IN THE SUPREME COURT OF MISSOURI

No. SC95422

STATE OF MISSOURI ex rel. JEREMIAH W. (JAY) NIXON,
Appellant/Cross-Respondent

v.

AMERICAN TOBACCO CO., et al.,

Respondents/Cross-Appellants

Appeal from the Circuit Court of the City of St. Louis
The Honorable Jimmie M. Edwards, Circuit Judge

SUBSTITUTE RESPONSIVE BRIEF OF RESPONDENTS/CROSS-APPELLANTS CERTAIN SUBSEQUENT PARTICIPATING MANUFACTURERS

Jonathan F. Dalton #35975
Angela L. Odlum #65380
ARMSTRONG TEASDALE LLP
7700 Forsyth Blvd., Suite 1800
St. Louis, MO 63105
(314) 621-5070
jdalton@armstrongteasdale.com
aodlum@armstrongteasdale.com

Robert J. Brookhiser, *pro hac vice*
Elizabeth B. McCallum, *pro hac vice*
BAKER & HOSTETLER LLC
1050 Connecticut Ave. NW, Suite 1100
Washington, DC 20036
(202) 861-1500
rbrookhiser@bakerlaw.com
emccallum@bakerlaw.com

Attorneys for Certain Subsequent Participating Manufacturers

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STATEMENT OF FACTS

As noted in their opening brief, the fifteen Subsequent Participating Manufacturers ("SPMs") joining this brief are smaller tobacco manufacturers, with national market shares ranging from below one tenth of one percent to 3-4 percent. They joined the Master Settlement Agreement ("MSA") voluntarily though most of them were never sued by any State. A group of SPMs were the first to move to compel arbitration on the 2003 NPM adjustment, in June 2004. As smaller companies with relatively limited resources, the SPMs would be directly and substantially prejudiced if they were required to participate in numerous separate and simultaneous state-specific arbitrations rather than the single multistate arbitration required by the MSA. *See Maryland v. Philip Morris, Inc.*, 123 A.3d 660, 686 (Md. Ct. Spec. App. 2015) (single-state arbitrations "would have a tremendous effect on all parties, especially the SPMs, which are smaller companies with more limited resources.")

The SPMs otherwise join the Statement of Facts in the Original Participating Manufacturers' ("OPMs") Responsive Brief.

ARGUMENT

POINTS ONE, TWO, AND THREE SHOULD BE DENIED FOR THE REASONS STATED IN THE OPMs' RESPONSIVE BRIEF, AND BECAUSE MULTIPLE SIMULTANEOUS ARBITRATIONS WOULD DIRECTLY AND SUBSTANTIALLY HARM THE SPMs

The fifteen SPMs listed below join in and adopt the arguments set out in the OPMs' responsive brief, and write separately only to point out the unique harm they will suffer if there are multiple simultaneous single-state arbitrations. As the OPMs explain in full, the language of the parties' contract requires a multistate arbitration. The trial court and every other court except the Court of Appeals to have addressed that question have agreed. Missouri's brief only barely acknowledges the governing MSA language and does not even mention the unanimous contrary authority (see List of Authorities starting on page 4 below, citing and quoting cases).

Nor does Missouri address the structural reasons why the MSA language requires nationwide arbitration here – because the dispute over whether or not the PMs receive the NPM Adjustment, including the incorporated diligent enforcement determinations, is a nationwide one affecting all PMs and States and requiring both consistency and the opportunity for all interested parties to participate. As the National Association of Attorneys General explained in 2003, "[i]t should be stressed that NPM sales anywhere in the country hurt all States. All payment

calculations are done on the basis of cigarette sales nationally. NPM sales in any state reduce payments to every other State. All States have an interest in reducing NPM sales in every State." NAAG Memorandum of Sept. 12, 2003 (attached to PMs' Statement of Claim in arbitration as App. 10). *Accord Connecticut v. Philip Morris, Inc.*, 905 A.2d 42, 50 (Conn. 2006) ("the agreement's broad referral to an arbitration panel … reflects the necessity of creating a uniform, nationwide set of rules by which the independent auditor is to calculate the annual payments").

