No. 84265-0

IN THE COURT OF APPEALS
OF THE STATE OF WASHINGTON
DIVISION I

STATE OF WASHINGTON,

Respondent/Cross-Appellant,

v.

R.J. REYNOLDS TOBACCO COMPANY, et al.,

Appellants/Cross-Respondents.

PARTICIPATING MANUFACTURERS' RESPONSE TO AMICUS CURIAE BRIEF

GREENBERG TRAURIG LLP
Elli Leibenstein (*pro hac vice*)
Gregory Ostfeld (*pro hac vice*)
77 West Wacker Drive,
Suite 3100
Chicago, IL 60601
(312) 456-8400

BYRNES KELLER
CROMWELL LLP
Bradley S. Keller, WSBA #10665
John A. Tondini, WSBA #19092
1000 Second Avenue, 38th Floor
Seattle, WA 98104
(206) 622-2000

Attorneys for Appellants R.J. Reynolds Tobacco Company and Santa Fe Natural Tobacco Company

Additional counsel for Appellants continue inside cover

Warren Rheaume WSBA #13627
James C. Grant WSBA #14358
DAVIS WRIGHT TREMAINE LLP
920 Fifth Avenue, Suite 3300
Seattle, WA 98104
Telephone: (206) 757-8265
Email: warrenrheaume@dwt.com
jamesgrant@dwt.com

Alexander Shaknes (*pro hac vice* pending)
Manvin Mayell (*pro hac vice* pending)
ARNOLD & PORTER KAYE SCHOLER LLP
250 West 55th Street
New York, NY 10019
Telephone: (212) 736-8000
Email: Alex.Shaknes@arnoldporter.com
Manvin.Mayell@arnoldporter.com
Attorneys for Appellants Philip Morris USA Inc. and Sherman's 1400 Broadway N.Y.C., LLC

Vanessa S. Power, WSBA #30777
Jenna M. Poligo, WSBA #54466
Stoel Rives LLP
600 University Street, Suite 3600
Seattle, WA 98101
Telephone: (206) 624-0900
Email: vanessa.power@stoel.com
jenna.poligo@stoel.com

Mark A. Loyd (*pro hac vice*)
Lauren R. Nichols (*pro hac vice*)
Dentons Bingham Greenebaum LLP
3500 PNC Tower
101 South Fifth Street
Louisville, KY 40202

Telephone: (502) 589-4200
Email: Mark.Loyd@dentons.com
Lauren.Nichols@dentons.com
Attorneys for Appellants Farmers Tobacco Company of Cynthiana, Inc. and Wind River Tobacco Company, LLC

Alexander Vitruk, WSBA #57337
Logan Peppin, WSBA #55704
Baker & Hostetler LLP
999 Third Avenue, Suite 3900
Seattle, Washington 98104
Telephone: (206) 332-1380
Fax: (206) 624-7317
Email: avitruk@bakerlaw.com
lpeppin@bakerlaw.com

Elizabeth B. McCallum (*pro hac vice*)
Carey S. Busen (*pro hac vice*)
Evan Mannering (*pro hac vice*)
Baker & Hostetler LLP
1050 Connecticut Avenue, NW, Suite 1100
Washington, DC 20036
Tel: (202) 861-1522
Email: Emccallum@bakerlaw.com
Cbusen@bakerlaw.com
Emannering@bakerlaw.com
Attorneys for Appellants Commonwealth Brands, Inc., Compania Industrial de Tabacos Monte Paz, S.A., Daughters & Ryan, Inc., House of Prince A/S, Japan Tobacco International U.S.A., Inc., King Maker Marketing, Inc., Kretek International, Liggett Group LLC, ITG Brands, LLC, Peter Stokkebye Tobaksfabrik A/S, P.T. Djarum, Reemtsma Cigarettenfabriken Gmbh, Scandinavian Tobacco Lane Limited, Top Tobacco, L.P., and Von Eicken Group

