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MONTANA FIRST JUDICIAL DISTRICT COURT
LEWIS AND CLARK COUNTY

STATE OF MONTANA ex rel, TIMOTHY C. FOX,	)	Cause No. CDV-1997-306
Plaintiff	)	Hon. Michael McMahon

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MONTANA FIRST JUDICIAL DISTRICT COURT
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STATE OF MONTANA ex rel, TIMOTHY C. FOX,	)	Cause No. CDV-1997-306
Plaintiff	)	Hon. Michael McMahon

vs.	
PHILIP MORRIS, INCORPORATED; RJ. REYNOLDS TOBACCO CO.; AMERICAN TOBACCO CORP.; BROWN & WILLIAMSON TOBACCO CORP.; LIGGETT & MYERS, INC.; LORILLARD TOBACCO COMPANY; UNITED STATES TOBACCO COMPANY; B.A.T. INDUSTRIES, P.L.C.; BRITISH AMERICAN TOBACCO COMPANY, LTD.; RJR NABISCO HOLDINGS CORP.; RJR NABISCO, INC.; HILL & KNOWLTON, INC.; THE COUNCIL FOR TOBACCO RESEARCH - U.S.A., INC.; and TOBACCO INSTITUTE, INC.,	**BRIEF IN SUPPORT OF MOTION TO ENFORCE CONSENT DECREE AND MASTER SETTLEMENT AGREEMENT AND JURY DEMAND**
Defendants.	

Introduction

1. The State of Montana, through Attorney General Timothy C. Fox, brings this action to hold the Defendant tobacco companies accountable for a sophisticated conspiracy to defraud Montana of tens of millions of dollars due under the Master Settlement Agreement ("MSA") and the Consent Decree.

2. In 1998, Montana and 51 other jurisdictions settled claims against certain tobacco companies for driving up the cost of publicly funded healthcare, marketing to children as "replacement smokers," distorting the science of nicotine addiction and smoking, and deceiving the public about the health effects of smoking. The parties struck a bargain—the MSA—wherein the Defendants agreed, among other obligations, to make

annual payments in perpetuity to settle the State's substantial past and future claims against them. Those annual payments to Montana are used predominantly to pay for tobacco prevention and cessation programs, the Children's Health Insurance, chronic disease programs, communicable disease programs, and family health programs.

3. As expressed by former Commissioner Scott Gottlieb of the Federal Food and Drug Administration and the World Health Organization, tobacco is the only product where if used correctly kills half of all long-term users. https://www.fda.gov/news-events/press-announcements/statement-fda-commissioner-scott-gottlieb-md-pivotal-public-health-step-dramatically-reduce-smoking; https://www.who.int/news-room/fact-sheets/detail/tobacco.

4. Although the tobacco companies denied all of the State's allegations in the original litigation and the case settled before liability determinations were made, these same allegations were later proven against several of the same Defendants before the United States District Court for the District of Columbia. In its 1,683-page opinion, that Court found that the tobacco companies violated the federal Racketeer Influenced and Corrupt Organizations Act ("RICO") and summarized its findings as follows:

> [This Federal RICO case] is about an industry, and in particular these Defendants, that survives, and profits, from selling a highly addictive product which causes diseases that lead to a staggering number of deaths per year, an immeasurable amount of human suffering and economic loss, and a profound burden on our national health care system. Defendants have known many of these facts for at least 50 years or more. Despite that knowledge, they have consistently, repeatedly, and with enormous skill and sophistication, denied these facts to the public, to the Government, and to the public health community. Moreover, in order to sustain the economic viability of their companies, Defendants have denied that they marketed and advertised their products to children under the age of eighteen and to young people between

> the ages of eighteen and twenty-one in order to ensure an adequate supply of "replacement smokers," as older ones fall by the wayside through death, illness, or cessation of smoking. In short, Defendants have marketed and sold their lethal product with zeal, with deception, with a single-minded focus on their financial success, and without regard for the human tragedy or social costs that success exacted.

United States v. Philip Morris USA, Inc., et al., 449 F. Supp. 2d 1, 28 (D.D.C. 2006).[1]

The Court further found, in a pattern similar to what Montana continues to experience through today, that:

> From at least 1952 until at least 2000, each and every one of these Defendants, repeatedly, consistently, vigorously, - and falsely - denied the existence of any adverse health effects from smoking. Moreover, they mounted a coordinated, well-financed, sophisticated public relations campaign to attack and distort scientific evidence demonstrating the relationship between smoking and disease, claiming the link between the two was still an "open question." Finally, in doing so, ignored the massive documentation in their internal corporate files from their own scientists, executives, and public relations people that, as Philip Morris's Vice President of Research and Development, Helmut Wakeham, admitted, there was "little basis for disputing the findings [of the 1964 Surgeon General's Report] at this time."

Id. at 824.

5. To this day, the Defendants continue to "consistently, repeatedly, and with enormous skill and sophistication" and "with a single-minded focus on their financial success" burden Montana's public health system by denying what they know to be true. This action is brought because those same big tobacco companies—and the host of smaller tobacco companies that ride their coattails—have once again resorted to deception to

[1] Defendants included: Philip Morris USA, R.J. Reynolds Tobacco Co., Brown and Williamson Tobacco Company, Lorillard Tobacco Company, The Liggett Group, American Tobacco Company, British American Tobacco, Council for Tobacco Research-U.S.A. Inc., and The Tobacco Institute.

deplete public funds for their own gain and deny the people of Montana the benefit of the MSA contract they agreed to, in violation of Defendants' duty of good faith and fair dealing and of the Montana False Claims Act.

6. The Defendant tobacco companies are engaged in a bad faith conspiracy to improperly reduce every annual payment obligation to Montana due under the MSA. The goal is to permanently, and in unison, reduce their payment obligations under the MSA through a scheme of distortion, deception, and delay.

7. Each year, Defendants assert a "dispute" with Montana over whether the contingency addressed in a particular provision in the MSA applies to Montana for that year. Having asserted this "dispute," the Defendants then withhold from Montana millions from each annual payment they owe under the MSA. The Defendants refuse to pay to Montana the withheld portion of its MSA payments unless and until Montana litigates each year's "dispute." However, it takes more than one year to litigate each "dispute" for each year's withheld payment, which creates an ever-increasing backlog of "disputes." Worse, even if Montana prevails in a "dispute," the Defendants refuse to make full payment to Montana until they resolve their analogous disputes for that year with all other MSA States.

8. Hence, the total amount of MSA payments that Defendants are withholding from Montana grows each year. In 2006, the amount withheld was less than $4 million and one dispute between the Defendants and Montana (over the amount withheld from the 2003 MSA payment) was awaiting resolution. Each year since 2006, they have asserted a new dispute that requires multiple years to resolve. Today, the amount withheld from Montana is more than $43 million and twelve "disputes" the Defendants have asserted

against Montana await resolution. These numbers will continue to increase each year until the Defendants' scheme is stopped.

9. Defendants intentionally create this circumstance. First, the Defendants assert a dispute each year—having no factual basis for asserting the dispute. Then, they withhold millions of dollars from Montana's MSA payment due that year on the bare assertion that there is a "dispute." Next, the Defendants insist that Montana spend multiple years litigating each of these annual disputes. When Montana prevails, the Defendants then insist that Montana wait to receive the withheld portion of its MSA payment until Defendants' analogous disputes with all other States are also resolved. As long as a new dispute is asserted each year, and it takes multiple years to resolve each dispute, the backlog of disputes increases each year. Defendants thus make it functionally impossible for Montana to ever recover the full amount of MSA payments withheld over the years—even if Montana wins every dispute asserted against it. The number of disputes asserted and the history of resolving them illustrates this clearly:

Calendar Year	**Disputed Payment Years Awaiting Resolution (newly asserted disputes in red)**	**Montana Litigation**	**Other States' Arbitration**
2006	2003	Montana litigation over 2003 payment dispute[2]	Arbitration over 2003 payment dispute[3]
2007	2003, 2004		
2008	2003, 2004, 2005		
2009	2003, 2004, 2005, 2006		
2010	2003, 2004, 2005, 2006, 2007		
2011	2003, 2004, 2005, 2006, 2007, 2008		

[2] Because the Defendants insist that, even after Montana prevails, the State cannot be paid until its disputes with all other states are resolved, Montana was forced to wait until the other states began their arbitration, which is a much slower proceeding than Montana's.

[3] The other states spent 2014–15 preparing for the second arbitration and appealing some of the arbitration decisions.

