

COPY

No. A-03-2020

STATE OF MINNESOTA
IN SUPREME COURT

COUNCIL OF INDEPENDENT TOBACCO MANUFACTURERS
OF AMERICA, CAROLINA TOBACCO COMPANY,
AND WINNER TOBACCO WHOLESALE, INC.,

Appellants,

v.

THE STATE OF MINNESOTA AND DAN SALOMONE,
IN HIS OFFICIAL CAPACITY AS THE COMMISSIONER OF
THE MINNESOTA DEPARTMENT OF REVENUE,

Respondents.

APPELLANTS' BRIEF

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STATEMENT OF THE ISSUES

1. Whether Minn. Stat. § 297F.24 (the “Cigarette Fee Act”) violates the First Amendment because it taxes only those cigarettes made by parties who have refused to relinquish their First Amendment rights and exempts cigarettes made by manufacturers who have surrendered certain First Amendment rights.

The District Court and the Court of Appeals held the Cigarette Fee Act does not violate the First Amendment.

Apposite Cases:

Speiser v. Randall, 357 U.S. 513 (1958)

Minneapolis Star & Tribune Co. v. Minn. Comm’r of Revenue, 460 U.S. 575 (1983)

Perry v. Sindermann, 408 U.S. 593 (1972)

FCC v. League of Women Voters, 468 U.S. 364 (1988)

2. Whether the Cigarette Fee Act violates the Equal Protection Clause of the United States Constitution and the Uniformity Clause of the Minnesota Constitution by singling out and taxing cigarettes made by parties who have refused to relinquish their First Amendment rights while exempting cigarettes made by manufacturers who have surrendered certain First Amendment rights.

The District Court and the Court of Appeals held the Cigarette Fee Act does not violate the Equal Protection Clause or the Uniformity Clause.

Apposite Cases:

Minneapolis Star & Tribune Co. v. Minn. Comm’r of Revenue, 460 U.S. 575 (1983)

Nat’l Tea Co. v. State, 208 Minn. 607, 294 N.W. 230 (1940)

3. Whether the Cigarette Fee Act violates the Bill of Attainder Clause of the United States Constitution by punishing cigarette manufacturers for alleged past conduct without the benefits and protections of a judicial trial.

The District Court and the Court of Appeals held the Cigarette Fee Act does not violate the Bill of Attainder Clause.

Apposite Cases:

Nixon v. Adm'r of Gen. Servs., 433 U.S. 425 (1977)

United States v. Brown, 381 U.S. 437 (1965)

United States v. Lovett, 328 U.S. 303 (1946)

Cummings v. Missouri, 71 U.S. (4 Wall.) 277 (1866)

STATEMENT OF THE CASE

Appellants Council of Independent Tobacco Manufacturers of America (“CITMA”), Carolina Tobacco Company, and Winner Tobacco Wholesale (collectively, “Appellants”) brought this action against Respondents State of Minnesota and Dan Salomone, in his official capacity as the Commissioner of the Minnesota Department of Revenue (collectively, “the State” or “Minnesota”) challenging the constitutionality of Minnesota Statutes section 297F.24 (the “Cigarette Fee Act”). (APP. 1-62.)¹ The Cigarette Fee Act imposes a 35 cent per pack tax on only those cigarettes manufactured by companies who have refused to surrender their fundamental First Amendment rights to free speech, petition the government for a redress of grievances, and access the courts. (APP. 1-62.) The Cigarette Fee Act violates the First Amendment of the United States Constitution, the Equal Protection Clause of the United States Constitution, the Uniformity Clause of the Minnesota Constitution, and the Bill of Attainder Clauses of the United States and Minnesota Constitution.² (APP. 1-62.)

On July 2, 2003, the District Court denied Appellants’ motion for a temporary restraining order and temporary injunction. (APP. 63-67.) The parties subsequently stipulated to many of the relevant facts (APP. 68-83) and filed cross-motions for summary judgment. (APP. 169-172.) On November 18, 2003, the District Court denied Appellants’ motion for summary judgment and granted the State’s motion for summary

¹ “APP” refers to Appellants’ Appendix.

² On appeal, Appellants have withdrawn their procedural due process claim under the United States Constitution. Although the District Court discussed whether the Cigarette Fee Act violates *substantive* due process, Appellants note they never raised such a claim.

judgment. (APP. 327-349.) On December 1, 2003, the District Court entered judgment dismissing Appellants' complaint. (APP. 350.)

On December 23, 2003, Appellants timely appealed the District Court's Order and Judgment. (APP. 351-353.) On August 24, 2004, the Court of Appeals affirmed the District Court's Order and Judgment in a published opinion. (APP. 354-366); 685 N.W.2d 467 (Minn. Ct. App. 2004).

On September 23, 2004, Appellants timely petitioned this Court seeking review of the Court of Appeals' decision. In an Order filed November 16, 2004, this Court granted Appellants' Petition.

STATEMENT OF THE FACTS

I. THE STATE SUED THE MAJOR TOBACCO COMPANIES TO RECOVER DAMAGES FOR HARM CAUSED BY THEIR FRAUDULENT AND UNLAWFUL CONDUCT.

On August 17, 1994, the State, along with co-plaintiff Blue Cross and Blue Shield, sued Philip Morris, Inc. ("Philip Morris"), R.J. Reynolds Tobacco Company ("R.J. Reynolds"), Brown & Williamson Tobacco Corporation ("Brown & Williamson"), B.A.T. Industries P.L.C., British-American Tobacco Company Limited, BAT (U.K. & Export) Limited, Lorillard Tobacco Company ("Lorillard"), The American Tobacco Company, Liggett Group, Inc. ("Liggett"), The Council for Tobacco Research-U.S.A., Inc., and The Tobacco Institute, Inc. (these proceedings shall be referred to as the "State Tobacco Lawsuit"). (APP. 71, 86-124.) The State did not sue Appellants or any members of CITMA.

In the State Tobacco Lawsuit, the State asserted claims for monetary, equitable and injunctive relief, and sought to place responsibility upon the defendant cigarette manufacturers for costs incurred, and to be incurred, by the State arising from the conduct of the defendant cigarette manufacturers regarding their products. (APP. 71, 86-124.) The State asserted nine causes of action against defendants, including claims for consumer fraud, false advertising, deceptive trade practices and anti-trust violations. (APP. 86-124.) The State alleged that the defendants "knew for decades from their own internal studies that their products are deadly and addictive," yet engaged in a "unified campaign of deceit and misrepresentation" in an effort to conceal this information. (APP. 71.) The State specifically singled out Philip Morris, for suppressing independent

research on the health effects of smoking; Liggett, for deciding not to market safer cigarettes; R.J. Reynolds, for marketing to children and concealing research on smoking related diseases; and Brown & Williamson, for suppressing information regarding the addictive nature of nicotine and the correlation between smoking and cancer rates. (APP. 4-5.) The State sought punitive damages, alleging that the defendants' conduct "demonstrate[d] a willful indifference to the rights or safety of others." (APP. 121.) The State also sought a declaration that the defendants had "engaged in consumer fraud, unlawful trade practices, deceptive trade practices, false advertising, unreasonable restraints of trade, and use of monopoly power to affect competition in violation of the laws of the State of Minnesota." (APP. 121.)

II. THE STATE NEGOTIATED A SETTLEMENT UNDER WHICH THE MAJOR TOBACCO COMPANIES AGREED TO MAKE SUBSTANTIAL PAYMENTS AND WAIVE CERTAIN FIRST AMENDMENT RIGHTS.

The parties ultimately reached a settlement of the State Tobacco Lawsuit. (APP. 71-74, 125-155.) Initially, the State settled with Liggett on March 20, 1997, in exchange for substantial cooperation in prosecuting the action against the remaining defendants. (APP. 71-72.) The State then settled with Philip Morris, R.J. Reynolds, Brown & Williamson and Lorillard (collectively, the "Majors") on or about May 12, 1998 (the "Settlement Agreement"), after extensive discovery, a lengthy trial and on the eve of the case going to the jury with the State seeking an award of substantial compensatory, punitive and treble damages. (APP. 72-74, 121-123, 125-155.)

Under the terms of the Settlement Agreement, the Majors agreed to make payments to the State and relinquish certain of their First Amendment rights. The Majors

agreed to pay an estimated \$6.1 billion over the first 25 years, with each manufacturer's payment calculated in proportion to its respective United States market share. (APP. 73-74, 130-136, 138-139, 152, 154-155.) The Majors also agreed to numerous restrictions of their First Amendment rights, including their rights to free speech, to petition the government by lobbying elected representatives, and to access the courts to challenge certain laws. (APP. 73, 139-143.) These waivers of First Amendment rights include advertising restrictions far more onerous than the State could constitutionally impose on cigarette manufacturers, such as removing all tobacco billboards and eliminating all tobacco advertisements on buses, taxis and bus shelters, discontinuing payments to movie and television producers, and ceasing distribution of promotional items such as hats and t-shirts bearing their products' brand names. (APP. 73, 139-143.) The Majors also agreed not to oppose certain legislation impacting the tobacco industry, including legislation "which would preempt, override, abrogate or diminish the State's rights or recoveries" under the Settlement Agreement. (APP. 139-140.) Further, the Majors agreed to waive their right of access to the courts, specifically agreeing not to "challenge the enforceability or constitutionality of existing Minnesota laws or rules relating to tobacco control." (APP. 139.)