TABLE OF CONTENTS

TABLE OF AUTHORITIES

The Participating Manufacturers ("PMs") respectfully submit this response to the *Amicus Curiae* Brief of Indian Tribal Governments Who Are Parties to Cigarette Tax Compacts with The State of Washington (the "*Amicus* Brief" or "Br."). The *Amicus* Brief concerns itself almost entirely with the irrelevant issue of whether Tribes have a sovereign power to levy taxes. But the U.S. Supreme Court long ago resolved that question. *See Washington v. Confederated Tribes of the Colville Reservation*, 447 U.S. 134 (1980). Put simply, the Tribes' inherent taxation power was not the question before the Panel, it was not the question before the Superior Court, and it is not the question before this Court. *Amici*'s arguments are thus directed to a strawman and provide no grounds supporting the State's request to vacate the arbitration Award entered against it or to sustain the Superior Court's improper declaratory judgment with respect to Washington's Qualifying Statute. Accordingly, for the reasons the PMs have articulated in their prior briefing, the PMs' appeal

should be granted, the declaratory judgment should be overturned, and the State's cross-appeal should be denied.

I. ARGUMENT

A. The Tribes' Power to Tax is Irrelevant to This Dispute.

The core premise of the *Amicus* Brief—that "Indian tribal governments have the inherent sovereign power to tax" (Br. at 1)—is both undisputed and irrelevant to the Award and to the pending cross-appeals from the Superior Court's order. During the 2004 Arbitration, the PMs did not contest, and the Panel did not overlook, that tribes have the inherent power to tax. Indeed, the Award acknowledges and discusses at length the U.S. Supreme Court's decision in *Colville*, including its holding that "Tribes have the power to impose their cigarette taxes on nontribal purchases," and the recognition that tribal taxation "is a fundamental attribute of sovereignty which the tribes retain." CP 680 (*quoting Colville*, 447 U.S. at 135-36). The Award also recounts testimony from Washington's witness, Kelly Croman,

regarding the "cigarette wars" between the State and the tribes and the resulting compact legislation. CP 684-687.

Rather than addressing broad questions of tribal sovereignty, the Panel in this case was asked to determine only a specific contractual question under the MSA: whether Washington diligently enforced its Qualifying Statute in 2004, including whether Washington's failure to even attempt to enforce escrow on tribal compact sales that its own Office of the Attorney General ("OAG") personnel considered to be "units sold" under the Qualifying Statute, and thus subject to escrow enforcement, was evidence of a lack of diligence.[1]

[1] Washington courts have twice held that these diligent enforcement issues, including interpretation of the Qualifying Statute's "units sold" language, are subject to mandatory arbitration. CP 623-635. Indeed, the State itself argued on multiple occasions that the 2003, 2004, and 2005-2007 Panels must decide the "unit sold" issue without any qualification. CP 765, 778, 844-850, 852-855, 896-911. It is only now that Washington has lost its diligence determination before the 2004 Panel that the State (and *amici*) claim this issue should supposedly be decided by the Washington courts.

The Panel's non-determinative conclusion that compact sales to non-tribal members constitute "units sold" that could be subject to escrow requirements does not undermine the tribes' power to tax. It is the NPMs that manufacturer the cigarettes—***not the tribal retailers***—that are required to deposit escrow on sales of compact cigarettes and that are subject to escrow enforcement. Likewise, enforcement of ***escrow*** deposits on compact sales does not deprive the tribes of ***tax*** revenue; the tribes retain that tax revenue regardless of whether the manufacturing NPMs are required to deposit escrow. Thus, even if the State had followed the guidance of its OAG personnel to enforce escrow on compact sales, its actions would have had no bearing on the tribes' power to tax.[2]

---

[2] *Amici* speculate, in a single footnote, that "State attempts to collect escrow deposits from cigarette manufacturers selling to tribes could interfere with tribes' ability to purchase cigarettes from out-of-state wholesalers and tribal manufacturers, RCW 43.06.455(5)(b)-(d), a right specifically bargained for by the tribes." Br. at 9 n.2. *Amici* do not substantiate this argument, nor do they explain how it is relevant to the Panel's determination that Washington did not diligently enforce its Qualifying Statute.

Further, while the MSA incentivizes states to enact and diligently enforce a Qualifying Statute, it does not mandate action. Rather, a state that fails to diligently enforce a Qualifying Statute is subject to a reduction of its annual settlement payment by application of the NPM Adjustment. Washington's election not to enforce its Qualifying Statute with respect to tribal sales for two decades, including in 2004, was a contractual choice with contractual consequences for the State. That financial choice has no impact on the tribes.