2012	2003, 2004, 2005, 2006, 2007, 2008, 2009		
2013	2004, 2005, 2006, 2007, 2008, 2009, 2010		
2014	2004, 2005, 2006, 2007, 2008, 2009, 2010, 2011		
2015	2004, 2005, 2006, 2007, 2008, 2009, 2010, 2011, 2012		
2016	2004, 2005, 2006, 2007, 2008, 2009, 2010, 2011, 2012, 2013		Arbitration over 2004 payment dispute (ongoing)[4]
2017	2004, 2005, 2006, 2007, 2008, 2009, 2010, 2011, 2012, 2013, 2014	Montana litigation over 2004 payment	
2018	2004, 2005, 2006, 2007, 2008, 2009, 2010, 2011, 2012, 2013, 2014, 2015		
2019	2005, 2006, 2007, 2008, 2009, 2010, 2011, 2012, 2013, 2014, 2015, 2016		
2020	2005, 2006, 2007, 2008, 2009, 2010, 2011, 2012, 2013, 2014, 2015, 2016, 2017		

10. The withheld amounts would have gone to tobacco prevention and cessation programs, Children's Health Insurance, the State's General Fund, and the Tobacco Trust—interest from which is further used to fund a variety of much-needed health programs around the state, including child mental health, communicable disease, suicide prevention, Medicaid, family health, and the Children's Health Insurance Program ("CHIP"), as well as tobacco enforcement efforts by the Montana Department of Justice and Department of Revenue.[5] The Defendants' wrongful conduct has deprived Montana of funds sufficient to provide health insurance for an additional 200–300 Montana children, annually.

[4] This arbitration is expected to continue into 2021 and possibly 2022.
[5] https://leg.mt.gov/content/Publications/fiscal/leg_reference/Brochures/tobacco-settlement-2018.pdf

Parties

11. Montana entered into the MSA and thus is a "Settling State" as defined in the MSA (hereafter "MSA State"). The Attorney General is authorized to bring this action to enforce the MSA on behalf of the State of Montana under Paragraph VI.A of the Consent Decree and Final Judgment and section VII(c)(l) of the MSA. The Attorney General is further authorized by § 17–8–405, MCA, to bring an action to enforce the Montana False Claims Act.

12. Defendants Philip Morris USA Inc., and R.J. Reynolds Tobacco Company, are Original Participating Manufacturers ("OPMs"), as defined in section II(hh) of the MSA.[6]

13. Defendants Commonwealth Brands, Inc., Farmer's Tobacco Company of Cynthiana, Inc., ITG Brands, LLC, Japan Tobacco International USA, Inc., King Maker Marketing, Inc., Kretek International, Inc., Liggett Group, LLC., Peter Stokkebye Tobaksfabrik A/S, Premier Manufacturing Inc., Santa Fe Natural Tobacco Company, Inc., Scandinavian Tobacco Group Lane Ltd., Sherman's 1400 Broadway N.Y.C., Inc., Tabacalera del Este, S.A. ("TABESA"), Vector Tobacco Inc., the Von Eicken Group, and Wind River Tobacco Company, LLC are Subsequent Participating Manufacturers ("SPMs"), as defined in section II (tt) of the MSA.[7]

[6] The remaining two OPMs, Brown & Williamson Tobacco Corporation and Lorillard Tobacco Company, are now part of R.J. Reynolds.

[7] In calculating the Defendants' MSA payment obligations, ITG Brands, LLC and Scandinavian Tobacco Group Ltd. are partially treated as OPMs with respect to the sales of certain brands that they have acquired from the OPMs.

14. The OPMs and SPMs are collectively referred to as the Participating Manufacturers ("PMs"). The PMs specifically identified above are referred to as "Defendants" throughout this Complaint.

15. The above-named Defendants are participants in a conspiracy to deprive Montana of funds contractually owed under the MSA that Montana uses for smoking cessation and children's and public health programs.[8] Several other SPMs do not participate in this scheme and, thus, are not named here as Defendants. Still other SPMs appear to have assigned their rights regarding the asserted dispute to the Defendant Commonwealth Brands or others, and may be added as Defendants to this lawsuit upon determination of the nature of the assignment of rights involved and the real party in interest.

16. The caption in this matter remains the original caption from the tort case filed in 1997. Since 1997, the parties to the MSA and to this case have changed significantly. A multitude of smaller companies have signed onto the MSA and made themselves party to this case. Some of those SPMs have gone out of business or stopped selling cigarettes, and thus are no longer active participants in the MSA. Some of the original defendants

[8] The Defendants have acted in concert throughout the history of their supposed "disputes." The two primary actors, Philip Morris and R.J. Reynolds, take the lead and set out their positions which, in the case of Montana, have always been identical. The SPMs—all represented by the same counsel—then collectively join or adopt the positions of Philip Morris and R.J. Reynolds. Farmers Tobacco Company has a second set of counsel, in addition to the counsel they share with the other SPM Defendants, and occasionally asserts additional positions independently from the other SPMs. Unless otherwise noted, the positions, arguments, conduct, and "disputes" attributed to the "Defendants" are expressly asserted jointly by all Defendants, or asserted by one or more of the Defendants and expressly ratified by the other Defendants. The term "Defendants" is not used when the conduct at issue is attributable to fewer than all Defendants.

have merged. Some of the SPMs, though active parties to the MSA, have never appeared in this case. Due to the ever-shifting number and name of the tobacco-company parties to the MSA and the unique procedural posture of this case, the State has not requested that the caption be amended. No need to amend the caption is apparent at this time, but the State does request that the Court note that, unlike a typical case, the caption here does not reflect the actual parties to these proceedings. For purposes of this pleading and the proceedings related to it, the parties are those identified in the preceding paragraphs.

Jurisdiction

17. This Court has exclusive subject matter jurisdiction over this action for the purposes of implementing and enforcing the MSA in Montana. (MSA, § VII(a)(2); Consent Decree § VI.A (Mont. First Jud. Dist. Dec. 14, 1998)).

18. Each Defendant consented to this Court's personal jurisdiction when it joined the MSA. (MSA, § VII(a)(l)).

19. Montana files this Motion pursuant to paragraph VI.A of the Consent Decree and Final Judgment, which authorizes the State to apply to this Court "at any time for further orders and directions as may be necessary or appropriate for the implementation and enforcement of the Consent Decree and Final Judgment," and also pursuant to section VII(c)(l) of the MSA, which authorizes any MSA State to bring an action to enforce the MSA ("Enforcement Order") or for a declaration construing any such term ("Declaratory Order") with respect to disputes, alleged violations, or alleged breaches within such MSA State.

20. Montana provided each Defendant with written notice of its intent to initiate proceedings, as required by section VII(c)(2) of the MSA, before filing this Motion.

PROCEDURE

21. As discussed above, the Consent Decree mandates that this cause of action remain open in perpetuity for purposes of implementing and enforcing the Master Settlement Agreement.

22. Past practice has been to file a motion under this cause number to bring a dispute between the MSA parties in front of this Court, even though the motion has been more in the nature of a complaint. The parties and the Court have always treated the motion as a complaint, to which the Defendants then file a response in the nature of an answer, which in turn initiates proceedings and a schedule consistent with a typical civil lawsuit.

23. This pleading asserts breach by the Defendants of the covenant of good faith and fair dealing inherent in the MSA as well as violation of the Montana False Claims Act, § 17-8-403, MCA, and conspiracy. It requests relief in the form of a judgment holding Defendants liable for the breach and statutory violations and resulting contract damages, statutory damages, and declaratory relief.

24. Capitalized terms used throughout this pleading are defined terms in the MSA. For the Court's convenience, an MSA Desk Reference is submitted with this

pleading that includes definitions of MSA terms of art and commonly used acronyms.[9]

THE SCHEME

25. Defendants' asserted "disputes" with Montana are baseless and Defendants have admitted as much. Defendants assert their disputes with Montana because they believe they are entitled to withhold money from Montana simply by saying "we dispute" and pointing to provisions in the MSA regarding disputed payments.[10] Despite the Defendants' lack of factual basis for their asserted dispute, their bare assertion of a dispute forces Montana to spend multiple years litigating each year's payment. Worse, Defendants have insisted that even if Montana prevailed now on all outstanding disputes, the State would still have to wait to receive payment until Defendants' disputes with all other states are resolved.

26. This is not an accidental result of how the MSA was written. This is a calculated strategy to permanently reduce the settlement payments Defendants agreed to in the MSA. Defendants' goal is to ensure that Montana's ability to recover all amounts owed remains functionally impossible.

