVICE, INC.,

*Defendant–Appellant–Cross-Appellee.*

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On Appeal from the United States District Court  
for the Southern District of New York

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### REPLY BRIEF FOR PLAINTIFFS–APPELLEES–CROSS-APPELLANTS

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## PRELIMINARY STATEMENT

The response of defendant United Parcel Service (UPS) to plaintiffs' cross-appeal on compensatory damages attacks a straw man in arguing that plaintiffs seek to eliminate any causation requirement under the Contraband Cigarette Trafficking Act (CCTA) and the Prevent All Cigarette Trafficking (PACT) Act. That assertion is false: plaintiffs acknowledge that they must show causation to recover for violations of these laws. And they have made that showing here through proof that UPS knowingly transported more than 10,000 untaxed cigarettes in violation of the CCTA, and delivered packages containing untaxed cigarettes for shippers on the federal government's Non-Compliant List (NCL) in violation of the PACT Act. In making these shipments, UPS both actually and proximately caused the consummation of transactions on which the required cigarette excise taxes were evaded. UPS thus directly contributed to the loss of the cigarette tax revenue that plaintiffs were owed.

The real dispute is not whether plaintiffs must show causation, but rather how to define the proper measure of damages attributable to UPS's conduct in violation of these federal statutes. As plaintiffs

explained in their principal brief, these statutes explicitly authorize the award of “money damages”—including recoupment of “any unpaid taxes”—against common carriers that engage in door-to-door deliveries of contraband cigarettes. Under a straightforward reading of this language, plaintiffs are entitled to damages equal to the amount of the unpaid taxes that were evaded by dint of UPS’s unlawful shipments.

UPS instead argues, and the district court ruled, that plaintiffs’ compensatory damages must be reduced by a counterfactual estimate of how much these cigarette excise taxes would have been evaded anyway if UPS had not been willing to ship untaxed cigarettes. But that theory is inconsistent with the CCTA and PACT Act, which contain no language authorizing a reduction in compensatory damages based on cigarette purchasers’ hypothetical ability to evade the law. That theory also fundamentally conflicts with the underlying purposes of these federal statutes, which Congress intended to meaningfully deter common carriers such as UPS from transporting untaxed cigarettes. And UPS cites no prior decision—not one—that permits a defendant to avoid the consequences of its misbehavior by pointing its finger at hypothetical continued wrongdoing by others.

This Court should accordingly reverse the district court's holding on the appropriate measure of damages and conclude that plaintiffs are entitled to the full amount of unpaid taxes on the contraband cigarettes that UPS transported.

## ARGUMENT

### **PLAINTIFFS' THEORY OF COMPENSATORY DAMAGES COMPORTS WITH THE RELEVANT STATUTES AND WITH GENERAL PRINCIPLES OF CAUSATION**

#### **A. The Text and Structure of the CCTA and PACT Act Support Measuring Compensatory Damages by the Amount of Unpaid Taxes Attributable to UPS's Violation of These Statutes.**

The parties agree that the CCTA and PACT Act determine the correct measure of damages relief for violations of those statutes. *See* Response and Reply Br. for Appellant (Resp. Br.) 116. The key statutory terms are not in dispute. Both statutes directly impose obligations on common carriers: the CCTA makes it “unlawful for any person” knowingly to “transport” contraband cigarettes, 18 U.S.C. § 2342(a); and the PACT Act specifies particular penalties for “a common carrier or other delivery service,” 15 U.S.C. § 377(b)(1)(B), while barring such

entities from knowingly completing “a delivery of any package for any person” listed on the federal NCL, *id.* § 376a(e)(2)(A).