III. THE MAJOR TOBACCO COMPANIES AND OTHER STATES ENTERED INTO THE MASTER SETTLEMENT AGREEMENT.

On November 23, 1998, about six months after execution of the Minnesota Settlement Agreement, the Attorneys General of 46 states and 6 territories (collectively, the "Settling States") entered into the Master Settlement Agreement ("MSA") with the

Majors. (APP. 76-77.) The MSA settled lawsuits that had been brought against the Majors by each of the Settling States based on allegations regarding the conduct of the Majors similar to those allegations made by Minnesota in the State Tobacco Lawsuit. (APP. 76-77.) Under the MSA, the Majors agreed to make initial and annual payments totaling over \$200 billion over the first 25 years. (APP. 76.) The Majors also agreed to adhere to comprehensive advertising and lobbying restrictions similar to those contained in the Minnesota Settlement Agreement. (APP. 76.)

Manufacturers who were not originally named in the Settling States' lawsuits have been "encouraged" to join the MSA as "Subsequent Participating Manufacturers." (APP. 76-77.) To entice manufacturers to join, the MSA provides that a Subsequent Participating Manufacturer who joined the MSA within 90 days of its execution does not owe any payments on sales that do not exceed its 1998 market share or 125% of its 1997 market share. (APP. 76-77.) Subsequent Participating Manufacturers are required to abide by the MSA's advertising and lobbying restrictions. (APP. 76-77.)

The MSA also encourages the Settling States to enact and "diligently enforce" Qualifying Statutes which require manufacturers who do not enter into the MSA ("Non-Participating Manufacturers") to pay similar amounts that would otherwise be owed under the MSA into interest bearing escrow accounts based on their cigarette sales in the Settling State. (APP. 77, 156-160.) Payments under these Qualifying Statutes remain in escrow earning interest for 25 years unless used to pay the Settling State for tobacco-related claims similar to those brought against the Majors. (APP. 77, 156-160.) If the Settling State does not recover such a judgment or settlement against the

Non-Participating Manufacturer, the escrow payments are returned to the manufacturer, with all of the earned interest, after 25 years. (APP. 77, 156-1 60.)

According to the MSA, the payments by Non-Participating Manufacturers into these escrow funds is necessary to (1) create a “reserve fund” to guarantee an “eventual source of recovery from [Non-Participating Manufacturers] *if they are proven to have acted culpably,*” and (2) “effectively and fully neutralize the cost disadvantages that the Participating Manufacturers experience vis-à-vis Non-Participating Manufacturers within such Settling State as a result of the provisions of this Agreement.” (APP. 76) (emphasis added).³ Settling States that do not enact and diligently enforce such a Qualifying Statute risk the loss of MSA payments. (APP. 76.) The MSA provides Settling States with a model Qualifying Statute. (APP. 77, 156-160.)

Courts have generally upheld the Qualifying Statutes in the face of constitutional challenges, relying on the fact that the Non-Participating Manufacturers are only required to pay money into interest bearing escrow accounts as security for potential judgments and that the escrowed funds shall be returned with the earned interest unless the manufacturer is found liable based on its conduct. See, e.g., PTI, Inc. v. Philip Morris, Inc., 100 F. Supp. 2d 1179 (C.D. Cal. 2000).

³ The full text of the MSA is available at http://www.naag.org/upload/1032468605_cigmsa.pdf. (APP. 76.)

IV. THE STATE ENACTED THE CIGARETTE FEE ACT TO SINGLE OUT AND TAX INDEPENDENT TOBACCO MANUFACTURERS WHO HAVE NOT BEEN SUED AND HAVE NOT SURRENDERED THEIR FIRST AMENDMENT RIGHTS.

Rather than enacting a Qualifying Statute to create an escrow fund as 46 other states have done, Minnesota decided to enact the Cigarette Fee Act which imposes a non-refundable tax on those cigarettes made by manufacturers that did not settle with Minnesota in the State Tobacco Lawsuit. (APP. 80-82, 85.) The Cigarette Fee Act is fundamentally different from the Qualifying Statutes because it imposes a non-refundable tax as opposed to requiring payments into a refundable escrow account. (APP. 80-82, 85.) Unlike the Qualifying Statutes, which expressly provide for the return of escrowed funds with interest if a cigarette manufacturer is not guilty of unlawful conduct similar to the Majors, Minnesota imposes a tax on all cigarettes made by non-settling manufacturers regardless of whether the manufacturer is ever sued or found liable for any allegedly wrongful conduct. (APP. 80-82, 85.)

On May 25, 2003, Governor Pawlenty signed legislation that included the Cigarette Fee Act. (APP. 80, 85.) The Cigarette Fee Act imposes a tax of 1.75 cents per cigarette (35 cents per pack of 20 cigarettes) (the "Tax") upon the sale of all "nonsettlement cigarettes" in Minnesota after June 30, 2003. (APP. 80-82, 85.) The Cigarette Fee Act defines a "nonsettlement cigarette" as a cigarette manufactured by a person other than a manufacturer making annual payments to the State under the State Tobacco Lawsuit Settlement Agreement, thereby exempting all of the Majors' products from the Tax. (APP. 80, 85.) The Cigarette Fee Act also exempts manufacturers who

have “voluntarily entered into an agreement” with the State with “terms similar to those contained in the Settlement Agreement,” including making annual payments to the State equal to at least 75 percent of the payments that would apply if the manufacturer was one of the four original parties to the Settlement Agreement. (APP. 81-82, 85.) As the State concedes, only those cigarette manufacturers who have surrendered certain First Amendment rights are exempt from the Tax, and the Tax is imposed on non-settling manufacturers’ products unless and until they surrender certain of their First Amendment rights. (APP. 81-82, 85.)

Additionally, although not expressly exempted under the terms of the statute, Liggett’s cigarettes are exempted from the Cigarette Fee Act as a result of the settlement of a lawsuit Liggett filed against the State on June 17, 2003. (APP. 306-326.) Liggett’s lawsuit sought a declaration that its products could not be treated as “nonsettlement cigarettes” within the meaning of the Cigarette Fee Act because Liggett had entered into a separate settlement with the State, which included provisions wherein Liggett agreed to relinquish certain of its First Amendment rights. (APP. 306-317.) Pursuant to the July 22, 2003 settlement of that lawsuit, the State agreed to exempt Liggett from the Tax, and Liggett agreed to make annual payments of \$100,000 to the State “with respect to all of Liggett’s brand styles.” (APP. 318-326.) Such payments are made irrespective of Liggett’s market share or how many cigarettes Liggett sells in Minnesota in a given year. (APP. 318-326.) Liggett’s waiver of its First Amendment rights under its prior settlement agreement with the State remains in effect. (APP. 318-326.)

The Cigarette Fee Act singles out and imposes a tax on those tobacco manufacturers who have refused to waive their First Amendment rights. The Tax also does not serve its professed purposes.

One stated purpose of the Cigarette Fee Act is to “prevent manufacturers of nonsettlement cigarettes from undermining the state’s policy of discouraging underage smoking.” (APP. 85.) However, the Tax does not serve that alleged purpose. In fact, the Minnesota Department of Health has determined that the Majors’ products, which are exempt from the Tax, account for the vast majority of underage smoking, while nonsettlement cigarettes account for very few underage sales. (APP. 79.)⁴

Another stated purpose of the Cigarette Fee Act is to “ensure that manufacturers of nonsettlement cigarettes pay fees to the state that are comparable to the costs attributable to the use of the cigarettes.” (APP. 85.) However, the Tax does not serve this alleged purpose either. The health effects caused by nonsettlement cigarettes, such as Appellants’ cigarettes, are no different than the health effects caused by cigarettes produced by the Majors. Yet the Majors’ products are exempt from the Tax and the Majors are not making payments to Minnesota because of their products, but rather because they settled claims concerning their fraudulent and illegal conduct in selling their products. Moreover, funds received by the State pursuant to the Cigarette Fee Act are not

⁴ The State reports that Marlboro, made by Philip Morris, Camel, made by R.J. Reynolds, and Newport, made by Lorillard, account for over 88% of sales to high schoolers and 75% of sales to middle schoolers. (APP. 79); Minnesota Department of Health, Results from the Minnesota Youth Tobacco Survey (Dec. 2000); see also United States Department of Health & Human Services, Study Shows Three Cigarette Brands Dominate Youth Smoking <<http://www.hhs.gov/news/press/1999pres/990414a.html>> (visited August 28, 2003) (Marlboro, Newport, and Camel “are by far the brands used most by teens,” totaling almost 90% of underage smokers).

allocated exclusively to anti-smoking or public health programs, but rather are merely deposited into the State's General Fund and allocated across the State's budget.

(APP. 85.)