Relevant MSA Provisions

27. The Defendants each make an MSA payment for each year that is subject to certain adjustments. (MSA §§ IX(c)(1); IX(j), clause First through Fourth).

[9] Available for download https://paolilaw.sharefile.com/d-sa466b514f2a45dbb.
[10] March 8, 2019 Letter from Elli Leibenstein and Charles Hansberry to the Montana Attorney General's Office. Attached as Exhibit 1.

28. Each year's MSA payments from all Defendants are then aggregated and the aggregate amount is allocated among the MSA States based on set, state-specific percentages ("Allocated Payments"). (MSA § IX(j), clause Fifth).

29. After allocation of the Defendants' aggregate payment among the MSA States, a final adjustment, the Non-Participating Manufacturer ("NPM") Adjustment, *may* apply to the Allocated Payments of *some* States *if and only if* certain prerequisites are met. (MSA § IX(j), clause Sixth).

30. Whether the NPM Adjustment applies to the allocated payment of *any* State in a given year, and—if it does—the amount of the NPM Adjustment for that year, is contingent upon the following **three prerequisites**:

a. The Defendants must have experienced "Market Share Loss" of more than 2% (two percentage points), nationwide, from their 1997 Market Share to the Non-Participating Manufacturers (MSA § IX(d)(1)(A), (B);

b. An economic consulting firm (called "the Firm" in the MSA) must determine that the MSA was a "Significant Factor" for the PMs' Market Share Loss (MSA § IX(d)(1)(C));

c. At least one MSA State **must** be deemed to (a) not have had a Qualifying Statute, or (b) to not have "diligently enforced" the statute in the preceding year. Otherwise, there is no State from whom the Defendants can collect the NPM Adjustment.

31. The amount of the NPM Adjustment then depends on which *specific* States—if any—either did not have a "Qualifying Statute" or have not "diligently enforced" their Qualifying Statute during the year in question (MSA § IX(d)(2)).

32. Unless the first two prerequisites are met in a given year, the NPM Adjustment does not even potentially apply, and any provisions that govern the application of the NPM Adjustment do not come into play for that payment year.

33. Even if the first two prerequisites are met, if all States had a Qualifying Statute and enforced it, then the amount of the NPM Adjustment is zero, meaning there is no NPM Adjustment that year. Alternatively, even if the first two prerequisites are met, and some States failed to enforce their statutes, but Montana is not one of those States, the NPM Adjustment still does not apply to Montana's MSA payment for that year.

34. The third prerequisite, regarding enforcement of a Qualifying Statute, is where the Defendants improperly hinge their "disputes" with Montana. *See State ex rel. Bullock v. Philip Morris, Inc.*, 2009 MT 261 ¶¶ 2-9, for details regarding Montana's Qualifying Statue and the Defendants' asserted dispute over whether Montana enforced it. The plain language of the MSA makes clear that the NPM Adjustment—if applicable for a given payment year—only reduces the MSA payments of States that either did not have a Qualifying Statute or did not enforce it. The Defendants concede that Montana has had a Qualifying Statute (Title 16, Chapter 11, Part 4, MCA) at all relevant times. However, they "dispute" that Montana has ever enforced its Qualifying Statute—that is, they jointly

allege that in the 20 plus-year history of the MSA, Montana has never once enforced its Qualifying Statute.[11]

35. Not only is the NPM Adjustment ***contingent*** upon the satisfaction of the three prerequisites identified above, but it is also ***unliquidated***. *See Vibo Corp. v. State ex rel. McDaniel*, 2011 Ark. 124, 18–19, 380 S.W.3d 411, 423 (2011) (NPM Adjustment is "contingent and unliquidated"). The dollar amount of the Adjustment depends on which *specific* States, if any, did not have or did not enforce a Qualifying Statute during the year subject to payment.

36. The NPM Adjustment is unliquidated because its magnitude (i.e., the dollar amount of the adjustment) depends on the total dollar amount of the combined Allocated Payments of the MSA States that are ultimately determined to have not had a Qualifying Statute or not enforced it.

37. Because of the unliquidated nature of the NPM Adjustment, there are two distinct calculations of the NPM Adjustment:

a. The first is the Maximum Potential NPM Adjustment, which represents the highest possible dollar amount by which the PMs' aggregate MSA payment for a given year could *theoretically* be reduced as a result of the NPM Adjustment. This is merely the theoretical ceiling of the actual applicable NPM Adjustment

[11] March 8, 2019 Leibenstein Letter, Ex. 1 ("The PMs claim that *each of their annual payments to Montana* is subject to an NPM Adjustment because Montana did not diligently enforce a Qualifying Statute *for each sales year*.") (emphasis added).

(called the "Available NPM Adjustment") for a given year, with the theoretical floor for each year being $0.

b. The second is the Available NPM Adjustment, which is the amount that *actually* applies to the PMs' aggregate MSA payment for the year after determination of which *specific* States' payments—if any—are subject to reduction. (MSA § IX(d)(3)). The actual Available NPM Adjustment for a given year can be anywhere from $0 up to the Maximum Potential NPM Adjustment for that year. If the NPM Adjustment is deemed to apply to a given MSA State for a given year, the adjustment can only reduce that State's allocated payment up to its total Allocated Payment. For example, if only two small States failed to enforce their Qualifying Statutes in 2004, and these two States' Allocated Payments added up to $100 million, then the NPM Adjustment for 2004 would be $100 million (and would reduce only the payment of those two small states), rather than the Maximum Potential NPM Adjustment, which, for some years, exceeds $1 billion. [12]

38. The distinction between the Maximum Potential NPM Adjustment and the Available NPM Adjustment is important because part of the Defendants' scheme is to assert entitlement, each year, to the Maximum Potential NPM Adjustment. The Maximum

[12] Exhibit 2, PwC Notice ID 0265 illustrates that, while the Maximum Potential NPM Adjustment can be calculated, the Available NPM Adjustment, which is the amount to which the PMs are actually entitled, cannot be calculated until there is a determination of which MSA States, if any, failed to enforce a Qualifying Statute.

Potential NPM Adjustment is promptly calculated in April of each payment year.[13] On the other hand, the Available NPM Adjustment cannot be calculated until it is known which States, if any, are subject to the NPM Adjustment. For example, the Maximum Potential NPM Adjustment for the 2004 payment was calculated by the Independent Auditor ("IA") as of April 2004, yet the Available NPM Adjustment for 2004 is still unknown. The yet-to-be-determined Available NPM Adjustment for 2004 (or for any later payment year) can be a small fraction of that year's Maximum Potential NPM Adjustment, and even $0, depending on which States, if any, failed to enforce their Qualifying Statutes.

39. Each year, the MSA IA calculates the *theoretical* Maximum Potential NPM Adjustment, but does not—and cannot—apply it to the Defendants' MSA payment obligations. That is because the Maximum Potential NPM Adjustment only defines the upper limit of the Adjustment. Under the plain language of the MSA, the *actual* Available NPM Adjustment cannot be determined (i.e., cannot be quantified) until it is known which *specific* States' payments—if any—are subject to reduction (MSA § IX(j), clause Fifth and Sixth). This is the case even if the first two prerequisites for an NPM Adjustment have been met. For example, the Maximum Potential NPM Adjustment for 2004 is $1.1 billion (as calculated by the IA), while the Available NPM Adjustment for 2004 still remains undetermined today (16 years later) and can ultimately end up being anywhere from $0 to $1.1 billion.[14]

[13] MSA payments are made in April of each year based on sales and data from the preceding year. Thus, the 2004 payment was calculated based off of 2003 sales.
[14] *PricewaterhouseCoopers* Notice ID 0265, Attachment 4(b), attached as Exhibit 2.

40. The bottom line being: the Defendants assert entitlement to the Maximum Poential NPM Adjustment but are only entitled to the Available NPM Adjustment. Unless and until it is known which MSA States, if any, failed to have a Qualifying Statute or failed to enforce it, there is no way for the IA to calculate the Available NPM Adjustment, much less apply it to the Defendants' payment obligations. The adequacy of any given MSA States' enforcement cannot be determined in a timely manner, however, because the Defendants dispute *every* MSA State's enforcement for *every* year, resulting in protracted proceedings that make it effectively impossible to ever resolve the dispute—one payment year, 2003, has been resolved in the fourteen years since these disputes began. Worse, as detailed below, the Defendants assert disputes with MSA States like Montana despite having no factual basis for believing Montana failed to enforce its statute. In fact, a wealth of data and information suggests the opposite, that Montana fully enforced its statute.