Both statutes also provide for remedies, including damages, in enforcement suits against common carriers. In addition to requiring per-violation penalties, the PACT Act allows a State or locality to recoup “any other damages,” which explicitly “include[s] the payment of any unpaid taxes.” *Id.* § 377(b)(2). And the CCTA allows States and localities to obtain “appropriate relief for violations,” including both “civil penalties” and “money damages.” 18 U.S.C. § 2346(2). The plain language of these statutes easily encompasses awards of compensatory damages in the amount of unpaid taxes evaded as a result of a common carrier’s unlawful transportation of cigarettes. *See Connecticut Nat’l Bank v. Germain*, 503 U.S. 249, 254 (1992) (where “the words of a statute are unambiguous,” then the “judicial inquiry is complete” (quotation marks omitted)).

The statutes’ history and purpose further support this measure of damages, as plaintiffs’ initial brief explains. *See Br. for Pls.-Appellees* 134-39; *see also Abramski v. United States*, 134 S. Ct. 2259, 2267 (2014) (courts “must” interpret statutory language with reference to context,



history, and purpose). UPS does not dispute that both the CCTA and the PACT Act are aimed squarely at preventing evasion of state and local cigarettes taxes. *See* Resp. Br. 121. Both statutes thus embody congressional efforts to strengthen federal remedies in the face of persistent evasion of such taxes over decades. Measuring damages by the amount of unpaid taxes on unlawful shipments aligns the monetary relief for violations of these statutes with Congress's purpose in enacting these statutes in the first place.

This measure of damages against common carriers is reinforced by UPS's concession that a *seller* of untaxed cigarettes "obviously" would be liable for unpaid taxes under the CCTA or PACT Act. *Id.* at 120. UPS now asserts that a common carrier's liability under these statutes should not parallel that of sellers. *See id.* at 119-20. To begin with, UPS did not present this distinction below, and should not be permitted to raise it for the first time on appeal. In the trial court, UPS proceeded on the assumption that a common carrier, like a seller, may be liable for

unpaid taxes under the CCTA and PACT Act, and disputed only the proper calculation of such liability.<sup>1</sup>

In any event, the damages provision of the CCTA draws no distinction between carriers (like UPS) that violate the statute by knowingly “transport[ing]” unstamped cigarettes in the amounts prohibited by law, 18 U.S.C. § 2342(a), and sellers (like UPS’s shipper partners) that violate the CCTA by knowingly “ship[ping]” or “sell[ing]” such cigarettes, *see id.*; *see also United States v. Skoczen*, 405 F.3d 537, 547 (7th Cir. 2005) (noting that CCTA “does not apply only to the person whom the state law requires to pay the stamps”). And although the PACT Act authorizes differing *penalties* for violations by a “delivery seller” and a “common carrier,” 15 U.S.C. § 377(b)(1), its authorization of *damages* makes no similar distinction, *see id.* § 377(b)(2). Both sellers and transporters of untaxed cigarettes jointly cause the evasion of taxes

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<sup>1</sup> Indeed, were it otherwise, UPS’s expert testimony about a proposed “diversion” rate to taxable sales would have been wholly irrelevant. UPS did not present the “diversion” theory as an alternative argument to reduce unpaid-tax damages, in the event that they were available against a common carrier; rather, the diversion theory was UPS’s exclusive argument on the point of compensatory damages. (*See* Dkt. No. 492, at 216-23.)

on those cigarettes. See *infra* at 8-12. If sellers of untaxed cigarettes may be held liable for unpaid taxes under these federal statutes, as UPS agrees, then so may common carriers such as UPS.<sup>2</sup> And if a seller has no “diversionary” defense for reducing unpaid-tax liability under the CCTA or PACT Act, as UPS also apparently agrees (*see* Resp. Br. 120), then a common carrier similarly lacks such a defense.