Instead, Missouri relies on an unfounded "course of conduct" argument that does not trump the actual language and structure of the MSA and that is in any event factually wrong, as the OPMs' brief explains. The "Agreement Regarding Arbitration," crucially, was a resolution addressing the States' continued refusal to arbitrate in spite of numerous court decisions requiring arbitration. Nor does Missouri's litany of false accusations of Panel misconduct in the arbitration on the *2003* NPM Adjustment help its argument that it should not be required to participate in the *2004* arbitration. The trial court rejected those allegations on their merits – for good reason – when it denied Missouri's motion to vacate the 2003 arbitration award, and Missouri has now chosen to abandon its appeal on that issue, conceding it has no merit.

Finally, and most importantly to the SPMs, enforcement of the parties' agreement to a single multistate arbitration in which all interested parties may

participate is critical for the SPMs. They are smaller companies with relatively limited resources. It would be difficult and potentially impossible for them to participate meaningfully in up to 27 simultaneous proceedings over each year's NPM Adjustment dispute, each with its own different and potentially conflicting discovery obligations, procedures, hearings, and rules. As numerous MSA courts have noted, "[t]he State … cannot explain how a proceeding that is subject to one final and binding determination would be less workable or expeditious than litigating the issue fifty-two times in fifty-two separate court systems with the imminent possibility of delays and appeals." *E.g., Maryland v. Philip Morris*, 944 A.2d 1167, 1180 (Md. Ct. Spec. App. 2008); *Pennsylvania v. Philip Morris, Inc.*, 128 A.3d 334, 348-55 (Pa. Cmwlth. Ct. 2015) (single-state arbitration "'would lead to an absurd result of a large number of separate arbitrations, and separate arbitration panels, being required to resolve a single year's NPM Adjustment dispute that involves all of the same parties and issues.'"). Such chaotic proceedings "would have a tremendous effect on all parties, especially the SPMs, which are smaller companies with more limited resources." *Maryland v. Philip Morris, Inc.*, 123 A.3d 660, 683-86 (Md. Ct. Spec. App. 2015) , *cert. denied*, 446 Md. 293 (2016).

The authorities cited in the first paragraph above addressing nationwide arbitration under the MSA are:

(1) *Alabama v. Philip Morris, Inc.*, 1 So.3d 1, 13-14 (Ala. 2008) ("Because a diligent-enforcement determination as to one settling state will have an adverse impact on the remaining nonexempt settling states, it is essential that disputes regarding diligent enforcement be resolved in a national arbitration proceeding. Individual resolution of diligent enforcement disputes in 52 separate state courts would involve the application of different standards in determining what activities constitute diligent enforcement and could lead to inconsistent and conflicting determinations on the issue. A national arbitration proceeding will ensure that disputes regarding diligent enforcement are resolved by three neutral arbitrators 'who are guided by one clearly articulated set of rules that apply universally in a process where all parties can fully and effectively participate.'"; "[The agreement requires a national, as opposed to a local, arbitration proceeding. … The settling states represent one side to the agreement; the PMs represent the other side. … [C]onducting 52 separate arbitration proceedings would likely be fraught with the same type of inequitable and inconsistent results that would arise were the individual state courts to resolve this dispute.").

(2) *Arkansas v. The American Tobacco Co. Inc.,* No. U1997-298, at 8 (Cir. Ct., Pulaski Cty., Ark. 2006) ("Uniformity of results would be enhanced with

one panel of arbitrators making a decision versus 50 or more state courts making potentially diverse decisions.").

(3) *Coordination Proceeding Tobacco Case*, JCCP 4041, at 4 (Super. Ct. San Diego Cty, Cal., 2006) (diligent enforcement "is a contractual term set out in the MSA, the determination of which has a direct impact on the payments received by each and every Settling State. Fairness in result requires the uniform application of the MSA contractual standards, including the interpretation of the term 'diligent enforcement.' Arbitration before one national panel will avoid the risk of inconsistent judgments") (LF 1951-55).