41. To be clear, while the preceding paragraphs reference various actions by the Independent Auditor, the State brings this enforcement action solely on the basis of the Defendants' conduct, not on the basis of anything the Independent Auditor did or did not do. References to the Independent Auditor's process and calculations are for context only.

History of the Defendants' "Disputes" to Date

42. The MSA was adopted and incorporated into this Court's Consent Decree dated December 14, 1998. The MSA parties later agreed that the NPM Adjustment would not apply for the years 1999–2002.

43. Montana has twice filed actions in this Court seeking to resolve the Defendants' alleged disputes at enormous cost to the State—once for the dispute over the

withheld amount for 2003, and again for the analogous dispute over the withheld amount for 2004. Both times, after forcing the State to incur substantial litigation costs, the Defendants conceded *before trial* that Montana was not subject to an NPM Adjustment. To date, the Defendants have never brought any action to resolve their supposed disputes with Montana and have never proven their allegation that Montana did not enforce its Qualifying Statute.

44. The Defendants' string of annual "disputes" against Montana began in 2006, when they sought to reduce Montana's 2003 MSA payment on the grounds that they were entitled to apply the MSA's NPM Adjustment provision after having met only the first two prerequisites for an NPM Adjustment but *without* having met the third prerequisite.[15] Montana filed a Motion for a Declaratory or Enforcement Order on May 8, 2006 to recover the withheld money. The Defendants then sought to compel arbitration.

[15] The "Significant Factor" determination for the 2003 payment was made in 2005. At that point, the Defendants effectively *took back* part of the 2003 MSA payments they had originally made under protest in April 2003 and retroactively locked them out of Montana's and the rest of the MSA States' reach. The Defendants effectuated this retroactive withholding by subtracting an amount equal to their 2003 withholdings from their 2006 MSA payments. The exact mechanics of the Defendants' withholdings differ from one Defendant to the next and from year to year, and have become increasingly more complex (and increasingly less transparent) over time, but the result is always the same: Montana is indefinitely denied millions of dollars per year of its MSA payments, with the total amount due to Montana and improperly withheld from Montana growing every year.

45. The Montana Supreme Court held that the dispute was not arbitrable.[16] The Defendants then sought rehearing from the Montana Supreme Court, which was denied.[17] The Defendants then petitioned the U.S. Supreme Court for a writ of certiorari, which was also denied.[18] The case finally returned to this Court for litigation in 2010. The Defendants then sought and obtained a stay in the District Court pending the resolution of their arbitration with all other MSA States. In 2011, the Montana Supreme Court overturned the stay on a writ of supervisory control.[19] One of the Justices filed a concurring opinion noting:

> The defendant tobacco manufacturers' historical—and ongoing—approach to this litigation has been to prevaricate, dissemble, and delay, and that is exactly what they have done here.[20]

46. In 2012, with the Defendants' judicial delay tactics finally exhausted, and the case ready to proceed, rather than proving their allegations in front of this Court, the Defendants conceded *before trial* that Montana's 2003 MSA payment was not subject to an NPM Adjustment, and that the payment reduction they had given themselves was improper. As a result, Montana received the withheld portion of its 2003 MSA payment

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[16] In 2009, the Montana Supreme Court held that, under Montana law, the adequacy of Montana's enforcement efforts is to be litigated, rather than arbitrated. *State ex rel. Bullock v. Philip Morris, et al.*, 2009 MT 261. Desk Reference Tab 5.

[17] DA 07-0299 (Sept. 9, 2009), 352 Mont. At 45a-45b, 217 P.3d at 486-87. Desk Reference Tab 6.

[18] *R.J. Reynolds Tobacco Co., et al. v. Montana ex rel. Steve Bullock*, 130 S. Ct. 3354 (2010). Desk Reference Tab 7.

[19] *State of Montana v. Montana First Judicial District Court*, OP 11-0150 (Mont. 2011). Desk Reference Tab 8.

[20] *Id.* at 19.

in 2014, eleven years after the 2003 MSA payment was due, and eight years after the Defendants asserted their first "dispute" over Montana's enforcement of its Qualifying Statute.

47. The other 45 MSA States arbitrated the Defendants' alleged disputes against them over those States' 2003 MSA payments in a single national arbitration that lasted from 2009 to 2013, with subsequent appeals continuing through 2017. Only fifteen MSA States arbitrated all the way through to a decision over the 2003 payment year. Three years into that first arbitration, twenty-one of the MSA States succumbed to the impossibility of resolving all of the Defendants' outstanding alleged disputes over the NPM Adjustment (of which there were seven by that point) through never-ending, costly arbitrations and, in late 2012, committed to a secondary agreement drafted by the Defendants that was initially introduced as the "Term Sheet." These 21 MSA States and the 15 other MSA States that joined the Term Sheet in later years are referred to as the "Term Sheet States" or "TSS." For nearly five years, that secondary agreement remained unfinalized (with its terms unclear and the TSS stuck in a pattern of uncertainty) until the Defendants and the TSS eventually executed the "2017 NPM Adjustment Settlement Agreement" in late 2017. (Both incarnations of this secondary agreement are hereinafter jointly referred to as the "Term Sheet".)

48. The Term Sheet requires each TSS to relinquish 25–54% of the money that Defendants unilaterally withheld from these States' MSA payments in connection with their alleged enforcement disputes, grants significantly expanded discretion to the Defendants over the application of the NPM Adjustment with regard to the TSS, imposes

additional, costly enforcement obligations on the TSS, and exceeds the MSA in both complexity and obscurity.[21]

49. Of the fifteen MSA States that arbitrated the 2003 disputes to a decision, the majority of the States prevailed. Only six were deemed to have failed to enforce their Qualifying Statutes for that payment year. Yet, despite the fact that only six MSA States have *ever* been deemed subject to an NPM Adjustment (after a full evaluation of the three prerequisites), to date the Defendants have withheld payments from *all* 52 MSA States and Territories (46 States,[22] plus Washington, D.C., and five U.S. Territories[23]), and have used this endless dispute-withhold-and-delay tactic to induce 37 of them to succumb to joining the Term Sheet.

50. The second national arbitration, this time over the Defendants' 2004 dispute, began in 2016 and is still ongoing, with no end in sight. No decisions regarding the Defendants' asserted disputes with the other MSA States (i.e., the MSA States—other than Montana—that rejected the Term Sheet) have been made in that arbitration.

51. The second Montana litigation, this one over the Defendants' 2004 dispute, began in 2017 and concluded in 2018 when the Defendants, again, conceded *before trial* that Montana was not subject to the NPM Adjustment for 2004. The 2017–2018 litigation

[21] The final version, known as the 2017 NPM Adjustment Settlement Agreement, is 118 pages long.

[22] Four U.S. States—Florida, Texas, Mississippi, and Minnesota—settled with the OPMs and some of the SPMs prior to the execution of the MSA in 1998. These four states are known as the Previously Settled States ("PSS").

[23] The five U.S. Territories that joined the MSA are Puerto Rico, Guam, American Samoa, the North Mariana Islands, and the U.S. Virgin Islands.

advanced all the way through discovery, in which Montana learned that the Defendants' claim that Montana did not enforce its Qualifying Statute is based solely on *national* data, i.e., data that do not—and cannot—possibly indicate anything about enforcement in Montana specifically. Defendants admitted that they did not rely on actual evidence that Montana specifically failed to enforce its Qualifying Statute when they asserted their "dispute" against it for 2004.

52. Even after the Defendants had the opportunity to depose five current and former State employees directly involved in enforcing Montana's Qualifying Statute and to review hundreds of thousands of pages documenting the State's enforcement actions under the Qualifying Statute, the Defendants still had no support for their allegations that Montana failed to enforce its Qualifying Statute in 2004. Hence, they simply dropped their "dispute" against Montana rather than proceeding to trial, but *only after* baselessly withholding a portion of Montana's 2004 MSA payments for eleven years, and *only after* wasting significant State resources in a litigation that they never intended to win. Despite massive amounts of discovery and years of litigation over the 2003 and later the 2004 payments, the Defendants have never identified to Montana or to this Court a single instance of a material violation of the Qualifying Statute that Montana either failed to detect or failed to take enforcement action against.[24]

53. As discussed in more detail below, Montana also learned through discovery in the 2017-2018 litigation of the Defendants' now-conceded 2004 payment "dispute" that

[24] 2017–2018 Discovery Responses of R.J. Reynolds, SPMs, Farmer's, and Philip Morris. Attached as Exhibit 3.

the Defendants collect enormous volumes of Montana-specific data and have considerable insight into Montana's cigarette market. The Defendants' own data do not support the allegation that Montana failed to enforce its Qualifying Statute. Instead, it contradicts that allegation.