UPS’s legal argument on damages boils down to the assertion that it bears lesser responsibility for the unlawful transactions here than do the relevant cigarette shippers. But both the cigarette sellers and their unofficial delivery arm, UPS, were vital participants in effectuating the thousands of unstamped-cigarette shipments that the district court found to have occurred. The full amount of unpaid taxes thus constitutes the minimum level of “appropriate relief” for violations of the CCTA, 18

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<sup>2</sup> This is not to say that a governmental plaintiff may recover the same unpaid taxes from both a seller and a common carrier on the same unlawful transactions, or that a damage award against one defendant could not be offset by the amount of a prior recovery from another. But plaintiffs have not recouped the applicable taxes from the sellers, as UPS notes (Resp. Br. 109), and this appeal therefore raises no question of a possible double recovery. *See Nature’s Plus Nordic A/S v. Nat. Organics, Inc.*, 646 F. App’x 25, 29 (2d Cir. 2016) (upholding damage award where record did “not ineluctably lead to the conclusion that [plaintiff] received a double recovery”).

U.S.C. § 2346(2), and reflects the “unpaid taxes” on the transactions that also violated the PACT Act, 15 U.S.C. § 377(b)(2).<sup>3</sup>

**B. Plaintiffs Have Established Causation.**

UPS is mistaken in arguing that plaintiffs’ construction of the CCTA and the PACT Act “dispense[s] with traditional causation principles.” Resp. Br. 121. To the contrary, plaintiffs have shown that UPS actually and proximately caused the violation of those statutes, by repeatedly and knowingly delivering untaxed cigarettes to consumers. By doing so, UPS played a critical role in effectuating transactions where cigarette excise taxes were unlawfully evaded. And those transactions caused injury to the State and City in the form of unpaid taxes.<sup>4</sup> Under established tort principles, UPS is therefore properly held

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<sup>3</sup> Nor does UPS suggest what other type of damages would be available under these laws for a common carrier’s unlawful transportation of untaxed cigarettes. Given UPS’s insistence that a permissible penalty cannot exceed some fixed multiple of compensatory damages (Resp. Br. 98-99, 102-03, 105-11), UPS’s position now appears to be that no monetary remedy whatsoever can attend its thousands of cigarette-trafficking violations.

<sup>4</sup> See, e.g., *City of New York v. Milhelm Attea & Bros.*, No. 06-cv-3620, 2012 U.S. Dist. LEXIS 116533, at \*14 (E.D.N.Y. Aug. (continued on the next page)

to account for plaintiffs' tax losses because, at a minimum, UPS provided "substantial assistance" to its shipper clients in evading plaintiffs' tax laws. *See* Restatement (Second) of Torts § 876(b)-(c); *see also id.* § 875 (reciting general rule that contributing tortfeasors are each "subject to liability to the injured party for the entire harm").

Even if UPS's conduct was not the *sole* cause of the claimed injuries here, its conduct was nonetheless both a cause-in-fact and proximate cause of the legal violations and the resulting losses to the State and City. To be sure, other wrongdoers (such as the shippers themselves) may also have violated the law by "sell[ing]" the untaxed cigarettes that UPS transported. *See* 18 U.S.C. § 2342(a). But the participation of others does not absolve UPS from responsibility for the injury that UPS's actions caused. Rather, it means that UPS may have the right to seek indemnity or contribution from shipper clients. *See Board of Educ. v. Sargent, Webster, Crenshaw & Folley*, 71 N.Y.2d 21, 27 (1987) (noting that adjudicated tortfeasor may seek indemnity or contribution from nonparty co-tortfeasor in later action). Indeed, UPS's

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17, 2012) (observing that governmental entity is injured "the minute" unstamped cigarettes are unlawfully "trafficked into" the jurisdiction).

tobacco agreements with shippers specifically require the shipper “to indemnify, defend and hold harmless UPS” from “all claims,” “liabilities,” “penalties,” and “enforcement procedures” deriving from that shipper’s “failure to comply with any applicable laws and regulations, whether such action is brought by a governmental agency or other person.” (J.A. 1704.) That more than one entity may have caused the untaxed cigarette transactions at issue thus provides no basis for minimizing the recovery to plaintiffs in this enforcement action against a defendant that independently violated the proscriptions of both the CCTA and the PACT Act.