Thus, *amici's* lengthy exposition on the history of the tribes' authority to tax simply has no bearing on the underlying dispute in the 2004 Arbitration or the issues on appeal, and provides no ground for vacating the Award. The tribes' power to tax is beside the point; the question the Panel considered was the contractual question of whether *Washington* had, in 2004, exercised diligence in seeking to enforce its Qualifying Statute on compact sales to nontribal members that its own OAG considered at the time to be "units sold." The 2004 Panel

correctly found that it had not, while also concluding that the issue of compact sales was not determinative of the Panel's overall finding of non-diligence. In either event, the tribes' power to tax supplies no justification to alter, amend, or vacate the Award or to uphold the Superior Court's improper declaratory judgment.

B. *Amici* Misconstrue the Panel's Ruling on Tribal Compact Sales, Which Was Not Determinative of Its Award.

The Superior Court properly denied the State's motion to vacate because the Panel made unmistakably clear that the only factual finding the State challenged—Washington's lack of diligence with respect to compact sales—was *not* determinative of the Award. *Amici* fail, just as the State did, to address the determinative grounds for the Panel's finding of non-diligence. The 2004 Arbitration assessed all aspects of Washington's enforcement activities, including resource allocation, data collection and verification, audits, inspections, lawsuits, and other enforcement actions. Among numerous enforcement

lapses, the Panel determined "Washington failed to enforce escrow on compact cigarette and RYO sales that met the definition of Units sold under the state's escrow statute." CP 763. As the Award states, however, "***Washington's failure to enforce escrow on compact sales was not determinative of the Panel's decision on diligent enforcement. The state's other lapses, independent of [the Panel's] ruling on compact sales, were determinative on the issue of diligence***." CP 763 at n.116 (emphasis added).[3] *Amici's* arguments are silent regarding these determinative lapses and thus provide no basis for vacating the Award.

[3] As detailed in the Award, the State's other lapses include: failing to devote sufficient resources to escrow enforcement; failing to support the audit function; failing to collect complete and reliable data on NPM cigarette sales; failing to cross-check and audit data received from NPMs and distributors; failing to impose reasonable sanctions on non-compliant distributors and NPMs; lax analysis and auditing of NPM and distributor sales that enabled widespread escrow evasion; failing to coordinate the three departments playing an enforcement role; failing to make effective use of retail inspections; and using unreliable data collection and verification. *See, e.g.,* CP 762-63.

Further, *amici's* argument regarding "units sold" misconstrues the basis of the Panel's decision on this issue. The Panel faulted the State not because it was clear as a matter of law at the time that Washington had the authority and obligation to enforce its Qualifying Statute on compact sales, but because Washington declined to even attempt to enforce escrow on these stamped, tax-paid cigarettes, despite the contemporaneous belief of State enforcement authorities that Washington could and should do so. The Panel found the State's failure even to make the attempt—in the face of an active internal debate in which the majority view favored enforcement, and in the absence of any contrary authority—was inconsistent with diligence. *See* CP at 678-709. This conclusion would be true regardless of any eventual judicial interpretation of the Qualifying Statute. Washington failed to diligently enforce ***under the MSA*** because it failed to even try to enforce escrow obligations on certain cigarettes. *See* CP 678, 709, 763.

C. *Amici* Misinterpret the Compact Legislation.

Although the Panel's ruling on compact sales was not determinative of the Award, it was correct. The Panel thoroughly weighed the evidence presented and agreed with the PMs—and Washington's own OAG enforcement personnel—that escrow was required on compact sales to non-tribal members. *See* CP 703-709. As the Award addressed in detail, the Washington OAG provided multiple justifications for its contemporaneous position that compact sales remained subject to the Qualifying Statute. These reasons included:

> (1) the compact legislation provided that the tribal tax stamp is directly "in lieu" of the SET tax stamp;
>
> (2) "but for the cigarette tax compact, the cigarettes would be subject to the state's excise tax and the packs would bear the state's excise tax stamp";
>
> (3) "when the Legislature passed the cigarette tax compact bill, it had no intention of impacting the NPM law";
>
> (4) "both the statute authorizing the tribal compacts, and the compacts themselves, specifically provide that the tribal compacts should not affect the MSA"; and
>
> (5) taking a contrary view would undermine "the intent and purposes of the MSA and the cigarette tax contract

> legislation," both of which were aimed at "leveling the playing field and under the MSA, reducing the level of smoking, and preventing minors from smoking."