54. Finally, in the course of this second litigation, Montana moved this Court for a determination as to which side bore the burden of proof with respect to the Defendants' assertion that Montana did not enforce its Qualifying Statute. On May 9, 2018, the Court ruled that the burden of proof is on the Defendants to establish that Montana failed to enforce its Qualifying Statute.

55. Based on this Court's ruling on the burden of proof and the Defendants' apparent vast insight into Montana's cigarette market, coupled with their inability to identify any actual, material violations of the Qualifying Statute that Montana failed to detect or failed to enforce against, Montana sent a demand letter to the Defendants on January 31, 2019, insisting that they cease withholding money from Montana unless and until they meet their burden of proving that Montana did not enforce its Qualifying Statute.

56. In a letter to the Montana Attorney General's Office dated March 8, 2019 and signed by counsel for R.J. Reynolds, Elli Leibenstein and Charles Hansberry,[25] the

[25] The letter speaks on behalf of "the PMs" collectively. Follow-up emails dated March 14, 2019, between Mr. Hansberry and the Attorney General's Office reveal that the letter was written on behalf of R.J. Reynolds, Santa Fe Natural Tobacco Company, Philip Morris USA Inc., Sherman's 1400 Broadway N.Y.C., LLC, Farmers Tobacco Co. of Cynthiana, Inc., Commonwealth Brands, Inc., Compania Industrial de Tabacos Monte Paz, S.A., House of Prince A/S, ITG Brands, LLC (formerly Lignum-2, LLC.), Japan Tobacco International U.S.A., Inc., King Maker Marketing, Inc., Kretek International, Inc., Liggett Group LLC, Peter Stokkebye Tobaksfabrik A/S, Premier Manufacturing, Inc., P.T. Djarum, Scandinavian Tobacco Group Lane Ltd (formerly Lane Limited), Tabacalera del Este, S.A. (TABESA), Vector Tobacco Inc., and the Von Eicken Group.

Defendants refused to cease withholding from Montana; threatened to force arbitration if Montana pressed the issue; claimed broad entitlement to assert any disputes they wished based solely on language in the MSA governing how (legitimately) disputed payments are to be handled; claimed that any data or information they possess about Montana does not make the disputed payments any less disputed; and affirmatively reasserted that "each of their annual payments to Montana is subject to an NPM Adjustment because Montana did not diligently enforce a Qualifying Statute for each sales year."

57. Finally, in the same March 8, 2019 letter, the Defendants stated:

> Indeed, no diligent State, including Montana (assuming *arguendo* that Montana is determined to be diligent), gets any portion of the DPA funds or withheld funds for a particular year unless and until all States are determined diligent for the relevant year; that determination has not been made for 2004 or any subsequent year.[26]

Thus, the Defendants reasserted their entitlement to indefinitely deprive Montana of millions of dollars of Montana's MSA payments for every year through the present without any evidentiary basis for asserting enforcement "disputes" against Montana, without initiating action to resolve such disputes, and without ever actually proving their allegations against Montana.[27]

This list encompasses all of the Defendants here. Counsel representing all of these Defendant companies were copied on the March 14, 2019 emails. None objected to the characterization of the letter as being sent on behalf of their clients.

[26] March 8, 2018 Leibenstein Letter, Ex. 1.

[27] The IA-calculated Maximum Potential NPM Adjustments for sales years 2006-2018 (payment years 2007-2019) range from 9.92% to 14.66% of Defendants' annual MSA payments. *PricewaterhouseCoopers* Notice IDs 0315, 0337, 0363, 0398, 0435, 0472, 0502, 0531, 0560, 0563, 0566, 0569, and 0571; Attachments 4(b).

How the Scheme Is Implemented

58. Each year, the Defendants draft and send a letter to the IA and the MSA States that asserts their entitlement to the Maximum Potential NPM Adjustment solely on the basis of the Market Share Loss and Significant Factor determination (i.e., solely on the basis of only two of the three prerequisites for an NPM Adjustment).[28] In doing so, the Defendants disregard the express language of the MSA, which permits *only* the Available NPM Adjustment (which can be as low as $0) to be applied to their payments, and which also makes clear that the *actual* Available NPM Adjustment depends on which States—if any—did not have or did not enforce a Qualifying Statute. The Defendants also disregard the fact that their claim to being automatically entitled to the Maximum Potential NPM Adjustment was already arbitrated and rejected.

59. Specifically, the Defendants' argument was rejected in 2011 by the Arbitration Panel in the first national arbitration (regarding the 2003 NPM Adjustment) involving the other MSA States.[29] Yet the Defendants still unilaterally assert entitlement to the Maximum Potential NPM Adjustment each year in "dispute" letters sent to the IA, and accordingly continue to withhold payments from the MSA States. The statute of limitations has clearly run on any claims the Defendants have that they are entitled to the Maximum Potential NPM Adjustment when only the first two prerequisites for an NPM

[28] Each of the 18 Defendants listed above sends one or more letters each year between March and April. Some of those letters are sent on behalf of one Defendant, some are sent on behalf of several Defendants. Copies of those letters are available upon request if the Court or any of the Defendants feels they are necessary in order to meet the specificity requirements of Mont. R. Civ. P. 9(b).

[29] *In the 2003 NPM Adjustment Proceedings*, Order Re: PMs Request for Order Re: Independent Auditor Authority, JAMS Ref. No. 110053390 (May 23, 2011), attached as Exhibit 4.

Adjustment are met. The IA has refused to apply the NPM Adjustment to the Defendants' payments since 2006.

60. The 2003 Arbitration Panel aptly noted that the Defendants' assertion that the MSA somehow automatically "entitles" them to the Maximum Potential NPM Adjustment based only on the first two prerequisites (Market Share Loss and Significant Factor)—if accepted—would deny the benefit of the MSA bargain for States like Montana:

> If the panel ordered the Auditor to withhold payments across the board from all states, prior to diligent enforcement determinations, even States whose diligent enforcement is ultimately not challenged by the PMs would be deprived of the benefit of their bargain in executing the MSA to recoup monies spent on remedying the effects of smoking related health care costs. This seems fundamentally unfair, and contrary to the purpose of the MSA.[30]

61. Though not binding, the Arbitration Panel's decision is instructive. Montana has always ended up being a "State[] whose diligent enforcement is ultimately not challenged by the PMs" (after Defendants conceded their "disputes" against Montana for both 2003 and 2004), and through the Defendants' ongoing withholding of MSA payments, Montana is unquestionably being "deprived of the benefit of [its] bargain in executing the MSA to recoup monies spent on remedying the effects of smoking related health care costs." *Id*.

62. Each year, each Defendant withholds part of the MSA payment it is contractually obligated to make, either by locking it in a Disputed Payments Account

[30] *Id* (emphasis added).

("DPA")[31] or simply by refusing to pay and retaining it.[32] While the mechanics of the Defendants' withholdings differ from one Defendant to the next, and from one year to the next, from the perspective of Montana, the only difference between (a) funds withheld through the DPA, and (b) funds withheld through refusal to pay, is that the former are summarized by the IA in annual "DPA balance" notices that provide some limited transparency, while the latter lack any transparency whatsoever and are difficult for a State to quantify.

63. The Defendants withhold in unison on the assertions that: (1) they are collectively entitled to the Maximum Potential NPM Adjustment, and (2) they are entitled to reduce every State's MSA payment—including Montana's—unless and until all States prove through litigation or arbitration that they both have and enforced a Qualifying Statute during the year subject to payment. Currently, the Defendants have withheld between 10%

[31] The Defendants characterize their placement of funds in the DPA as "*paying* into the DPA," but in reality, it is not payment at all. Depositing funds into the DPA is more appropriately characterized as "withholding" given that DPA money is kept out of Montana's reach or control. The Defendants' continued control of the funds after placing them into the DPA is evidenced by several undisputed facts: (1) only a Defendant—not an MSA State—can unilaterally authorize that a portion of the DPA funds be released; (2) only a Defendant—not an MSA State—can retroactively decide that certain funds placed into the DPA for a given payment year are to be netted out of that Defendant's MSA payment due in a later payment year; and (3) only Defendants—not an MSA State—have ever engaged in transactions with respect to the ownership rights over the DPA balances, where one Defendant sells the rights to its DPA balance to another Defendant. All of these are examples of things that the Defendants have *actually* done—and continue to do—with the funds they place into the purportedly neutral DPA demonstrate that the Defendants treat the DPA as their own property, and <u>not</u> as a neutral holding account that both sides—the States and the Defendants—are equally precluded from accessing prior to a "dispute" resolution.