Contrary to UPS’s assertion, the Supreme Court’s decision in *Hemi Group, LLC v. City of New York*, 559 U.S. 1 (2010), warrants no different conclusion. *See* Resp. Br. 118. *Hemi Group*—which was decided before the PACT Act’s passage and did not involve the CCTA—rejected New York City’s civil RICO claim seeking damages from a cigarette seller in the amount of unpaid taxes, based on the seller’s failure to comply with certain reporting requirements under the federal Jenkins Act. The Court concluded that the City had not established a sufficiently close causal link between the seller’s mere “failure to file reports” and cigarette

purchasers' separate and distinct "failure to pay" excise taxes. *Hemi Grp.*, 559 U.S. at 11, 16 n.2. And as the Court further observed, the Jenkins Act itself authorized only a criminal penalty and \$1,000 fine, but not damages, for reporting violations. *See* 15 U.S.C. § 377 (eff. 1949), *superseded by* Pub. L. 111-154, § 2, 124 Stat. 1087 (2010).

Neither of these essential features of *Hemi Group's* holding is present here. *First*, UPS's shipments directly facilitated (and, indeed, were essential to effect) the sales of untaxed cigarettes between sellers and purchasers. And *second*, plaintiffs' claims here are brought under laws expressly authorizing recovery of money damages, including unpaid taxes, from common carriers like UPS.<sup>5</sup> Indeed, UPS does not dispute that unpaid taxes are a recoverable item of damages in claims under the CCTA and PACT Act, but rather contests only the amount of unpaid taxes that are properly attributable to its conduct. As already

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<sup>5</sup> District courts in this Circuit already have rejected a reading of *Hemi Group* as meaning that a common carrier's CCTA violation cannot be the proximate cause of the State's and City's tax losses, even for purposes of a RICO claim. *See, e.g., City of New York v. FedEx Ground Package Sys., Inc.*, 175 F. Supp. 3d 351, 371 (S.D.N.Y. 2016) ("FedEx's alleged involvement in an enterprise designed to ship unstamped cigarettes into New York City and State was precisely the conduct that led to the Plaintiffs' losing tax revenue.").

demonstrated, that sum equals the full amount of unpaid taxes on the transactions.

**C. UPS May Not Reduce Its Damages by Asserting that Cigarette Purchasers Would Have Found Other Ways, Including Illegal Methods, to Evade Taxation.**

UPS contends (Resp. Br. 94-97), and the district court below agreed (S.A. 439-442), that compensatory damages should be reduced here by estimating, and excluding from the calculation, the number of cigarette purchases that would have been made through other tax-free means—or not at all—if UPS had not made prohibited shipments. But UPS cites no prior case holding that general causation principles require consideration of what hypothetical actors might (or might not) have done absent the defendant’s wrongdoing, when the *actual* harms flowing from the defendant’s actions are mathematically undisputed.

The traditional common-law standards of causation that UPS invokes (Resp. Br. 117) do not support its “diversion” theory for reducing its damages liability. These standards would not permit UPS to reduce its liability based on the existence of other *actual* wrongdoers. *See Basko v. Sterling Drug, Inc.*, 416 F.2d 417, 429 (2d Cir. 1969);



*Navigazione Libera Triestina Societa Anonima v. Newtown Creek Towing Co.*, 98 F.2d 694, 697 (2d Cir. 1938) (Hand, J.). Even less do these decisions allow a defendant to reduce its recoverable damages by positing *hypothetical* wrongdoing by others. The law does not support UPS's extraordinary theory that it may avoid responsibility for its misconduct by asserting that cigarette purchasers might have found other means of evading New York's excise taxes.