CP 700-701, 703-705.

Under such circumstances, it is unsurprising that OAG Special Counsel Hankins testified that, in 2004, "he considered a pack of compact cigarettes stamped with a tribal stamp to be a Unit sold because the stamp was authorized by the state of Washington." CP 707. As the OAG correctly recognized:

> [T]he fact that a tribal stamp is on the cigarette when, in the absence of the cigarette contract, a state stamp would be on the cigarette, does not exempt the cigarette from counting as a unit sold under RCW 70.157. A contrary interpretation would have the effect of the cigarette contract statute superceding [sic] the escrow statute, which would directly contradict the contract. Not counting the MSA sales of cigarettes to non-Indians on the reservation would place at risk the State's MSA share. These sales must be counted.

CP 705.

Despite the well-reasoned bases to pursue enforcement of escrow on compact sales, the State ultimately declined to follow the recommendation of key OAG personnel. The State also disregarded the view of the National Association of Attorneys

General ("NAAG") that "[c]ertainly the intent of the statute would have been to count these cigarettes," and "[i]f the [] stamp—ether [sic] state or tribal—is required by WA law, then I think you have a good argument that the stamp is a stamp of the State." CP 706-707. Following a ten-minute meeting in 2005, newly-elected Attorney General Robert McKenna, who had succeeded Attorney General Christine Gregoire, "announced his decision that compact sales were not subject to escrow." CP 707-708.

Amici's contention—that a tax imposed explicitly "in lieu" of a state tax is unrelated to the State's authority—is without merit. While the tribes certainly have an independent power to tax, there is also no dispute that "[t]he imposition of Washington's cigarette and sales taxes on on-reservation purchases by nonmembers of the Tribes is valid." CP 680 (*quoting Colville,* 447 U.S. at 135). For those compact tribes that do not share tax revenue with the State, the tribes' taxes explicitly

took the place of the state excise taxes ("SET") and served the identical function with the State's participation and blessing.

Indeed, as a practical matter, no tribal tax could have been imposed in lieu of State taxes without the State's collaboration. As *amici* recognize, "because the Tribes themselves impose a tax on the transaction, if the state tax is also collected the price charged will necessarily be higher and the Tribes will be placed at a competitive *disadvantage* as compared to businesses elsewhere." Br. at 17 (citing *Colville*, 447 U.S. at 154). The compact system for these tribes works only because Washington foreswore its right to tax and required, via the compact legislation and cigarette tax contracts, a "tribal" tax "in lieu of" imposition of SET, at a rate equal to 100 percent of the SET. Washington itself even issued the "tribal" stamps to be used by the tribes. CP 689-690.

Moreover, as set forth in the PMs' subsequent Motion for Clarification of the Superior Court's Order,[4] the State's and *amici's* arguments are inapplicable to cigarettes sold beginning in mid-2005 under the Puyallup Tribe's compact. Notably, the Puyallap Tribe has not joined the *Amicus* Brief, nor do *amici* address the issue presented by that compact.

The Puyallup compact was the subject of separate legislation "due to the very different nature of the cigarette trade on the Puyallup Indian reservation," and addressed "the substantial distinctions" through enacting legislation setting forth a different tax arrangement. RCW 43.06.465, Notes, Findings. Specifically, the cigarette tax agreement under any compact with the Puyallup Tribe "must include a provision requiring the tribe to transmit thirty percent of the tribal tax revenue on all cigarette sales to the state." RCW 43.06.465(3).

[4] The Superior Court's denial of that motion is the subject of a separate appeal pending before this Court (*see* Appeal No. 84691-4).

Indeed, wholesalers purchase the Puyallup Tribe tax stamps from U.S. Bank, the same entity selling State excise tax stamps; U.S. Bank collects the tax revenue from the sales of the Puyallup Tribe stamps, just as it does from the sales of State stamps; and U.S. Bank transfers tax revenues from Puyallup tax stamps to the same State tax fund as tax revenues from State tax stamps. Thus, the Puyallup legislation directly contradicts Washington and *amici's* repeated representations that "***tax revenue belongs to the tribe, not the State***" (CP 29, emphasis added) and that the "***the taxes are not imposed or authorized by the State***." Br. at 27 (emphasis added).