[32] Information regarding which Defendants withheld how much and when is contained in *PricewaterhouseCoopers* Notice IDs 0576, 0577, and 0578, attached as Exhibit 5.

and 15% of Montana's annual MSA payments due for 2006 through the present—over $43 million dollars.

64. In the March 8, 2019 Leibenstein letter, the Defendants collectively asserted that they are entitled to withhold from Montana solely because they *say* that they have a "dispute" with Montana over whether Montana enforced its Qualifying Statute and imply that whatever evidence they do or do not have "does not affect the fact that the payments are disputed."

65. This behavior is at the heart of the Defendants' scheme and it is what makes the scheme improper and illegal. The Defendants' perennial and unsubstantiated assertions of a "dispute" for each and every year are made in bad faith. Every year without fail (and without consideration to Montana-specific facts or circumstances), the Defendants assert a "dispute" over Montana's enforcement of its Qualifying Statute and withhold millions they owe Montana on the pretext of that "dispute," despite having no reasonable belief that Montana did not enforce its Qualifying Statute. Moreover, the Defendants implement this same scheme year after year knowing that even a naked assertion of a "dispute" without any merit or credibility makes it effectively impossible for Montana to recover the improperly withheld amounts *for many years and even decades*. Simply put, every year without fail, the Defendants continue to knowingly and willingly abuse the dispute-resolution provisions of the MSA in order to withhold payments, deprive Montana of the benefits of the MSA bargain, and extort State after State to join onerous secondary settlements that contradict and undermine the MSA.

66. No part of the MSA could reasonably be read to include a requirement that

each year's MSA payment must be litigated, at substantial cost, in perpetuity, and with ever-increasing delays. *See* § 1-3-233, MCA (interpretation must be reasonable). Nor, for that matter, can the MSA reasonably be read to grant to the Defendants unfettered discretion to assert "disputes" that lack a reasonable factual basis and with knowledge to the contrary.

Defendants Admitted to Having No Basis for Disputing Montana's Enforcement of its Qualifying Statute when they Withheld Montana's MSA Payments

67. Montana first became aware of the Defendants' total lack of basis for the asserted "disputes" against it in 2018 during the depositions of the two principal actors in the scheme, Philip Morris and R.J. Reynolds. The designated corporate representatives of both companies admitted in sworn testimony that they had no basis for believing that Montana did not enforce its Qualifying Statute when they asserted that Montana's 2004 MSA payment should be reduced because of the supposed "dispute" and accordingly withheld millions of Montana's 2004 MSA payment for over a decade until 2018 when they finally conceded the baseless dispute. While Montana ultimately recovered the improperly-withheld portion of its MSA payment for 2004, the Defendants continue to employ the very same scheme to withhold over $43 million of Montana's MSA payments for all years from 2006 through the present.

A. Defendant Philip Morris

68. In his May 8, 2018 deposition, Philip Morris USA's Rule 30(b)(6) corporate representative, Agustin Rodriguez, admitted that Philip Morris does not consider any information specific to Montana before it withholds part of Montana's MSA payment. As

of the date of his deposition in 2018, Mr. Rodriguez could only point to the *ex-post* theories of Philip Morris's litigation counsel, developed many years *after* Philip Morris "disputed" Montana's enforcement of its Qualifying Statute by withholding a portion of Montana's 2004 MSA payment.

69. Mr. Rodriguez's testimony regarding the support for Philip Morris's "dispute" of Montana's enforcement consisted of evasion, gambling on incorrect legal assertions, and hiding behind a façade of ignorance as to Montana's actual enforcement. Specifically, Mr. Rodriguez (1) expressed "Philip Morris's opinion [] that Montana has the burden of proving that it diligently enforced its escrow statute[33] for the time period in question" (Rodriguez Tr. 18:20-23)—an opinion that directly contradicts the burden-of-proof ruling of this Court; (2) claimed that "really, the company has very little information outside of this litigation, outside of the documents that Montana possessed and that Montana produced in this proceeding, very little information" (Rodriguez Tr. 19:13-16)[34]; and (3) could only think of a single piece of Montana-specific evidence that, in fact, supports that Montana did indeed enforce its Qualifying Statute: "with respect to Montana's specific information is I know that the Montana AG, I believe, in 2002 issued a press release in which the AG's office announced that it was filing lawsuits against some number—and I don't remember the number—of NPMs. Other than that, ***the information that we have I would categorize as national in scope, not Montana-specific*** that—in terms

[33] "Escrow statute" is another way of referring to a Qualifying Statute.
[34] The entirety of Mr. Rodriguez's deposition was filed with the Court in 2018 and is in the record.

of Montana's enforcement efforts." (Rodriguez Tr. 20:12-21, emphasis added)

70. Thus, based on Philip Morris's own 30(b)(6) witness testimony, the *only* information Philip Morris considered at the time of withholding Montana's payments was "national in scope, not Montana-specific"—i.e., information that indicates *nothing* about Montana's enforcement. Mr. Rodriguez went on to state that he "wouldn't have any such information [regarding specific enforcement deficiencies in Montana] other than what's been produced in this litigation and is subject to the privilege … Now, generally speaking, ***on a national basis***, we [Philip Morris] have information and information from the arbitration that speaks to ***national trends*** and ***national issues*** that we've seen with respect to NPM proliferation that we saw with respect to NPM proliferation during that time frame, for example, when [the ***national***] ***share of NPMs*** went from 0.5 percent before the MSA to 8 percent around this time frame. That is the type of information that I'm aware of." (Rodriguez Tr. 21:17-22:5, emphasis added) In summary, every time Mr. Rodriguez was asked about Philip Morris's basis for asserting a dispute over Montana's enforcement, he offered an answer that had nothing to do with Montana and inevitably pointed back to what Philip Morris claims to have observed *nationally*.

Q Can you tell me, please, what opinions has Philip Morris held regarding Montana's enforcement efforts for the relevant time period?
A Well, I'm not sure I understand your question. We have a number of pleadings that we have rendered in this proceeding.
Do you have a specific question about something that we've raised in those pleadings?

Q I'm asking what is Philip Morris's opinion regarding Montana's enforcement efforts for the relevant time period.

MR. SHAKNES: Let me interject for a second. I just want to caution you that any conversations you may have with your litigation counsel in this proceeding regarding the counsel's opinions of the strengths and weaknesses of Montana's claim of diligent enforcement would be protected by the attorney work-product doctrine and attorney-client privilege.

A Do you want to make your question more specific?

Q Well, let's start here: Does Philip Morris have an opinion on Montana's enforcement efforts for the relevant time period?

A Well, I guess the way -- I'm trying not to make this difficult for you, but, I guess, the way you're asking the question is very broad. So why don't we just start with Philip Morris's opinion is that Montana has the burden of proving that it diligently enforced its escrow statute for the time period in question.

Q Does Philip Morris have any knowledge or information that it believes is evidence that Montana

did not diligently enforce the escrow statute in the relevant time period?

MR. SHAKNES: Again, I want to caution you that your discussions with your litigation counsel or the counsel's opinion of the strengths and weaknesses of Montana's claim that it diligently enforced will be protected by the attorney work-product and attorney-client privilege.

But if the company has information outside of what you may have discussed with counsel as part this litigation, then feel free to answer that.

THE WITNESS: Yeah.

A And so, really, the company has very little information outside of this litigation, outside of the documents that Montana possessed and that Montana produced in this proceeding, very little information.

Q Well, based on the documents that have been produced and what Philip Morris does have as far as information regarding Montana's enforcement efforts, has Philip Morris formed an opinion regarding any of Montana's enforcement efforts for the relevant time period?

MR. SHAKNES: And, again, I want to caution you that the opinion of your litigation counsel in this proceeding -- opinion of litigation counsel in

this proceeding of the merits of Montana's claim of diligent enforcement and your discussions with your counsel with respect to counsel's opinions is quintessential attorney work-product and attorney-client privilege.

But if you have information outside -- you or the company has information outside of those discussions, then by all means.

THE WITNESS: Yeah.

A And the only information that I can think of that I would have outside of that category would be a couple of examples. And one would be, you know, with respect to Montana's specific information is I know that the Montana AG, I believe, in 2002 issued a press release in which the AG's office announced that it was filing lawsuits against some number -- and I don't remember the number -- of NPMs.