V. APPELLANTS ARE AMONG THOSE WHO HAVE BEEN SINGLED OUT BY THE STATE.

Appellant CITMA is an association of small, independent tobacco manufacturers located throughout the United States whose products are unconstitutionally subject to the Tax under the Cigarette Fee Act. (APP. 3, 302.) Several CITMA members (such as Appellant Carolina Tobacco) sell tobacco products in Minnesota, including cigarettes which are "nonsettlement cigarettes" under the Cigarette Fee Act. (APP. 302.) As a result, CITMA members' cigarettes are subject to the 35 cent per pack Tax under the statute. (APP. 3, 302.) The Tax effectively raises the price of CITMA members' products resulting in decreased demand for these products. (APP. 7-8, 302.)

No CITMA members were parties to the State Tobacco Lawsuit, or the settlement thereof; no CITMA members have been accused of the type of fraudulent and unlawful activities for which the Majors have been held culpable; and no CITMA members have "voluntarily" agreed to terms similar to those contained in the settlement of the State Tobacco Lawsuit. (APP. 3, 302.) CITMA members do not want to relinquish their First Amendment rights. (APP. 3.) Although Appellants acknowledge that cigarette smoking is harmful and that the State has a legitimate interest in seeking to protect the public health, Appellants sell a legal product and have First Amendment rights. See Lorillard Tobacco Co. v. Reilly, 533 U.S. 525, 554 (2001).

Appellant Carolina Tobacco is a manufacturer of tobacco products, including cigarettes which are distributed and sold in the State of Minnesota and which are subject to the Cigarette Fee Act. (APP. 3, 300.) The State's imposition of the Tax on Carolina Tobacco's products has significantly and irreparably damaged Carolina Tobacco's ability to compete in Minnesota with those manufacturers whose products are exempt from the Tax. (APP. 300-301.) As a result of the Cigarette Fee Act, the cost of Carolina Tobacco's cigarettes has increased significantly and, therefore, Carolina Tobacco has sold significantly fewer cigarettes in Minnesota. (APP. 300-301.) The decrease in Carolina Tobacco's sales is the direct result of the Cigarette Fee Act because the Tax has caused distributors and retailers to purchase fewer, or in some instances to cease buying altogether, Carolina Tobacco's cigarettes. (APP. 300-301.)

Appellant Winner Tobacco is a distributor of tobacco products in the State of Minnesota, including cigarettes which are subject to the Tax pursuant to the Cigarette Fee Act. (APP. 4, 292-293.) Pursuant to the statute, Winner Tobacco must tender payment of the Tax to the State. (APP. 85, 292-293.) Winner Tobacco does not distribute cigarettes made by the Majors. (APP. 292.) The Tax significantly and irreparably damages Winner Tobacco's ability to compete with distributors who sell cigarettes manufactured by the Majors because Winner Tobacco competes primarily on price. (APP. 293-295.) The statute has also interfered with Winner Tobacco's ability to obtain valuable retail store shelf space as a result of its decreased ability to compete on price. (APP. 293-295.) Winner Tobacco has suffered significant harm as a result of the Tax

which has increased the price and decreased the sale of the cigarettes it distributes. (APP. 293-295.)

SUMMARY OF THE ARGUMENT

The Cigarette Fee Act is unconstitutional because the imposition of the Tax is entirely contingent on whether the cigarette manufacturer has surrendered its First Amendment rights. The Tax is imposed only on those products made by manufacturers who have refused to relinquish their fundamental First Amendment rights to freedom of speech, petition the government, and access the courts, and it exempts those manufacturers that have agreed to surrender these rights. The Cigarette Fee Act therefore violates the United States and Minnesota Constitutions because it draws explicit distinctions and discriminates based on the exercise of First Amendment rights.

The District Court and the Court of Appeals failed to apply the correct standards to analyze the constitutionality of this Tax which singles out parties because they have not waived their First Amendment rights. Rather than presuming its constitutionality, the Cigarette Fee Act must be presumed to be unconstitutional because of the distinctions it draws based upon the exercise of First Amendment rights. As such, the burden is on the State—not Appellants—to demonstrate its constitutionality. The State has not met, and cannot meet, its burden.

First, and foremost, the Cigarette Fee Act violates the First Amendment because it punishes Appellants and other nonsettlement cigarette manufacturers who refuse to surrender their First Amendment rights by taxing their products while exempting the products made by parties who have waived their rights. Second, the Cigarette Fee Act

violates the Equal Protection Clause of the United States Constitution and the Uniformity Clause of the Minnesota Constitution because it discriminates against Appellants and other non-settling cigarette manufacturers by taxing their products based on their refusal to waive their First Amendment rights while exempting products made by manufacturers who have surrendered their rights. The Cigarette Fee Act also constitutes an unconstitutional Bill of Attainder because it penalizes Appellants and other non-settling manufacturers for purported conduct that has neither been alleged nor proved by the State. The State itself effectively acknowledges as much by purporting to justify the Tax on Appellants' products by claiming the Tax payments are equivalent to the settlement payments made by the Majors—payments made to settle claims that the Majors committed fraud, falsely advertised their products, and violated anti-trust laws allegedly entitling the State to punitive damages.

ARGUMENT

“Evaluating a statute’s constitutionality is a question of law.” Hamilton v. Comm’r of Pub. Safety, 600 N.W.2d 720, 722 (Minn. 1999). “Questions of law are subject to de novo review; therefore, [this Court] is not bound by the lower court’s decision.” Id. This Court has a duty to declare a statute unconstitutional when it “runs afoul of [a] constitutional mandate.” State v. Harris, 667 N.W.2d 911, 920 (Minn. 2003).

I. THE CIGARETTE FEE ACT IS UNCONSTITUTIONAL BECAUSE IT IMPOSES A TAX BASED ON WHETHER A TOBACCO MANUFACTURER HAS WAIVED ITS FIRST AMENDMENT RIGHTS.

The Cigarette Fee Act violates the First Amendment⁵ on its face because it taxes products based on whether the manufacturer has surrendered its First Amendment rights. The Act imposes a tax only on those products manufactured by parties who have refused to relinquish their First Amendment rights, while exempting products made by parties who have waived their rights. Just as it would be unconstitutional for the State to directly impose the Settlement Agreement's restrictions on cigarette manufacturers' First Amendment rights, it is also unconstitutional to tax Appellants' products because they have refused to surrender such rights. Similarly, the Cigarette Fee Act's attempt to impose the Settlement Agreement's restrictions on First Amendment rights indirectly by offering them as an "alternative" to the Tax is also unconstitutional.

The Court of Appeals' ruling that the Cigarette Fee Act does not violate the First Amendment because it has a "legitimate purpose" and is "not a direct attempt to regulate speech" is wrong and contrary to United States Supreme Court precedent. The United States Supreme Court has squarely held that "Illicit government intent is not the sine qua non of a violation of the First Amendment. . . . We have long recognized that even regulations aimed at proper governmental concerns can restrict unduly the exercise of

⁵ The First Amendment to the United States Constitution provides: "Congress shall make no law . . . abridging the freedom of speech . . . or the right of people . . . to petition the Government for redress of grievances." U.S. Const. amend. I. In addition, the Minnesota Constitution provides: "[A]ll persons may freely speak, write and publish their sentiments on all subjects." Minn. Const. art. I, § 3. The Minnesota Supreme Court has interpreted the scope of this provision to be same as the First Amendment to the United States Constitution. See State v. Wicklund, 589 N.W.2d 793, 799-801 (Minn. 1999). Thus, the Cigarette Fee Act also violates article I, section 3 of the Minnesota Constitution.

rights protected by the First Amendment.” Minneapolis Star & Tribune Co. v. Minn. Comm’r of Revenue, 460 U.S. 575, 592 (1983); see also NAACP v. Alabama, 357 U.S. 449, 461 (1958) (violation of First Amendment rights, “even though unintended, may inevitably follow from varied forms of government action”); Johnson v. Dir. of Prof’l Responsibility, 341 N.W.2d 282, 285 (Minn. 1983) (although rule was designed to serve a “meritorious goal,” it violated the First Amendment). The United States Supreme Court and this Court have repeatedly struck down as unconstitutional laws burdening First Amendment rights that served legitimate purposes and were not direct attempts to regulate speech. See, e.g., Minneapolis Star, 460 U.S. at 592; NAACP v. Alabama, 357 U.S. at 461; NAACP v. Button, 371 U.S. 415, 439 (1963); Lovel v. Griffin, 303 U.S. 444, 451 (1938); Schneider v. New Jersey, 308 U.S. 147 (1939); Minn. Fifth Cong. Dist. Indep.-Republican Party v. State, 295 N.W.2d 650, 654-55 (Minn. 1980).

The State’s argument that Appellants and other non-settling cigarette manufacturers would be subject to similar financial burdens if they agreed to waive their First Amendment rights under the “voluntary” agreement authorized by the Cigarette Fee Act is irrelevant and does not save the statute from its constitutional infirmities. Indeed, the argument fails to address Appellants’ principal attack on the statute: The Cigarette Fee Act is unconstitutional because it taxes Appellants’ products based on their refusal to surrender their First Amendment Rights, regardless of whether they may avoid the Tax by entering into “voluntary” agreements waiving their First Amendment rights. Finally, the State’s reliance on caselaw upholding Qualifying Statutes imposing refundable

escrow payments are inapplicable and irrelevant to determining whether the nonrefundable Tax imposed by the Cigarette Fee Act is constitutional.