The Superior Court's blanket declaratory judgment that compact sales are not units sold, applicable to all current and future arbitrations, ignores this context and highlights the need for arbitration panels to consider all relevant facts for a given year and to issue a final award before the Superior Court undertakes its limited review role under the Federal Arbitration Act. Whether Washington failed to diligently enforce its

Qualifying Statute, including by omitting to pursue escrow deposits on compact sales, is a fact question for arbitrators to decide under the MSA. The Superior Court correctly denied the State's motion to vacate the Award but exceeded its authority when it issued a declaratory judgment that "units sold" excludes tribal compact cigarette sales. This declaratory relief intrudes on fact-finding in ongoing and future arbitration proceedings and misconstrues the definition of "units sold."

II. CONCLUSION

Neither *amici* nor the State present any valid grounds to overturn the Award or to sustain the Superior Court's declaratory judgment. The record reflects that Washington elected not to even attempt to collect escrow on tens of millions of compact tribal NPM sales in 2004 when there was at minimum a healthy internal debate over whether Washington should do so. Washington sought at its hearing, as Washington and *amici* do now, to justify this laxity and define away the issue by insisting after the fact that such sales were not "units sold" and therefore

irrelevant to Washington's diligence. The Panel rejected this argument and was correct to do so. Accordingly, the PMs' appeal should be granted, and the State's cross-appeal should be denied.

The undersigned certifies that the number of words contained in this document, exclusive of words contained in the appendices, the title sheet, the table of contents, the table of authorities, the certificate of compliance, the certificate of service, signature blocks, and pictorial images (e.g., photographs, maps, diagrams, and exhibits) is 2,617 words, which is within the limits of RAP 18.17.

DATED this 30th day of January, 2023.

BYRNES KELLER CROMWELL LLP

By /s/ John A. Tondini

Bradley S. Keller, WSBA #10665
John A. Tondini, WSBA #19092
1000 Second Avenue, 38th Floor
Seattle, WA 98104
Telephone: (206) 622-2000
Email: bkeller@byrneskeller.com
jtondini@byrneskeller.com

GREENBERG TRAURIG LLP
Elli Leibenstein (*pro hac vice*)
Gregory Ostfeld (*pro hac vice*)
77 West Wacker Drive, Suite 3100
Chicago, IL 60601
Telephone: (312) 456-8400
Email: leibensteine@gtlaw.com
ostfeldg@gtlaw.com

Attorneys for R.J. Reynolds Tobacco Co. and Santa Fe Natural Tobacco Co.

Warren Rheaume WSBA #13627
James C. Grant WSBA #14358
DAVIS WRIGHT TREMAINE LLP
920 Fifth Avenue, Suite 3300
Seattle, WA 98104
Telephone: (206) 757-8265
Email: warrenrheaume@dwt.com
jamesgrant@dwt.com

Alexander Shaknes
(*pro hac vice* pending)
Manvin Mayell
(*pro hac vice* pending)
ARNOLD & PORTER KAYE SCHOLER LLP
250 West 55th Street
New York, NY 10019
Telephone: (212) 736-8000
Email: Alex.Shaknes@arnoldporter.com
Manvin.Mayell@arnoldporter.com

Attorneys for Appellants Philip Morris USA Inc. and Sherman's 1400 Broadway N.Y.C., LLC

Vanessa S. Power, WSBA #30777
Jenna M. Poligo, WSBA #54466
STOEL RIVES LLP
600 University Street, Suite 3600
Seattle, WA 98101
Telephone: (206) 624-0900
Email: vanessa.power@stoel.com
jenna.poligo@stoel.com

Mark A. Loyd (*pro hac vice*)
Lauren R. Nichols (*pro hac vice*)
DENTONS BINGHAM GREENEBAUM LLP
3500 PNC Tower
101 South Fifth Street
Louisville, KY 40202
Telephone: (502) 589-4200
Email: Mark.Loyd@dentons.com
Lauren.Nichols@dentons.com