Other than that, the information that we have I would categorize as national in scope, not Montana-specific that -- in terms of Montana's enforcement efforts.

MR. LEISHER: Kristina, could you hand Document A to Mr. Rodriguez, please.

And we're going to mark this Exhibit 149.

(Exhibit 149 was marked for identification

and is attached to the transcript.)

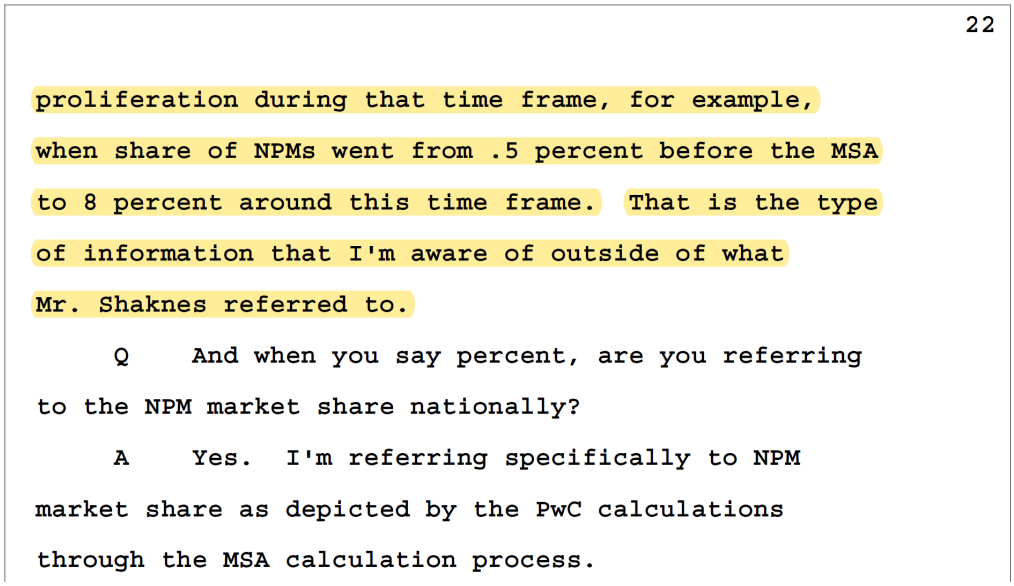
Q Mr. Rodriguez, before I ask you some questions about this document, let me ask you: Does Philip Morris believe that Montana did anything wrong as far as its enforcement efforts for 2003 to 2004?

MR. SHAKNES: And, again, I want to caution you that opinions of your litigation counsel about the merits of Montana's claim of diligent enforcement and your discussions with your litigation counsel in connection with these proceedings about the merits of Montana's claim and possible responses that we may have to Montana's claim are attorney work-product and attorney-client privilege communications.

THE WITNESS: Right.

A And so to stick with your question, Mr. Leisher, anything wrong, I believe is how you phrased it, I wouldn't have any such information other than what's been produced in this litigation and is subject to the privilege that Mr. Shaknes just referenced.

Now, generally speaking, on a national basis, we have information and information from the arbitration that speaks to national trends and national issues that we've seen with respect to NPM proliferation that we saw with respect to NPM



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proliferation during that time frame, for example, when share of NPMs went from .5 percent before the MSA to 8 percent around this time frame. That is the type of information that I'm aware of outside of what Mr. Shaknes referred to.

Q And when you say percent, are you referring to the NPM market share nationally?

A Yes. I'm referring specifically to NPM market share as depicted by the PwC calculations through the MSA calculation process.

71. It is not possible to draw reliable or meaningful inferences about Montana's market or about Montana's enforcement based on the national data that Phillip Morris claims it considered *exclusively* when deciding to withhold a portion of Montana's MSA payment. While the national NPM market share calculated by the IA for 2006-2018 was 5.4%–7.3% (up from 0.4% in 1997),[35] Montana's NPM market share over the same 12-year period remained much lower at only 1.0%–2.5%. Thus, even if the Defendants had some undisclosed evidence that their Market Share Loss (i.e., the growth in the national NPM market share from less than 0.5% pre-MSA to 5%-7% post-MSA) was primarily, or even partially, due to the alleged failure of some MSA States to enforce their Qualifying Statutes, such hypothetical evidence would not support the assertion that Montana was among the States with deficient enforcement. That is, if the rest of the U.S. tobacco market

[35] *PricewaterhouseCoopers* Notice IDs 0315, 0337, 0363, 0398, 0435, 0472, 0502, 0531, 0560, 0563, 0566, 0569, and 0571; Attachments 11(a) report the PMs' combined national market share for each year. The national NPM market share for each year is calculated as the residual, i.e., 100% – PM market share %.

looked like the Montana market, even the very first prerequisite for an NPM Adjustment—that of a PM Market Share Loss of more than 2%—would not be satisfied, and the NPM Adjustment would not come into play at all. *See* MSA § IX(d)(1)(A)(i) (subtracting the first two percentage points from the base market share for calculating Market Share Loss).

72. Furthermore, the national data that Phillip Morris *exclusively* considered when deciding to withhold a portion of Montana's MSA payments is also severely skewed by the four states that are not part of the MSA—Florida, Texas, Mississippi, and Minnesota. Because these States have no escrow requirements for NPMs, and for many years imposed no additional costs to NPMs that would mimic the additional settlement costs of the PMs (Florida *still* does not impose any such costs), these States have disproportionally large NPM sales that not only dwarf Montana's NPM sales, but are also a major driver in the growth of the national NPM market share over time. For example, in 2004 the Florida Senate reported that NPM market share in Florida was as high as 16%,[36] more than double the national NPM market share of 6.2%,[37] and *eight times* Montana's 2004 NPM market share of 2%.[38]

[36] *Florida Tobacco Settlement and Nonsettling Manufacturers*, November 2004, Report # 2005-157, prepared for the Florida Senate by the Committee on Regulated Industries: "The Division [of Alcoholic Beverages and Tobacco] estimates that 16 percent of the Florida market share is held by nonsettling manufacturers." (p. 8) *See* archive.flsenate.gov/data/publications/2005/senate/reports/interim_reports/pdf/2005-157rilong.pdf.

[37] *PricewaterhouseCoopers* Notice ID 0265, Attachment 11(a), reports the PMs' combined national market share for sales year 2004 to be 93.8%, with the residual 6.2% representing the national NPM market share.

[38] Tobacco Memo (attached to the State's *Brief in Support of Motion for Declaratory Order*, filed March 24, 2017, in this cause number).

B. Defendant R.J. Reynolds

73. Like Philip Morris, R.J. Reynolds also did not consider Montana-specific information at the time it withheld part of its MSA payments to Montana. In his May 2, 2018 deposition, R.J. Reynolds' Rule 30(b)(6) corporate representative, Thomas McKim, testified that R.J. Reynolds also withheld part of what it owed Montana based solely on: (1) purported *national* "evidence that the states ***generally*** were not diligently enforcing [given] the significant growth of NPM volume in the marketplace ***generally***" (McKim Tr. 20:7-9, emphasis added); (2) information regarding "the states ***generally***" that "is not so much limited to particular states" regarding "the existence of … impossibly low-priced cigarette[s]" (McKim Tr. 20:10-14, emphasis added);[39] and (3) the fact that while the Defendants concede that "the vast majority of states have qualifying statutes and [] don't dispute that," they "do dispute [whether] the small number of the specifically identified states have qualifying statutes" (McKim Tr. 21:6-17)—a moot issue with regards to Montana since the Defendants concede that Montana has always had a Qualifying Statute.

74. Thus, Mr. McKim admitted that the *only* state-specific issue that R.J. Reynolds considers at the time of asserting its conveyor-belt disputes against every MSA State for every year is whether an individual State has a Qualifying Statute, not whether

[39] The mere existence of "low priced cigarettes" does not indicate a violation of Montana's Qualifying Statute, and simply means that there is some level of competition in the marketplace that protects consumers from paying inflated monopolistic or oligopolistic prices. Furthermore, what Mr. McKim characterized as "impossibly low-priced cigarettes" are, in fact, cigarettes sold by low-cost, low-markup manufacturers who utilized various *legal* strategies available to them under the Qualifying Statute to *legally* minimize their escrow obligations and pass such savings down to consumers in the form of lower prices.

the individual State enforced its Qualifying Statute during the year subject to payment. Based on R.J. Reynold's own 30(b)(6) witness testimony, prior to asserting a "dispute" over Montana's 2004 enforcement, and prior to withholding a portion of Montana's MSA payment for 2004, the Defendants did not review *any* Montana-specific information to determine whether they had grounds for such a dispute against Montana specifically. It was only in 2017, when Montana initiated litigation to resolve the 2004 "dispute," that the Defendants allegedly *first* considered any state-specific information regarding Montana's enforcement actions during 2004. And then R.J. Reynolds, like the rest of the Defendants, conceded the dispute before trial.