A. The State Bears the Burden of Proving the Cigarette Fee Act is Constitutional.

Although Minnesota statutes are generally presumed to be constitutional, see State v. Behl, 564 N.W.2d 560, 566 (Minn. 1997), this presumption of constitutionality is reversed where, as here, the challenged statute infringes upon First Amendment rights. See State v. Casino Mktg. Group, Inc., 491 N.W.2d 882, 885 (Minn. 1992). This is because the “presumption of constitutionality cannot be reconciled with the unique protections afforded by the First Amendment.” Id. at 885. Thus, when a statute is alleged to violate the First Amendment, the government bears the burden of proving that the law is constitutional. Id. Accordingly, it is an “error of law” to employ a presumption of constitutionality in evaluating a claim that a statute burdens First Amendment rights, even if the statute is ultimately held to be constitutional. Id. at 885, 891-92. Since Appellants have raised a First Amendment challenge to the Cigarette Fee Act, the State bears the burden of establishing that the statute is constitutional. Id.; see also Kismet Investors, Inc. v. County of Benton, 617 N.W.2d 85, 93 (Minn. Ct. App. 2000) (“Although statutes and ordinances generally carry a presumption of constitutional validity, when an ordinance *allegedly* infringes First Amendment rights, the local government bears the burden of demonstrating that the ordinance is constitutional.”) (emphasis added). As shown below, the State has failed to carry its burden.

B. The Cigarette Fee Act is Unconstitutional on its Face Because it Taxes Products Based on Whether the Manufacturer Has Surrendered its First Amendment Rights.

The Cigarette Fee Act violates the First Amendment by taxing all products made by parties that have refused to surrender their First Amendment rights and exempting all products made by parties that have agreed to surrender their First Amendment rights. In this way, the statute draws a facially discriminatory and unconstitutional distinction based solely on whether the tobacco manufacturer has waived its First Amendment rights. Accordingly, the Cigarette Fee Act is unconstitutional because it effectively conditions the right of non-settling manufacturers to engage in advertising and lobbying protected by the First Amendment on the payment of the Tax on their products. See Minneapolis Star & Tribune Co. v. Minn. Comm’r of Revenue, 460 U.S. 575, 586 n.9 (1983) (“By imposing the tax as a condition of engaging in protected activity, [the government] imposed a form of prior [unconstitutional] restraint on speech”); Follett v. Town of McCormick, 321 U.S. 573, 577 (1944) (“The exaction of a tax as a condition to the exercise of the great liberties guaranteed by the First Amendment is as obnoxious . . . as the imposition of the censorship or a previous restraint.”)

The United States Supreme Court has held that these types of state taxing schemes that seek to limit taxpayers’ freedom of speech or to punish taxpayers for engaging in speech protected by the First Amendment are unconstitutional. In Speiser v. Randall, 357 U.S. 513 (1958), the Supreme Court struck down a California tax law which exempted only those veterans who swore a loyalty oath. Id. at 518-19. The Court held that, just as the State could not constitutionally require veterans to take the loyalty oath,

the State likewise could not tax only those veterans who refused to take the loyalty oath. Id. Allowing the State to do so would allow it to unconstitutionally punish veterans who retained their First Amendment rights and to seek to coerce those veterans into waiving their First Amendment rights. Id.

The United States Supreme Court has explained that Speiser stands for the proposition that the government “may not deny a benefit to a person on a basis that infringes his [or her] constitutionally protected interests—especially, his [or her] interest in freedom of speech.” Perry v. Sindermann, 408 U.S. 593, 597 (1972). This is because if the government “could deny a benefit to a person because of his [or her] constitutionally protected speech or associations, his [or her] exercise of those freedoms would in effect be penalized and inhibited.” Id. In other words, the government may not impose a penalty, such as a tax, to “produce a result which it could not command directly.” Id. (quoting Speiser, 357 U.S. at 526).

In FCC v. League of Women Voters, 468 U.S. 364 (1988), the Supreme Court applied these same principles and struck down a federal law that conditioned the grant of federal funds on whether a television station agreed to refrain from editorializing. The Court reasoned that, because editorializing is a right protected by the First Amendment, the government could not condition funding on a station’s decision to surrender that right. Id. at 400-02. To allow the government to condition the receipt of funds on a waiver of First Amendment rights would unconstitutionally allow the government to punish those broadcasters who retained their First Amendment rights and coerce them into waiving their First Amendment rights. Id.; see also Rosenberger v. Rectors & Visitors of the

Univ. of Va., 515 U.S. 819 (1995) (public university could not condition grant of funds on student group's waiver of its First Amendment right to publish religious periodical).

The Cigarette Fee Act is essentially the same as the statute held unconstitutional in Speiser. Indeed, the principle of Speiser, that the government may not condition a tax exemption on the surrender of First Amendment rights, compels a ruling that the Cigarette Fee Act is unconstitutional. The Cigarette Fee Act violates the First Amendment because it exempts from taxation only those products made by manufacturers that have surrendered their First Amendment rights to advertise, petition the government, and access the courts. See Speiser, 357 U.S. at 518. As the Court explained in Speiser, “[t]o deny [a tax] exemption to [parties] who engage in certain forms of speech is in effect to penalize them for such speech. Its deterrent effect is the same as if the State were to fine them for this speech,” and it is therefore unconstitutional. Id.; see also Perry, 408 U.S. at 597. Indeed, the only way that non-settling tobacco manufacturers such as Appellants can avoid the Tax on their products is to enter into an agreement with the State surrendering certain of their First Amendment rights.⁶ “Such interference with constitutional rights is impermissible.” Perry, 408 U.S. at 597.

⁶ Whether the amount required to settle with the State is more or less than the Tax is irrelevant. See infra pp. 27-30. The fact is that non-settling manufacturers are being singled out, and their products are being taxed, until and unless they waive their First Amendment rights.

C. The State's Attempt to Impose First Amendment Restrictions Indirectly by Offering Them As An "Alternative" to the Tax Is Just As Unconstitutional as it Would be for the State to Impose the Restrictions Directly.

The Settlement Agreement between the State and the Majors imposes numerous restrictions on the Majors' constitutionally-protected First Amendment rights. The Settlement Agreement limits the Majors' ability to oppose certain legislation impacting the tobacco industry, effectively relinquishing the Majors' constitutional right to petition the government. The Settlement Agreement also restricts the Majors' commercial speech rights, including a ban on advertising on billboards, buses, taxis and bus shelters, a ban on making payments to movie and television producers for product placement, and a ban on distributing promotional items, such as hats and t-shirts, bearing their products' brand names. Further, the Settlement Agreement limits the Majors' constitutionally protected right of access to the courts by restricting their ability to challenge the constitutionality and validity of certain laws regulating tobacco. These restrictions on the rights to lobby, advertise and access the courts would be unconstitutional if imposed directly by the State.

It is well-settled that lobbying restrictions of the sort contained in the Settlement Agreement are unconstitutional. These lobbying restrictions regulate pure political speech, which is afforded the highest possible protection under the First Amendment. See 44 Liquormart, Inc. v. Rhode Island, 517 U.S. 484, 498 (1996) (suppression of political speech is justified only by an emergency). The right to lobby, which is part of the overall right to petition the government for a redress of grievances, "extends to all departments of the Government," California Motor Transport Co. v. Trucking Unlimited,

404 U.S. 508, 510 (1972), and is considered “core” political speech protected by the First Amendment. E. R.R. Presidents Conference v. Noerr Motor Freight, Inc., 365 U.S. 127, 139 (1961). Indeed, the United States Supreme Court has long “recognized this right to petition as one of the most precious of the liberties safeguarded by the Bill of Rights.” BE&K Constr. Co. v. NLRB, 536 U.S. 516, 524 (2002) (internal quotation omitted). Thus, there is no doubt that, if the lobbying restrictions contained in the Settlement Agreement were imposed directly by the State, they would be unconstitutional.

Likewise, if imposed directly by the State, the commercial speech restrictions contained in the Settlement Agreement would be unconstitutional. In fact, in Lorillard Tobacco Co. v. Reilly, 533 U.S. 525 (2001), the United States Supreme Court held that advertising restrictions nearly identical to those contained in the Settlement Agreement violated the First Amendment. Id. at 554. The restrictions at issue in Lorillard forbade outdoor tobacco advertising within a 1,000-foot radius of a school or playground and prohibited indoor, point-of-sale advertising “lower than five feet from the floor of any retail establishment which is located within a one thousand foot radius of” any school or playground. Id. at 535-36. The Court ruled that the first restriction, which constituted nearly a total ban on outdoor advertising in certain cities, was more extensive than necessary to serve the state’s interest in curbing underage smoking. Id. at 561-66. The Court held that the second restriction also was unconstitutional, finding that the 5-foot limit did not advance the state’s goal in preventing minors from using tobacco products, since “[n]ot all children are less than 5 feet tall, and those who are certainly have the ability to look up and take in their surroundings.” Id. at 566.