(4) *Colorado v. R.J. Reynolds Tobacco Co.*, No. 97 CV 3432, at 7 (Dist. Ct. Denver Cty. Colo. 2006) ("The Court also finds that the need for uniformity compels the result reached in this decision. … The avoidance of fifty or more separate actions, and fifty or more varying outcomes, was a key rationale for the parties entering into the MSA.") (LF 1906-13).

(5) *Connecticut v. Philip Morris, Inc.*, 905 A.2d 42, 50 (Conn. 2006) ("the agreement's broad referral to an arbitration panel … reflects the necessity of creating a uniform, nationwide set of rules by which the independent auditor is to calculate the annual payments. Indeed, the trial court aptly stated that, if the interpretation of the rules on calculating annual payments were left up to the courts of each of the settling states, 'fifty-two different sets of payment rules might

emerge, sowing confusion, depriving [s]ettling [s]tates of mon[eys] needed for smoking cessation and other essential health programs, and causing wave after costly wave of new litigation.'"; "[T]he state argued that … the arbitration provision does not provide for a single nationwide resolution of disputes, but would result in fifty-two separate arbitration proceedings as each settling state would seek to select their own arbitration panels. We disagree with the state's interpretation of the arbitration provision because the arbitration provision expressly provides that '[e]ach of the two sides to the dispute shall select an arbitrator.' Accordingly, this language envisions that the settling states would select one arbitrator and the participating manufacturers would select one arbitrator."), *aff'g Connecticut v. Philip Morris, Inc*., 2005 Conn. Super. LEXIS 2067 at *116 (Conn. Super. Ct. Aug. 3, 2005) ("Each Settling State thus has a vital interest in the granting or denial of each other Settling State's individual claim for exemption, and for obvious reasons, their interests are conflicting. Submitting such a dispute to a neutral panel of competent arbitrators affords all interested parties the right to be heard on a level playing field where no interested party enjoys an apparent home-field advantage").

(6) *Delaware v. Philip Morris USA*, 2006 WL 3690892, at *5 (Del. Chanc. Ct. 2006) ("permitting individual state courts to determine not only whether their state diligently enforced the statute, but also the standard by which that

determination is made, would almost certainly lead to inconsistency and the likely evisceration of the NPM Adjustment, as each state acted to protect its share of the payments. The parties to the MSA clearly recognized this risk and provided for arbitration of disputes concerning the operation or application of the adjustments to guarantee uniformity, impartiality, and fairness"), *aff'd Delaware v Philip Morris USA*, 925 A.2d 504 (Del. 2007).

(7) *District of Columbia v. Philip Morris USA, Inc.*, No. 2006 CA 003176 B, at 3 (D.C. Super. Ct. 2006) ("a single arbitration proceeding in which all the parties' claims can be resolved in full is warranted to ensure that the Independent Auditor makes its determinations subject to a single set of rules applicable to all Settling States. To rule otherwise would promote chaos.") (LF 1994-08).

(8) *Hawaii v. Philip Morris USA, Inc.,* Civil No. 06-1-0695-04 KSSA, at 7 (Hawaii Circ. Ct. 2006) ("to permit individual states to separately determine the question of diligent enforcement, a question intertwined in and necessary to the determination of the applicability, or not, of the NPM Adjustment, would create confusion and unfairness to other states") (LF 1915-32).

(9) *Idaho v. Philip Morris, Inc.*, No. CVOC, at 11 (Idaho Dist. Ct, 4th Dist., 2006) ("The Court believes that the need for uniformity is of paramount concern. The PMs are rightly concerned with a situation in which fifty-two governmental organizations turn to fifty-two different court systems to arrive at

fifty-two different interpretations of what should be a uniformly interpreted contract. … Arbitration before one national panel, therefore, is the most appropriate outcome."; argument that there should be 52 separate arbitration panels "is plainly refuted by the language of Section XI(c), which provides that each 'side' is entitled to choose one arbitrator each. In other words, the State of Idaho and all the Settling States are to come together to choose one representative arbitrator who would sit on the only arbitration panel provided for in the MSA.") (LF 1833-60).