UPS also fails to address, let alone to resolve, the fundamental inconsistency between its damages theory and the federal statutes at issue here. Nothing in the text of the CCTA or PACT Act remotely suggests that a defendant may reduce damages by pointing to the prevalence of illegal cigarette trafficking in New York. And such an approach would conflict with the core purposes of these laws. Most strikingly, under UPS's approach, the damages available to States and localities under these anti-trafficking statutes would be the least in those jurisdictions where evasion of cigarette taxes is worst. That interpretation makes no sense. Higher-tax jurisdictions naturally suffer from widespread evasion on many different fronts. But this evasion gives such jurisdictions *greater* need for these laws' protections. UPS's

approach, by contrast, would dilute the damages remedies authorized by the CCTA and PACT Act in precisely those jurisdictions where strong remedies were most needed.

Indeed, the absurdity of UPS's theory is highlighted by the fact that its expert suggested that damages under the CCTA and PACT Act in this State would be "possibly zero," given the prevalence of cigarette-tax evasion in New York. (J.A. 2037.) Congress enacted the legislation at issue here in part to provide States and localities with a damages remedy for trafficking in untaxed cigarettes; it is inconceivable that Congress intended to eliminate that remedy in States and localities where the misconduct is most prevalent. *See DeMartino v. Comm'r*, 862 F.2d 400, 407 (2d Cir. 1988) ("[A] statute should not be interpreted to produce an absurd or unreasonable result.").

UPS's approach would lead to many other anomalies. For example, the two major common carriers in the shipment industry (UPS and FedEx) could each seemingly avoid damages liability for transporting unstamped cigarettes by arguing that the *other* carrier would have transported the contraband anyway if the first had not. And UPS's theory would also allow cigarette sellers to sidestep damages by pointing

to their fellow violators, reasoning—using the same “diversion” analysis that the district court accepted here—that the State and City suffered no harm at all because a purchaser would just have gone elsewhere. This Court should not endorse, or invite, such arguments.

This Court likewise should reject UPS’s claim that damages must be reduced to account for the possibility that some consumers would have forgone purchases of cigarettes entirely if UPS had complied with the law. (*See* J.A. 2037.) UPS’s expert acknowledged that only a small number of cigarette users would have gone this route; by contrast, the “overwhelming” majority—i.e., up to 83%—of the cigarette sales “at issue would divert to another source of untaxed cigarettes.” (J.A. 2049-2050.) UPS also has never specifically requested a partial reduction in damages for the modest number of cigarette sales that purportedly would not have occurred at all in a counterfactual world where UPS had followed the law. Nor would such a reduction be justified. In the *real* world, those untaxed purchases were made, and those cigarettes were smoked, with all the attendant public health consequences that the excise tax works to avoid. UPS’s proposed measure of damages—inclusive of its “diversion” theory—would fail

entirely to account for those harms.<sup>6</sup> By contrast, setting damages equal to the unpaid excise taxes on all of the transactions that did occur ensures that the costs of addressing those real public health harms are at least partly defrayed.

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<sup>6</sup> Similarly, New York's damages should not be reduced for the possibility, also presented by UPS's expert, that New York residents might have crossed state lines to buy cigarettes in person absent UPS's door-to-door transportation services. (*See* J.A. 2045-2046.) Again, the cigarettes were in fact bought and smoked in New York, and this consequence of UPS's unlawful conduct caused harm to plaintiffs that should be accounted for in the damages calculation. Moreover, such hypothetical cross-border cigarette transactions would in any event give rise to a tax obligation to New York on any interstate transportation of more than 400 cigarettes (two cartons). *See* Tax Law § 471-a.

## CONCLUSION

On plaintiffs' cross-appeal, this Court should order that the damages award cover the full amount of unpaid taxes on the unlawful transactions at issue.

Dated: New York, NY  
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## CERTIFICATE OF COMPLIANCE

Pursuant to Rule 32(a) of the Federal Rules of Appellate Procedure, Max Kober, an employee in the Office of the Attorney General of the State of New York, hereby certifies that according to the word count feature of the word processing program used to prepare this brief, the brief contains 3,171 words and complies the typeface requirements and length limits of Rule 32(a)(5)-(7).

/s/ Max Kober