The restrictions on access to the courts to challenge certain laws regulating tobacco contained in the Settlement Agreement would also be unconstitutional if imposed directly by the State. The right of access to the courts to challenge the constitutionality or validity of a law is a central aspect of the First Amendment's right to "petition the government for a redress of grievances." California Motor, 404 U.S. at 510, 513. The Settlement Agreement restricts this access because the Majors agreed not to "challenge the enforceability or constitutionality of certain laws regarding cigarettes." (APP. 139.)

In sum, the restrictions on lobbying, commercial speech, and access to the courts contained in the Settlement Agreement would be unconstitutional if imposed directly by the State. The State does not dispute this; indeed, the State expressly conceded in the District Court that the Cigarette Fee Act exempts only those manufacturers that have agreed "to curtail specified *First Amendment* activities." (APP. 227) (emphasis added). As a result, the State cannot condition the avoidance of the 35 cent per pack Tax on Appellants' agreement to surrender their First Amendment rights. Speiser, 357 U.S. at 518; Perry, 408 U.S. at 597; League of Women Voters, 468 U.S. at 400-02. Similarly, the State cannot punish Appellants by subjecting their products to the Tax based on Appellants' refusal to waive these fundamental constitutional rights. Id.

D. The Court of Appeals Erroneously Ruled that the Cigarette Fee Act is Constitutional.

The Court of Appeals erroneously ruled that the Cigarette Fee Act is constitutional because it has a "legitimate purpose" and "it is not a direct attempt to regulate speech." (APP. 361); 685 N.W.2d at 473. This ruling is directly contrary to United States

Supreme Court precedent. First, the Court has “long recognized that even regulations aimed at proper governmental concerns can restrict unduly the exercise of rights protected by the First Amendment.” Minneapolis Star, 460 U.S. at 592. This is understandable since government restrictions on speech are often presumed to be well-intentioned. Thus, the fact that the Cigarette Fee Act purports to serve several legitimate government purposes is irrelevant to whether the statute violates the First Amendment. Id.

Second, the Court of Appeals erred in ruling that the Cigarette Fee Act was constitutional because it was not a direct attempt to regulate speech. It is an undisputed and stipulated fact that unless and until Appellants surrender certain of their fundamental First Amendment rights, their products are subject to the Tax. Accordingly, the Cigarette Fee Act certainly appears to be a direct attempt to regulate speech.

Regardless of whether the Cigarette Fee Act is a direct attempt to regulate speech, it is still unconstitutional. As the Court of Appeals itself recognized, the government “may not condition a tax exemption on the renunciation of an individual’s right to free speech.” (APP. 360); 685 N.W.2d at 472; Speiser, 357 U.S. at 518; Perry, 408 U.S. at 597. In this case, that is exactly what the State has done: the Tax exemption contained in the Cigarette Fee Act is expressly conditioned on a party surrendering certain of their First Amendment rights. Thus, the statute is unconstitutional. Id.

The Court of Appeals’ reliance on Regan v. Taxation With Representation of Washington, 461 U.S. 540 (1983), is misguided. Rather than supporting a ruling that the Cigarette Fee Act is constitutional, Regan actually supports Appellants’ argument that the

Cigarette Fee Act violates the First Amendment. In Regan, the United States Supreme Court explained that, “although government may not place obstacles in the path of a person’s exercise of freedom of speech, it need not remove those not of its own creation.” 461 U.S. at 549-550 (internal quotation and alterations omitted). The Court upheld the statute in Regan because, while the government had chosen not to subsidize lobbying, it had placed no impediments to the plaintiff’s First Amendment right to lobby. Here, in contrast, the government has placed obstacles and impediments directly in the path of Appellants’ exercise of their First Amendment rights through the Cigarette Fee Act. The State has imposed a tax on the exercise of free speech and other First Amendment rights. The Cigarette Fee Act’s Tax on Appellants’ products effectively conditions Appellants’ retention of their First Amendment rights on Appellants’ products being taxed. Thus, this case does not concern a failure by the State to remove obstacles not of its own creation – it involves the State affirmatively creating and placing obstacles squarely in the path of Appellants’ exercise of their First Amendment rights. As such, the Cigarette Fee Act is unconstitutional.

E. Whether Non-Settling Manufacturers Would be Subject to a “Similar” Financial Burden under a “Voluntary” Waiver of Rights is Irrelevant.

The State has argued that the Cigarette Fee Act does not violate the First Amendment because Appellants would be subject to “similar” financial burdens if they agreed to waive their First Amendment rights under the “voluntary” agreement authorized by the statute. In effect, the State argues that Appellants should be happy that their products are taxed at 35 cents per pack because Appellants’ only alternative under

the statute, i.e. to agree to restrictions on their First Amendment rights, results in Appellants having to pay the State 48 cents per pack. However, this argument ignores the fact that those manufacturers who have already waived their First Amendment rights are exempt from the Tax. Thus, the undisputed fact remains that the Cigarette Fee Act draws an explicit distinction and imposes the Tax based on whether the manufacturer has relinquished its First Amendment rights. As such, the statute is unconstitutional.

This Court should reject any argument by the State based on an alleged comparison of the burdens of the Tax versus the burdens of a “voluntary” agreement authorized by the Cigarette Fee Act. Indeed, in Minneapolis Star & Tribune Co. v. Minnesota Commissioner of Revenue, 460 U.S. 575 (1983), Minnesota made exactly such an argument, and the United States Supreme Court rejected it. Specifically, the State argued that a tax, which singled out newspapers for different treatment than other businesses, actually favored the press over other businesses and therefore did not violate the First Amendment. Id. at 588. The Court found this argument meritless, explaining that it “would be hesitant to fashion a rule that automatically allowed the State to single out the press for a different method of taxation as long as the effective burden was no different from that on other taxpayers or the burden on the press was lighter than that on other businesses.” Id. The Court reasoned that singling out entities based on their exercise of First Amendment rights threatens such entities “not only with the current *differential* treatment, but also with the possibility of subsequent differentially *more burdensome* treatment.” Id. (emphasis in original). The Court also noted that “courts as institutions are poorly equipped to evaluate with precision the relative burdens of various

methods of taxation” and, given the potential threat to First Amendment rights, the Court could not “tolerate th[e] possibility” of miscalculating the relative burdens. Id. at 589.

Contrary to the State’s arguments, the Cigarette Fee Act does not merely offer a “voluntary” waiver of First Amendment rights. Rather, the statute attempts to force small tobacco manufacturers to waive their First Amendment rights by offering such a waiver as the only alternative to the Tax. Under such circumstances, First Amendment rights cannot constitutionally be waived, irrespective of whether the State chooses to characterize the waiver as “voluntary.” See, e.g., O’Hare Truck Serv., Inc. v. City of Northlake, 518 U.S. 712, 716 (1996) (“A State may not condition public employment on an employee’s exercise of his or her First Amendment rights.”).

In any event, there is no basis for the State’s claim that Appellants are better off paying the Tax and not waiving their First Amendment rights. Initially, it should be noted that the State itself appears to be unclear on the amount that Appellants would have to pay under a “voluntary” agreement authorized by the statute. The State initially represented to the District Court that manufacturers entering agreements with the State would be required to pay 36 cents per pack. (APP. 248.) This amount subsequently increased to 48 cents per pack in the parties’ stipulation. (APP. 175, 260.) This imprecision in the State’s calculation exemplifies the concern the Supreme Court outlined in Minneapolis Star & Tribune and demonstrates why this Court should reject such an analysis. “The complexities of factual economic proof always present a certain potential for error, and courts have little familiarity with the process of evaluating the relative economic burden of taxes.” Minneapolis Star & Tribune, 460 U.S. at 589. “Taking the

chance that [the State's calculations] or others like them are erroneous is a risk that the First Amendment forbids." Id. at 590 n.14.

The State's comparison of the alleged 48 cent per pack payment under the "voluntary" agreement authorized by the statute and the 35 cent per pack Tax mandated by the Cigarette Fee Act is also flawed because it ignores the "value" of First Amendment rights and the "cost" of waiving those rights. By entering into the "voluntary" agreement, the manufacturer makes the formulated payments to the State on each pack sold and incurs the "cost" of waiving its First Amendment rights in exchange for a release from civil liability for any claims relating to its sale of cigarettes. Non-settling manufacturers such as Appellants incur the burden of the Tax imposed under the Cigarette Fee Act and retain the "value" of their First Amendment rights, while receiving none of the civil liability protections granted under the release in the "voluntary" settlement. Thus, it is difficult, if not impossible, for a court to determine which of these "choices" has either the greater inherent value or economic benefit for cigarette manufacturers, let alone to evaluate the level of coercion imposed on such manufacturers. The only thing that is clear is that the Cigarette Fee Act, just as the tax law that was struck down in Star Tribune, unconstitutionally singles out and taxes certain businesses based on their First Amendment rights.

F. Caselaw Addressing Challenges to Qualifying Statutes are Irrelevant to Evaluating the Constitutionality of the Cigarette Fee Act.

Caselaw addressing challenges to the Qualifying Statutes that have been enacted in other states are irrelevant in evaluating the constitutionality of the Cigarette Fee Act

because of the fundamental differences between these Qualifying Statutes and the Cigarette Fee Act.