(10) *Illinois v. Lorillard Tobacco Co.*, 865 N.E.2d 546, 554 (Ill. Ct. App. 2007) ("we agree with those courts before us that have pointed out the 'compelling logic to having these disputes handled by a single arbitration panel of three federal judges, rather than numerous state and territorial courts.'").

(11) *Illinois v. Lorillard Tobacco Co.,* No. 96 L 13146, at 2 (Cir. Ct. Cook Cty. Ill. 2008) (Illinois' attempt to choose its own arbitrator with 11 other states "constitutes a clear violation of the [Illinois order compelling arbitration], as well as the Illinois Appellate Court's decision, mandating a single, nationwide arbitration panel.") (LF 1924-28).

(12) *Indiana v. Philip Morris USA, Inc.*, 879 N.E.2d 1212, 1220 (Ind. Ct. App. 2008) ("the application of the diligent enforcement defense for any Settling State affects all other Settling States, thus creating the need for a single decision-

maker, and making it all the more important to resolve these disputes under a single set of rules that apply equally to each Settling State. The language as well as the structure of the MSA requires disputes such as this to be determined by a single, national arbitration panel."; "Both the language and the structure of the MSA require that the dispute concerning the 2003 NPM Adjustment, including the Settling States' claims of diligent enforcement of their Qualifying Statutes, must be submitted to a single, national arbitration panel. … [T]he MSA refers to the two sides to this agreement settling their disputes by choosing one arbitrator for each side. Those two sides are: (1) the PMs (which contend that they are entitled to an NPM Adjustment) and (2) the Settling States (which contend that no NPM Adjustment can be applied).").

(13) *Kansas v. R.J. Reynolds Tobacco Co.*, No. 96-CV-919, at 9 (Dist. Ct. Shawnee Cty., Kan. 2007) (rejecting argument that arbitration would overly burden a single panel; "it would be more burdensome to reconcile potential divergent outcomes resulting from 52 independent decisions, if each Settling State was to assert jurisdiction over the present dispute.").

(14) *Kentucky v. Brown & Williamson Tobacco Co.*, No. 98-CI-01579, at 2 (Ky. Franklin Cty. Ct. 2006) ("To rule [against arbitration] would promote chaos.") (LF 1816-21).

(15) *Maryland v. Philip Morris*, 944 A.2d 1167, 1180-81 (Md. Ct. Spec. App. 2008) ("the granting of an exemption to one Settling State will inexorably lead to the reallocation of its allocated portion of the NPM Adjustment to all other non-exempt Settling States. Each Settling State thus has a vital interest in the granting or denial of each other Settling State's individual claim for exemption, and for obvious reasons, their interests are conflicting. Submitting such a dispute to a neutral panel of competent arbitrators affords all interested parties the right to be heard on a level playing field where no interested party enjoys an apparent home-field advantage.").

(16) *Maryland v. Philip Morris, Inc.*, 123 A.3d 660, 683-86 (Md. Ct. Spec. App. 2015) ("the circuit court correctly recognized the "two sides to the dispute" to be "the MSA States in opposition to the downward adjustment, and the PMs."), *aff'g Maryland v. Philip Morris*, Case No. 24-C-96122017/CL211487, at *16 (Md. Balt. Cir. Ct., July 23, 2014) ("[T]he only reasonable interpretation of the MSA is that nationwide arbitration is required"; the States constitute a single "side"; rejecting the argument that "unfair" treatment in the 2003 arbitration trumped plain contractual language.

(17) *Massachusetts v. Philip Morris Inc.*, 864 N.E.2d 505, 512 (Mass. 2006) ("[t]he application (or not) of the NPM adjustment to one State's share potentially affects the payments to many other States. 'Accordingly, the

[settlement agreement's] broad referral to an arbitration panel of '[a]ny dispute, controversy or claim arising out of' the independent auditor's calculations or determinations reflects the necessity of creating a uniform, nationwide set of rules by which the independent auditor is to calculate the annual payments.'").

(18) *New Hampshire v. Philip Morris USA, Inc.*, 927 A.2d 503, 511 (N.H. 2007) ("[T]he application of the NPM Adjustment to one state's allocated share affects the payments made to the other settling states."; "[T]he [MSA's] broad referral to an arbitration panel of any dispute, controversy or claim arising out of the independent auditor's calculations or determinations reflects the necessity of creating a uniform, nationwide set of rules by which the independent auditor is to calculate the annual payments.").