Attorneys for Appellants Farmers Tobacco Company of Cynthiana, Inc. and Wind River Tobacco Company, LLC

Alexander Vitruk, WSBA #57337
Logan Peppin, WSBA #55704
Baker & Hostetler LLP
999 Third Avenue, Suite 3900
Seattle, Washington 98104
Telephone: (206) 332-1380
Fax: (206) 624-7317
Email: avitruk@bakerlaw.com
lpeppin@bakerlaw.com

Elizabeth B. McCallum (*pro hac vice*)
Carey S. Busen (*pro hac vice*)

Evan Mannering (*pro hac vice*)
Baker & Hostetler LLP
1050 Connecticut Avenue, NW, Suite 1100
Washington, DC 20036
Tel: (202) 861-1522
Email: Emccallum@bakerlaw.com
Cbusen@bakerlaw.com
Emannering@bakerlaw.com

Attorneys for Appellants Commonwealth Brands, Inc., Compania Industrial de Tabacos Monte Paz, S.A., Daughters & Ryan, Inc., House of Prince A/S, Japan Tobacco International U.S.A., Inc., King Maker Marketing, Inc., Kretek International, Liggett Group LLC, ITG Brands, LLC, Peter Stokkebye Tobaksfabrik A/S, P.T. Djarum, Reemtsma Cigarettenfabriken Gmbh, Scandinavian Tobacco Lane Limited, Top Tobacco, L.P., and Von Eicken Group

Attorneys for Appellants

CERTIFICATE OF SERVICE

The undersigned attorney certifies that on the 30th day of January, 2023, a true copy of the foregoing was served on each and every attorney of record herein via email.

I declare under penalty of perjury under the laws of the State of Washington that the foregoing is true and correct.

DATED in Seattle, Washington, this 30th day of January, 2023.

/s/ John A. Tondini
John A. Tondini
Byrnes Keller Cromwell LLP
1000 Second Avenue, 38th Floor
Seattle, WA 98104
Telephone: (206) 622-2000

BYRNES KELLER CROMWELL LLP

January 30, 2023 - 1:38 PM

Transmittal Information

Filed with Court:	Court of Appeals Division I
Appellate Court Case Number:	84265-0
Appellate Court Case Title:	State of Washington v. American Tobacco Co., et al.

The following documents have been uploaded:

- 842650_Briefs_20230130133229D1701174_3988.pdf
  This File Contains:
  Briefs - Answer to Amicus Curiae
  The Original File Name was 2023.01.30 Resp to Amicus Brief by PMs.pdf

A copy of the uploaded files will be sent to:

- Alex.Shaknes@arnoldporter.com
- Christine.Truong@atg.wa.gov
- Jessica.Buswell@atg.wa.gov
- Lbruner@quinault.org
- Manvin.Mayell@arnoldporter.com
- anitamiller@dwt.com
- avitruk@bakerlaw.com
- bkeller@byrneskeller.com
- cbusen@bakerlaw.com
- chloe.villagomez@foster.com
- comcec@atg.wa.gov
- danielanajera@dwt.com
- devontiam@clearwatercasino.com
- dmadams@bakerlaw.com
- elees@skokomish.org
- emannering@bakerlaw.com
- emccallum@bakerlaw.com
- jenna.poligo@stoel.com
- jimgrant@dwt.com
- joshua.weissman@atg.wa.gov
- klyon@squaxin.us
- lauren.nichols@dentons.com
- lees@nelson-lees.com
- leibensteine@gtlaw.com
- leslie.lomax@stoel.com
- lparlange@kalispeltribe.com
- lpeppin@bakerlaw.com
- mark.loyd@dentons.com
- pateus@aol.com
- rene.tomisser@atg.wa.gov
- rsage@swinomish.nsn.us
- twoolsey@suquamish.nsn.us
- vanessa.power@stoel.com
- warrenrheaume@dwt.com

Comments:

Sender Name: Kim Wolf - Email: kwolf@byrneskeller.com
Filing on Behalf of: John Arthur Tondini - Email: jtondini@byrneskeller.com (Alternate Email:)

Address:
1000 Second Avenue
38th Floor
Seattle, WA, 98104
Phone: (206) 622-2000

Note: The Filing Id is 20230130133229D1701174