The Qualifying Statutes require non-participating cigarette manufacturers to make payments into an interest bearing escrow account, roughly equivalent to payments that would be required if these manufacturers had joined the Master Settlement Agreement. These escrow payments remain the property of the non-participating manufacturers and the manufacturers are entitled to the return of all such escrow payments with interest unless and until they are held liable for damages caused by their conduct. Thus, these manufacturers do not and will not lose ownership of these escrowed funds unless and until the particular state establishes that the manufacturer is liable for damages caused by its conduct.

In contrast, the Cigarette Fee Act imposes a direct Tax on only those cigarettes made by non-settling manufacturers who have refused to surrender their First Amendment rights, and exempts all cigarettes made by manufacturers who have waived their First Amendment rights. The Tax is not refundable; the manufacturers will not receive the return of these funds under any circumstances; the State never has to establish that the manufacturer is liable; and the Tax payments go directly into the State's General Fund without any requirement that the State establish the non-settling manufacturers' liability.

The District Court erroneously relied on PTI, Inc. v. Philip Morris, Inc., 100 F. Supp. 2d 1179 (C.D. Cal. 2000), a case concerning California's escrow estate, to hold that the Cigarette Fee Act is constitutional. In PTI, the court addressed the

enforceability of California's Qualifying Statute, which required cigarette manufacturers to either become a signatory to the Master Settlement Agreement, including agreeing to the MSA's advertising and lobbying restrictions, or make annual payments into an escrow account. In arguing that the statute unconstitutionally coerced them into foregoing their First Amendment rights, the cigarette manufacturers highlighted that, while the escrow payments were not deductible under state and federal income tax laws, in contrast the settlement payments under the MSA that were deductible. The escrow payments were not deductible under the state and federal tax laws because the manufacturers retained ownership of the payments. The court explained that the unfavorable tax treatment of the escrow payments was imposed pursuant to generally applicable tax laws that were "wholly separate" from the Qualifying Statute's escrow payment obligations. *Id.* at 1206-07. Therefore, the court rejected plaintiffs' First Amendment challenge because the unfavorable tax treatment of the escrow payments was not based on whether the manufacturer had waived its First Amendment rights, but was instead based on generally applicable tax laws unrelated to the Master Settlement Agreement.

In contrast to the Qualifying Statute in PTI, the Tax imposed by the Cigarette Fee Act is not based on the application of an independent statute or regulation; instead, the unfavorable tax treatment is the Cigarette Fee Act's Tax itself which is imposed based on whether a cigarette manufacturer has waived its First Amendment rights. Moreover, unlike the escrow mechanism upheld in PTI, in which escrow payments are refunded to the manufacturer with interest if no liability is determined, the Tax under the Cigarette

Fee Act must be paid and will not be refunded regardless of whether the manufacturer is ever deemed liable for any damages.

The District Court's and the State's reliance on Star Scientific, Inc. v. Beales, 278 F.3d 339 (4th Cir. 2002), is similarly misplaced. Significantly, the court in Star Scientific did not even address any First Amendment arguments; the court instead rejected an inference that the Virginia Qualifying Statute was intended to coerce non-participating manufacturers into joining the Master Settlement Agreement because such an intention was not among the statute's expressly stated purposes. See id. at 349-50.

In this case, however, no such inference is necessary because the Cigarette Fee Act's text shows that the intent of the statute is to encourage manufacturers to waive their First Amendment rights. The Cigarette Fee Act imposes the Tax because the manufacturer has not waived its First Amendment rights. Likewise, the statute's express terms provide that a manufacturer can obtain an exemption from the Tax only if it waives its First Amendment rights. Therefore, unlike in Star Scientific, this Court need not infer the legislature's intent; the legislature's intent to target First Amendment rights is apparent from the face of the statute.

Moreover, as noted above, PTI, Star Scientific, and the other cases addressing Qualifying Statutes are wholly irrelevant because these cases dealt with the payment of funds into an escrow account that were fully refundable with interest, whereas the instant case involves the payment of a tax that will not be refunded under any circumstances.

In sum, the Cigarette Fee Act violates the First Amendment by taxing only those products made by manufacturers who have refused to waive their First Amendment rights and exempting products made by those manufacturers who have surrendered their First Amendment rights. This unconstitutionally singles out and taxes Appellants and other non-settling manufacturers for their refusal to waive their First Amendment rights. The fact that the statute purports to serve legitimate purposes or somehow does not “directly” regulate speech is irrelevant. Neither the State’s faulty comparison of the burden of the Tax and “voluntary” agreements authorized by the Cigarette Fee Act, nor its reliance on distinguishable caselaw upholding Qualifying Statutes can save the Cigarette Fee Act.

II. THE CIGARETTE FEE ACT VIOLATES THE EQUAL PROTECTION CLAUSE AND THE UNIFORMITY CLAUSE BECAUSE IT DISCRIMINATES AGAINST CERTAIN CIGARETTE MANUFACTURERS BASED ON WHETHER THEY HAVE WAIVED FUNDAMENTAL CONSTITUTIONAL RIGHTS.

The Cigarette Fee Act violates the Equal Protection Clause of the Fourteenth Amendment to the United States Constitution,⁷ and the Uniformity Clause of the Minnesota Constitution⁸ because it discriminates against Appellants and other non-settling manufacturers based on their refusal to waive their fundamental

⁷ The Fourteenth Amendment to the United States Constitution provides: “No state shall make or enforce any law which shall . . . deny to any person within its jurisdiction the equal protection of the laws.” “It is well established that a corporation is a ‘person’ within the meaning of the Fourteenth Amendment.” Metro. Life Ins. Co. v. Ward, 470 U.S. 869, 881 n. 9 (1985).

⁸ Similar to the Equal Protection Clause, Article X, section 1 of the Minnesota Constitution, referred to as the Uniformity Provision, mandates that “[t]axes shall be uniform upon the same class of subjects.” “It is established in Minnesota that the uniformity provision of the state constitution is no more restrictive upon the legislature’s power to tax or classify than is the equal protection clause in the Fourteenth Amendment to the United States Constitution.” Westling v. County of Mille Lacs, 581 N.W.2d 815, 820 (Minn. 1998). Thus, “[t]he same test is used for both analyses.” Id.

constitutional rights. The “equal protection clause protects the individual from state action which selects him out for discriminatory treatment by subjecting him to taxes not imposed on others of the same class.” Hillsborough v. Cromwell, 326 U.S. 620, 623 (1946). The Cigarette Fee Act violates equal protection because it burdens fundamental rights by applying the Tax only to products made by manufacturers that have refused to surrender their First Amendment rights.

The proper test to be applied to a tax under the Equal Protection Clause, and therefore the Uniformity Clause as well, depends on whether the tax is based on a suspect classification (such as race), or seeks to limit or burden the exercise of the taxpayer’s constitutional rights (such as freedom of speech). If the tax is not imposed based on a suspect classification or does not limit or burden fundamental constitutional rights, it is generally evaluated under the rational basis test. See Minneapolis Star & Tribune Co. v. Minn. Comm’r of Revenue, 460 U.S. 575, 582-83 (1983). However, in situations such as the instant case where a tax limits or burdens the exercise of a constitutional right, the statute must “satisfy strict scrutiny.” See City of Cleburne v. Cleburne Living Ctr., 473 U.S. 432, 440 (1985); Granville v. Minneapolis Pub. Sch., 668 N.W.2d 227, 230 (Minn. Ct. App. 2003). Under strict scrutiny, a statute’s classifications “are constitutional only if they are narrowly tailored measures that further compelling government interests.” Adarand Contractors, Inc. v. Pena, 515 U.S. 200, 227 (1995).

For example, in Minneapolis Star & Tribune, the Supreme Court applied strict scrutiny and struck down a Minnesota state tax which unconstitutionally burdened First Amendment rights. 460 U.S. at 592-93. The case involved Minnesota’s use tax on the

cost of paper and ink products consumed in the production of periodic publications. The Court held that a “tax that burdens rights protected by the First Amendment cannot stand unless the burden is necessary to achieve an overriding governmental interest.” Id. at 582. The Court further held that the State’s asserted interest in raising revenue—an interest “critical to any government”—was insufficient to justify the differential treatment because the State “could raise the revenue by taxing businesses generally” and thereby avoid a tax that restricts First Amendment rights. Id. at 586. Accordingly, the Court held the statute was unconstitutional.

The analysis and holding in Minneapolis Star & Tribune apply to this case and compel a ruling that the Cigarette Fee Act is unconstitutional. As with the statute in Minneapolis Star & Tribune, the Cigarette Fee Act is subject to strict scrutiny because it burdens Appellants’ First Amendment rights. The Cigarette Fee Act taxes Appellants’ and other manufacturers’ products based on their refusal to relinquish their First Amendment rights, in contrast to manufacturers who have waived their First Amendment rights and whose products are therefore exempt from the Tax. As with the statute in Minneapolis Star & Tribune, the Cigarette Fee Act fails the strict scrutiny test because it is not narrowly tailored to further a compelling government interest.