(19) *New Mexico v. The American Tobacco Co.*, 194 P.3d 749, 754 (N.M. Ct. App. 2008) (rejecting argument that a New Mexico-specific arbitration was required; "the text of the MSA supports the district court's order compelling arbitration of this dispute before a nationwide panel").

(20) *New York v. Philip Morris Int'l*, 858 N.Y.S.2d 134, 136 (N.Y. App. Div. 1st Dep't 2008) (reversing trial court order permitting state to pick its own arbitrator as a single side; "This Court [previously] rejected plaintiffs' arguments that each Settling State constituted a 'side' to the dispute, under section XI(c) of the Master Settlement Agreement, with the right to select its own Arbitrator. …

Other courts have also concluded that the Settling States constitute one side for purposes of the diligent enforcement dispute").

(21) *New York v. Philip Morris Int'l Inc.*, 869 N.E.2d 636, 464 (N.Y. 2007) ("[W]e agree with the Appellate Division that there is fairness to all parties in a 'mechanism of submitting disputes involving the decisions of the Independent Auditor to a neutral panel of competent arbitrators, who are guided by one clearly articulated set of rules that apply universally in a process where all parties can fully and effectively participate'"), *aff'g New York v. Philip Morris Int'l Inc.*, 813 N.Y.S.2d 71, 76 (N.Y. App. Div. 1st Dep't 2006) ("Since the granting of an exemption by one settling state will automatically lead to the reallocation of its allocated portion of the NPM adjustment to all other non-exempt settling states, each governmental signatory has its own self-interest at stake in the outcome of this issue, which is necessarily in conflict with every other state. Such a result defeats the whole purpose of having a Master Settlement Agreement. The mechanism of submitting disputes involving the decisions of the Independent Auditor to a neutral panel of competent arbitrators, who are guided by one clearly articulated set of rules that apply universally in a process where all parties can fully and effectively participate, obviates this problem and ensures fairness for all parties to the MSA. To hold otherwise is contrary to both the spirit and the plain language of the Master Settlement Agreement.").

(22) *North Dakota v. Philip Morris Inc.*, 732 N.W.2d 720, 730 (N.D. 2007) (same).

(23) *Oregon v. Philip Morris USA, Inc.*, No. 0604-0452, at 6 (Or. Cir. Ct. 2006) (rejecting Oregon's argument that it may choose its own arbitrator; "the Settling States represent one 'side' of the dispute and the PMs represent the other 'side.'").

(24) *Pennsylvania v. Philip Morris, Inc.*, 128 A.3d 334, 348-55 (Pa. Cmwlth. Ct. 2015) (single-state arbitration "'would lead to an absurd result of a large number of separate arbitrations, and separate arbitration panels, being required to resolve a single year's NPM Adjustment dispute that involves all of the same parties and issues.' The obvious disadvantage of separate, parallel proceedings is the risk of inconsistent results. Such complications can be readily avoided by a nationwide arbitration involving all interested parties, as envisioned by the MSA. Submitting the dispute to a single nationwide arbitration panel, chosen by the Settling States and PMs, and guided by a uniform set of rules, affords all interested parties the opportunity to be heard on a level playing field."), *aff'g Pennsylvania v. Philip Morris USA, Inc.,* No. 2422 C.D. 2014, at *19, 26 (Penn. Phila. Ct. Common Pleas, Feb. 23, 2015) ("[T]he MSA 'evinces the parties' intention to have a single, national arbitration' for NPM Adjustment disputes"; rejecting arguments that diligent enforcement is a separate state-specific dispute

unrelated to the nationwide dispute over application and allocation of the NPM Adjustment; and citing the "interconnectedness" of diligent enforcement determinations as a reason why the MSA drafters intended a nationwide arbitration).

(25) *South Carolina v. Brown & Williamson Tobacco Co.,* No. 97-CP-4746, at 3 (S.C. Richland Cty Ct. 2008) (rejecting South Carolina's argument that it should be permitted to choose its own arbitrator; "the Court concludes that the MSA requires nationwide arbitration, as opposed to state-specific arbitration").

(26) *South Dakota v. R.J. Reynolds Tobacco Co.*, No. 06-161, Findings of Fact and Conclusions of Law at 3 (S.D. Cir. Ct. Hughes Cty. 2006) ("[A diligent enforcement finding for any one State will impact the annual payment received by each other state. Under these circumstances it is important that this dispute be resolved in a single arbitration proceeding in which all parties can participate according to one clearly articulated set of rules.") (LF 2008-12).

(27) *Vermont v. Philip Morris USA, Inc.*, 945 A.2d 887, 894 (Vt. 2008) (rejecting State argument "that submitting each settling state's dispute over diligent enforcement to one 'nationwide arbitration' is unworkable; "other courts addressing this issue … have found 'compelling logic' in having disputes over diligent enforcement handled by one arbitration panel rather than separate courts in each settling state").

(28) *Virginia v. Brown & Williamson Tobacco Co.*, No. HJ-224l, at 6 (Va. Cir. Ct. 2006) ("[The determination of whether a particular state diligently enforced its Qualifying Statute has the potential to affect other states' distributions. … Submission to a neutral panel that will apply a single unitary standard where all parties may participate is the most practical way that the Agreement can reasonably be enforced.") (LF 1930-37).

(29) *Washington v. Philip Morris USA, Inc.*, No. 06-2-l3262-9SEA, at 3 (Wash. Super. Ct, King Cty. 2006) ("it would make no sense in the context of the MSA to have [diligent enforcement] addressed independently by the various state courts, for both procedural and substantive reasons. It is manifest from the Agreement that the parties were concerned that there be uniformity when addressing any NPM adjustment, and that objective would be significantly impaired were the State's approach adopted.") (LF 2004-06).

(30) *McGraw v. American Tobacco Co.*, 681 S.E.2d 96, 108 (W.V. 2009) (rejecting state argument for a single-state arbitration; "Having reviewed the MSA, including the arbitration provision in dispute, this Court concludes that the provision unambiguously provides for arbitration of a diligent enforcement determination before a single panel of three former federal judges. Although the specific term 'nationwide' does not appear in the MSA's arbitration provision, reading the MSA as a whole clearly demonstrates that it contemplates that a single

panel of arbitrators resolve disputes regarding any diligent enforcement determination with respect to all MSA participants").

CONCLUSION

This Court should affirm the trial court's order denying Missouri's request for its own single-state arbitration.

Dated: August 1, 2016

Respectfully submitted,

/s/ Jonathan F. Dalton

Robert J. Brookhiser, *pro hac vice*
Elizabeth B. McCallum, *pro hac vice*
BAKER & HOSTETLER LLC
1050 Connecticut Ave. NW, Suite 1100
Washington, DC 20034
(202) 861-1500
rbrookhiser@bakerlaw.com
emccallum@bakerlaw.com

Jonathan F. Dalton #35975
Angela L. Odlum #65380
ARMSTRONG TEASDALE LLP
7700 Forsyth Blvd., Suite 1800
St. Louis, MO 63105
(314) 621-5070
jdalton@armstrongteasdale.com
aodlum@armstrongteasdale.com

Attorneys for 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, Inc., Liggett Group LLC, Peter Stokkebye Tobaksfabrik A/S, P.T. Djarum, Santa Fe Natural Tobacco Company, Inc., Sherman 1400 Broadway N.Y.C., Inc., Top Tobacco, L.P., Von Eicken Group, and for purposes of this brief only also appearing for Farmers Tobacco Company of Cynthiana, Inc.

CERTIFICATE OF SERVICE AND COMPLIANCE

A copy of this document was served on counsel of record through the Court's electronic notice system on August 1, 2016.

This brief includes the information required by Rule 55.03 and complies with the requirements contained in Rule 84.06. Relying on the word count of the Microsoft Word program, the undersigned certifies that the total number of words contained in this brief is 4,166, excluding the cover, signature block, and this certificate.

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/s/ Jonathan F. Dalton