A tax is subject to strict scrutiny if it makes distinctions based on the exercise of fundamental constitutional rights, such as free speech rights. The Cigarette Fee Act makes precisely such a distinction by conditioning the imposition of the Tax on whether a cigarette manufacturer has surrendered its First Amendment rights. Products made by those manufacturers that have refused to waive their First Amendment rights are subject

to the Tax, and products made by those manufacturers that have waived their First Amendment rights are exempt from the Tax. Thus, non-settling manufacturers, including Appellants, are subject to the Tax on their products because they have refused to waive their First Amendment rights.⁹ Accordingly, because the Tax presents the non-settling manufacturers with the Hobson's Choice of either foregoing their First Amendment rights or having their products subject to Tax, the Cigarette Fee Act is subject to strict scrutiny. See Minneapolis Star & Tribune, 460 U.S. at 592-93.

The State has never argued that the Cigarette Fee Act can survive strict scrutiny. Indeed, the State could not establish that the Cigarette Fee Act survives such heightened scrutiny because the statute is not narrowly tailored to serve a compelling state interest. All of the State's claimed purposes for enacting the Cigarette Fee Act could be achieved through legislation that does not punish Appellants and other non-settling manufacturers for refusing to surrender their First Amendment rights or seek to coerce Appellants and other non-settling manufacturers into waiving their First Amendment rights. For example, the State could increase the general excise tax on all cigarettes, could fund programs designed to reduce smoking, or could more aggressively police underage sales. There are, of course, numerous other ways that the State could seek to decrease smoking, especially by minors, without burdening Appellants' First Amendment rights.

⁹ Unlike the *Majors*, which the State of Minnesota alleged committed fraud, falsely advertised their products and violated anti-trust laws while engaged in a "unified campaign of deceit and misrepresentation" to conceal information regarding the health effects of smoking, the State has not alleged, and cannot establish, similar conduct on the part of Appellants or other non-settling manufacturers. Without engaging in culpable conduct, which has not been alleged by the State, Appellants cannot lawfully be punished merely for selling cigarettes, which conduct is entirely lawful. See FDA v. Brown & Williamson Tobacco Corp., 529 U.S. 120, 138-39 (2000).

The Cigarette Fee Act also violates the Uniformity and Equal Protection clauses because it arbitrarily and unfairly distinguishes among cigarette manufacturers in imposing the Tax. In National Tea Co. v. State, 205 Minn. 443, 286 N.W. 360 (1939),¹⁰ this Court held unconstitutional a sales tax which imposed different rates of taxation on stores selling the same merchandise based solely on the merchant's sales volume. As this Court explained, the law taxed "different persons" at "different rates" for the "privilege of doing the same act." Id. at 361. Accordingly, this Court held that the tax was arbitrary, unfair, and unequal, and that it therefore violated the Uniformity Clause. Id.

The Cigarette Fee Act is indistinguishable from the tax struck down in National Tea. As in National Tea, the Cigarette Fee Act imposes a different tax on "different persons" for the "privilege of doing the same act," and "different owners are taxed at different rates for performing the same acts." Id. at 361. There is no rational, legitimate difference between the products sold by the Majors and the products sold by non-settling manufacturers such as Appellants. Both groups manufacture and sell the same product — cigarettes. The only difference is that the Majors agreed to make annual payments to the State and to surrender their First Amendment rights pursuant to the Settlement Agreement to avoid liability for fraud, false advertising, and anti-trust violations. No such allegations have ever been made, let alone proven, by the State

¹⁰ This Court issued two opinions over two years in National Tea. First, in 1939, this Court ruled that a state statute imposing a sales tax which varied from .05% to .85% of a sale based on the merchant's volume was unconstitutional because it was arbitrary, unequal and discriminatory. 205 Minn. at 449, 286 N.W. at 363. Following remand from the United States Supreme Court, the Minnesota Supreme Court clarified that the sales tax violated the Uniformity Clause of the Minnesota Constitution. 208 Minn. 607, 608, 294 N.W. 230, 231 (1940).

against Appellants or any other non-settling manufacturers. As such, the Cigarette Fee Act is arbitrary, unfair, unequal, and irrational, and it is therefore unconstitutional under the Equal Protection Clause and the Uniformity Clause. Id.

Appellants do not challenge the State's ability to tax cigarettes, so long as all cigarette manufacturers are treated equally. However, the State cannot tax certain manufacturers' products and exempt others when there is no reasonable basis for the distinction. In this regard, the District Court's analogy between the Cigarette Fee Act and general taxes on liquor and other license fees is misplaced because all liquor manufacturers are taxed equally without regard for who made the beer, wine, or spirits. The liquor taxes and license fees are constitutional because they apply equally. The Cigarette Fee Act, by contrast, exempts only certain companies without any reasonable basis. Cigarette manufacturers' products are not taxed equally; they are taxed disparately based on whether the manufacturer has agreed to surrender its First Amendment rights. If the State wants to tax cigarettes, it can tax cigarettes generally without violating the Equal Protection Clause. However, the State should not be allowed to use its taxing power to attack and penalize certain manufacturers for their refusal to waive their First Amendment rights.

The District Court erroneously relied upon two lower federal court decisions addressing challenges to Qualifying Statutes in rejecting Appellants' equal protection claims. (APP. 296-302) (citing Star Scientific, Inc. v. Beales, 278 F.3d 339 (4th Cir. 2002); PTI, Inc. v. Philip Morris, Inc., 100 F. Supp. 2d 1179 (C.D. Cal. 2000)). However, as discussed above, these cases are inapplicable to Appellants' challenges

because the Qualifying Statutes are fundamentally different than the Cigarette Fee Act. The Qualifying Statutes require escrow payments that are returned to the manufacturer, whereas the Cigarette Fee Act imposes non-refundable taxes.

III. THE CIGARETTE FEE ACT VIOLATES THE BILL OF ATTAINDER CLAUSES OF THE UNITED STATES AND MINNESOTA CONSTITUTIONS BECAUSE IT PENALIZES APPELLANTS FOR PURPORTED CONDUCT WHICH HAS NEVER BEEN ALLEGED OR PROVED BY THE STATE.

The Cigarette Fee Act violates the Bill of Attainder Clauses of the United States and Minnesota Constitutions¹¹ because it penalizes Appellants and other non-settling manufacturers for purported conduct which has never been alleged or proved by the State. The context in which the Cigarette Fee Act was enacted demonstrates that it violates the Bill of Attainder Clauses. The statute was enacted only as a consequence of Minnesota's settlement of the State Tobacco Lawsuit against the Majors, a lawsuit based on the Majors' fraud, false advertising and anti-trust violations. Without that lawsuit, and the settlement thereof, the Cigarette Fee Act never would have been enacted. By passing the Cigarette Fee Act, the State is admittedly seeking to impose those same settlement costs on Appellants without allowing Appellants access to the judicial process received by the Majors in the State Tobacco Lawsuit. By seeking to impose those same settlement costs on Appellants, the State has legislatively judged Appellants and other non-settling manufacturers guilty of the Majors' transgressions, without giving Appellants the

¹¹ Article I, Section 11 of the United States Constitution provides that: "No state shall . . . pass any Bill of Attainder." Similarly, the Minnesota Constitution provides that "no bill of attainder . . . shall be passed." Minn. Const. art. I, § 11. In determining whether a statute violates the Minnesota Constitution's or the United States Constitution's prohibitions against bills of attainder, the Minnesota Supreme Court applies the same analysis. See Reserve Mining Co. v. State, 310 N.W. 487, 490-92 (Minn. 1981).

opportunity to rebut these charges in court. Presumably, the State enacted the Cigarette Fee Act after determining that a similar lawsuit against Appellants and other non-settling manufacturers would be unsuccessful. Such a legislative attempt to circumvent the judicial process renders the statute an unconstitutional bill of attainder.¹²

A bill of attainder is “a law that legislatively determines guilt and inflicts punishment upon an identifiable individual without provision of the protections of a judicial trial.” Nixon v. Adm’r of Gen. Servs., 433 U.S. 425, 468 (1977). The prohibition against bills of attainder forbids state legislatures from assuming judicial functions or conducting trials. United States v. Brown, 381 U.S. 437, 442 (1965). This provision was included in the Constitution “not as a narrow, technical (and therefore soon to be outmoded) prohibition, but rather as an implementation of the separation of powers, a general safeguard against legislative exercise of the judicial function, or more simply – trial by legislature.” Id.

A law is an unconstitutional bill of attainder if it: (1) applies to designated individuals or groups; and (2) imposes punishment. Nixon, 433 U.S. at 474. The Cigarette Fee Act is an unconstitutional bill of attainder under this two-part analysis.

First, the Tax applies only to designated entities—all cigarette manufacturers that did not participate in the Settlement Agreement and surrender their First Amendment rights. See Brown, 381 U.S. at 450 (statute that did not “set forth a generally applicable

¹² The Cigarette Fee Act itself makes clear that the only way cigarette manufacturers can avoid the Tax is to enter into a settlement with the State “similar” to the Majors’ Settlement Agreement. Unlike the Majors’ settlement, which came by way of the judicial process, the “similar” settlement is imposed upon Appellants and other non-settling manufacturers by legislative fiat.

rule . . . and leave to courts and juries the job of deciding what persons . . . possess the specified characteristics” violated the Bill of Attainder Clause). The number of such manufacturers is not relevant to the analysis. A bill of attainder may apply to “relatively large groups of people, sometimes by description rather than name.” Id. at 461.

Second, the Cigarette Fee Act inflicts punishment on Appellants and other non-settling manufacturers. In determining whether a statute inflicts forbidden punishment under the Bill of Attainder Clause, courts examine whether: (1) the statute falls within the historical meaning of legislative punishment; (2) the statute “can reasonably be said to further nonpunitive legislative purposes”; and (3) the legislative record “evinces a congressional intent to punish.” Nixon, 433 U.S. at 473, 475-76, 478.

In this case, while nominally designated as a “fee,” the Tax imposed by the Cigarette Fee Act is in effect a fine that punishes Appellants and non-settling manufacturers for their purported conduct—conduct similar to that alleged against the Majors, but neither asserted nor proved with respect to Appellants. See Carmichael v. S. Coal & Coke Co., 301 U.S. 495, 508 (1937) (“The particular name which a . . . legislature may give to a money payment commanded by its statute is not controlling here when its constitutionality is in question.”). As Chief Justice John Marshall famously stated, “the power to tax involves the power to destroy.” M’Culloch v. Maryland, 17 U.S. (4 Wheat.) 316, 431 (1819). The State sued the Majors based on their past conduct, and the Majors settled with the State to avoid liability for such conduct, including potential punitive damages. The State has now exercised the “power to

destroy” by imposing the Tax to punish Appellants for similar conduct that has neither been alleged nor proven. Id.

The fact that the Tax constitutes a punishment is unquestionable. The State itself refers to the Majors’ settlement payments as “*retribution payments.*” See Minnesota Department of Human Services, Chemical Health Division, Annual Synar Report FFY 2003, at 4, available at http://www.dhs.state.mn.us/main/groups/disabilities/documents/pub/dhs_id_003465.hcsp, (visited December 12, 2004) (emphasis added). The State has also conceded that the purpose of the Cigarette Fee Act and similar statutes passed pursuant to the Master Settlement Agreement is to “encourage other [non-settling] manufacturers to *settle*” with the State. (APP. 210, 214.) (emphasis added). In addition, the statute expressly provides that the Tax is imposed upon non-settling manufacturers in an effort to force them to remit payments that are “similar” to the payments the Majors are making to the State. Of course, the Majors are making such payments because they sought to avoid potential liability for compensatory, treble and punitive damages. Given that the impetus for the Cigarette Fee Act was to prompt a settlement by small tobacco manufacturers—without affording such manufacturers any of the rights in the judicial process to which the Majors were given full access—it is clear that the Cigarette Fee Act

is “a law that legislatively determines guilt and inflicts punishment upon an identifiable [group] without provision of the protections of a judicial trial.” Nixon, 433 U.S. at 468.¹³

The Cigarette Fee Act is expressly designed to punish non-settling manufacturers for allegedly engaging in the same conduct for which the State originally sued the Majors. The State has singled out the non-settling manufacturers because the Majors who engaged in fraud and false advertising are purportedly already paying their “fair share” to the State pursuant to the Settlement Agreement. The State enacted the Tax because it is far easier to simply mandate payments by legislative fiat than it is to establish, through the judicial process, that the non-settling manufacturers engaged in conduct giving rise to legal liability. However, the Bill of Attainder Clause prohibits the State from acting as prosecutor, judge and jury in this fashion.

The Minnesota Legislature expressly provided in the Cigarette Fee Act that the State was imposing the Tax to “ensure that manufacturers of nonsettlement cigarettes pay” the same penalties the Majors are paying as a result of the State Tobacco Lawsuit. The punitive sanction imposed by the State is the Tax itself, which is nothing more than a fine intended to roughly approximate the retribution payments being made by the Majors pursuant to the Settlement Agreement. Thus, there is a clear legislative “intent to punish”

¹³ The District Court suggested that Appellants have not been deprived of the judicial process received by the Majors, stating that Appellants “have had their day in court. They have been allowed to argue their points clearly.” (APP. 309.) The fact that Appellants have been heard on their constitutional claims in this proceeding, however, does not remedy the deprivation of their rights in the judicial process suffered by Appellants as to any claim the State may have for payments for smoking-related damages. As discussed above, the Majors received the benefits of the judicial process as to such claims, and settled these claims on mutually agreeable terms. Appellants and other non-settling manufacturers have received no such opportunity.

the non-settling manufacturers in the Cigarette Fee Act in the same manner the State Tobacco Lawsuit sought to punish the Majors.

The Court of Appeals and District Court erroneously ruled that the Cigarette Fee Act does not violate the Bill of Attainder Clause because it purportedly applies only to future activities, suggesting that Appellants can avoid the Tax by either: (1) “voluntarily” terminating their sales of cigarettes in the State; or (2) “voluntarily” settling with the State and agreeing to pay a “similar” amount. This analysis defies logic and is at odds with the Constitution.

The United States Supreme Court has repeatedly held that, “[w]hen past activity serves as ‘a point of reference for the ascertainment of particular persons ineluctably designated by the legislature’ for punishment, the Act may be an attainder.” Selective Serv. Sys. v. Minn. Pub. Interest Research Group, 468 U.S. 841, 847 (1984) (quoting Cummings v. Missouri, 71 U.S. (4 Wall.) 277, 324 (1866)). Appellants’ past activity—failing to relinquish their First Amendment rights and make annual settlement payments to the State—serves as the *only* basis for the Tax.¹⁴ The fact that Appellants have the “option” of “voluntarily” agreeing to pay an amount similar to the Tax or terminating their sales of cigarettes to “avoid” the Tax has no constitutional significance. If it did, state legislatures could render every statute immune from scrutiny under the Bill of

¹⁴ Contrary the State’s claim, Appellants’ “prospective” sale of cigarettes in the future does not form the basis for the Tax. Appellants and the Majors engage in the same “prospective” conduct: selling cigarettes in Minnesota. However, the Tax is not imposed because of this prospective conduct; it is imposed based on a manufacturer’s past conduct—whether it has relinquished its First Amendment rights and is paying amounts in settlement of the State’s claims of unlawful conduct.

Attainder Clause merely by including a provision allowing parties to “voluntarily” agree to cease their lawful conduct in the future to avoid the punishment inflicted by the law. Of course, this is not the law. See Brown, 381 U.S. at 449-52, 458-59 (holding unconstitutional as a bill of attainder a federal law that prospectively denied members of communist party from holding a leadership position in a union even though the individuals could have voluntarily sought a different position); United States v. Lovett, 328 U.S. 303, 315-16 (1946) (holding unconstitutional as a bill of attainder a federal law that prospectively denied certain government employment to certain individuals even though the individuals could have voluntarily sought different employment); Cummings v. Missouri, 71 U.S. (4 Wall.) 277 (1866) (holding unconstitutional as a bill of attainder a state law requiring persons to take a loyalty oath as a prerequisite to continuing to practice a profession, even though the individuals could have voluntarily ceased practicing their profession in Missouri); Nixon, 433 U.S. at 476 n.40 (“[P]unishment is not restricted purely to retribution for past events, but may include inflicting deprivations on some blameworthy or tainted individual in order to prevent his future misconduct.”) (citing Brown, 381 U.S. at 458-59).

Indeed, by arguing that Appellants can avoid the Tax by ceasing to sell cigarettes in Minnesota, the State demonstrates that the Cigarette Fee Act also seeks to “banish” Appellants from the State. “Banishment,” however, is one of the historical forms of impermissible legislative punishment barred by the Bill of Attainder Clause. Nixon, 433 U.S. at 474. Thus, this does not save the Cigarette Fee Act from being a bill of attainder; instead, it is further proof that the statute is an unconstitutional bill of attainder.

Finally, the District Court erroneously relied upon PTI, Inc. v. Philip Morris, Inc., 100 F. Supp. 2d 1179 (C.D. Cal. 2000), in upholding the Cigarette Fee Act against Appellants' bill of attainder challenge. PTI is readily distinguishable from the instant case. The court in PTI held that California's Qualifying Statute did not impose legislative punishment because the statute merely required non-participating manufacturers to pay money into an interest bearing escrow account, which payments were returned with interest after 25 years if the cigarette manufacturer is not held liable for its conduct. 100 F. Supp. 2d at 1199-1200. In contrast, the Tax imposed by the Cigarette Fee Act is nonrefundable, and must be paid to the State irrespective whether the manufacturer is held liable for its conduct. Under the circumstances, the Tax imposed by the Cigarette Fee Act imposes impermissible legislative punishment, and is an unconstitutional bill of attainder.

CONCLUSION

For the above-stated reasons, Appellants respectfully request that this Court reverse the order and judgment entered by the District Court and affirmed by the Court of Appeals and order the District Court to enter summary judgment in favor of Appellants declaring the Cigarette Fee Act unconstitutional.

Dated: December 16, 2004

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CERTIFICATE OF COMPLIANCE

Pursuant to Minnesota Rule of Civil Appellate Procedure 132.01 subd. 3, the undersigned hereby certifies, as counsel for Appellants, that this brief complies with the type-volume limitation as there are 12,638 words of proportional space type in this brief. This brief was prepared using Microsoft Word 2000.

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