75. Like Mr. Rodriques for Philip Morris, Mr. McKim went on to state that R.J. Reynolds' "skepticism that the states were diligently enforcing" was based on "concerns about the rapidly growing volume of NPM product" in the *national* market.

Q. Now, Mr. McKim, can you give me your best recollection of what those responses to PWC's information requests say?

A. It is -- I think I can do it reasonably accurately, but I think the gist of that response is focused on whether or not we dispute whether or not any of the states have qualifying statutes. I believe there is a question in the information response just asking whether or not all the states -- we agree that all the states have qualifying statutes, and overtime there have been at least a couple states, perhaps several, as to which we do dispute whether or not they're qualifying the statutes that they enacted in an effort to have a qualifying statute were, in fact, a qualifying statute. I believe that was the case specifically with among others New Mexico, I think perhaps also Virginia. I'm

not absolutely certain. I'm quite certain that New Mexico is on that list, but anyway, we note the fact that we don't believe that one or more states have qualifying statutes.

And then there is some reference to, in essence, the marketplace conditions that suggest to us as -- as evidence that the states generally were not diligently enforcing where we note the significant growth of NPM volume in the marketplace generally. I think that part of the statement is not so much limited to particular states, it's more of a commentary of the states generally. I think we note the existence of, I'm not sure we refer to it this way, but what I would refer to currently as impossibly low-priced cigarette. Cigarettes that appear to be in the marketplace at price points that would not support the cost of manufacturing the product, plus federal excise tax, plus, you know, distribution, plus escrow payments to the extent they're NPM brands. And so, we take note of that. That's what I can recall at the moment.

Q. Now, am I understanding correctly that in response to the question from PWC regarding qualifying statutes, that response is -- is state specific; is that correct?

A. No, their information request is kind of a -- is

not really crafted in terms of how they make -- they make their inquiries on a state specific basis. They --

Q. And, I'm sorry, my question was not as to their question, but your response lists which states you believe do not have a qualifying statute; is that right?

A. Only in that respect, that's right, because the vast majority of states have qualifying statutes and we don't dispute that. It's only a small handful of states that we have that issue with. So, we don't go through the process of listing all the states we think have a qualifying statute, we simply note that we do dispute that the specifically identified, the small number of the specifically identified states have qualifying statutes.

Q. And that's the only part of your response that's state specific, right?

A. I believe that's the case, yes.

Q. You look or does RJR look at what individual states have done as far as diligent enforcement before drafting that response?

A. Well, that gets -- that's perhaps a more complex question than you might think. You know, we have had a long process of dealing with the states on the issue of diligent enforcement. We have expressed since very early days operating under the MSA or skepticism that

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the states were diligently enforcing. And I say that broadly because in the early days, typically we were having those conversations with the states primarily in the context of the semiannual meetings that were called for under the MSA, and at virtually every one of those meetings early on, we would we would express our concerns about the rapidly growing volume of NPM product and observe that we -- we were surprised, we would -- we were left to conclude in light of that the rapid growth that the states must not be enforcing the escrow statures. Overtime we had we made inquiries to the states and asked them to provide us with information regarding what efforts they were making to diligently enforce their statutes.

76. As explained above, the Defendants cannot, in good faith, base their decision to withhold a portion of Montana's MSA payments on only national data, because many factors *in states other than Montana* drive up the national NPM market share. In fact, R.J. Reynolds admitted that much back in 2005 in its *Initial Submission, In the Proceeding Before the Firm Pursuant to Section IX(d)(1)(C) of the Master Settlement Agreement*, where—among other factors and drivers—it discussed the undeniable role of the four PSS (Florida, Texas, Mississippi, and Minnesota) in the growth of national NPM sales.

77. Much like the boy who cried wolf every day without seeing a wolf, the Defendants cry "dispute" over Montana's enforcement practices every year without seeing state-specific evidence of Montana's alleged lack of enforcement. Defendants lodge annual disputes against Montana and use these pro-forma disputes as a pretext to withhold

millions of dollars in MSA payments that they are contractually obligated to pay Montana every year, without regard to the evidence, data, records, or other information specific to Montana. Year after year, the Defendants' strategy remains to "cry 'dispute' today," and worry about whether there are any grounds for a colorable dispute against Montana *many years later*, when Montana—not the Defendants—initiates litigation.

78. In conclusion, Philip Morris's and R.J. Reynolds's bald admissions that both companies only consider national data of the PMs' national market share loss to the NPMs when deciding to withhold money from each and every MSA State–including Montana—carries a clear message: if the MSA States do not help Defendants maintain their market share, the Defendants will withhold MSA payments from the States and will force the States into endless, expensive, and increasingly inefficient litigation and arbitration proceedings, regardless of what each State did or did not do with regards to enforcement. The Defendants will then maintain the pressure of endless litigation and ever-growing amounts of withheld payment until each State agrees to further, costly obligations designed to protect the Defendants' market share and agrees to make it easier for the Defendants to continue to withhold more money in later years.

The Defendants' Have Substantial Documents, Information, and Data on Montana's Enforcement—None of Which Show Enforcement Failures

79. Despite claiming ignorance of Montana-specific facts when asserting their "disputes" again Montana, in the ordinary course of business, the Defendants collect and have amassed substantial information regarding Montana's cigarette market and Montana's enforcement actions—information that does not support the allegation that

Montana did not enforce its Qualifying Statute. If anything, the information that the Defendants possess contradicts their assertion that Montana did not enforce its Qualifying Statute.

80. First, Philip Morris and R.J. Reynolds both collect detailed sales data from Montana's cigarette wholesalers and retailers. As noted above, at any given time the PMs supply over 97.5% of the cigarettes in the Montana market. Both Philip Morris and R.J. Reynolds have contracts with the overwhelming majority of licensed cigarette wholesalers in Montana that require the wholesalers to submit detailed data for *all shipments of both PM and NPM cigarettes* that the wholesaler makes to a Montana retailer, specifying the manufacturer, brand, quantity of cigarettes shipped, and the specific retailer to whom they were shipped. In fact, the detailed sales data routinely collected by both R.J. Reynolds and Philip Morris are the backbone of the OPMs' post-MSA marketing activities. Since Defendants are no longer allowed to advertise their deadly products directly to consumers, their marketing strategies are centered on financially incentivizing wholesalers and retailers to push their brands over other brands at the point of sale. Both Philip Morris and R.J. Reynolds depend on detailed sales data to tell them which specific wholesalers and retailers are their top "wholesale partners" or "retail leaders" and should be rewarded for prioritizing their brands over competitors' brands versus which specific wholesalers and retailers need to be reminded to do so.

81. Moreover, the Defendants maintain regular in-person contact with Montana's wholesalers and retailers through their trade representatives and extensive sales force. According to Mr. McKim, just in 2003-2004, R.J. Reynolds alone had "something

north of 24,000 [in person] contacts with wholesalers and retailers" in Montana. Indeed, as Mr. McKim articulated in his deposition, the job of the trade reps is to "feel the heartbeat of the community."

82. Defendant Philip Morris also collects detailed sales data through two programs: STARS and IRI/Capstone.[40] Philip Morris uses these programs in part to track the success of Montana's enforcement actions in reducing the NPM market share in the State.[41] Moreover, the Defendants have collectively proffered the STARS data in the two national arbitrations against the rest of the MSA States as purported evidence that other MSA States allegedly failed to enforce their Qualifying Statutes, yet they have never asserted that the same data suggest an enforcement failure by Montana.

83. Second, in 2005 the Defendants made a public records request for documents related to Montana's enforcement of its Qualifying Statute. On February 25, 2005, attorney Shane Coleman sent a public records request to the Montana Department of Justice on behalf of Philip Morris, R.J. Reynolds, and Lorillard asking for all documents that fell within a number of broad categories related to enforcement of the Qualifying Statute. In response, the Montana Department of Justice produced some 50,000 pages of documents. None of the Defendants have made another public records request since. Instead, the Defendants have adopted the tactic of pretending to be ignorant of Montana's enforcement

[40] *See* Alex Shaknes letter dated May 24, 2018, explaining and describing Philip Morris's data collection and data summary reports prepared for the 30(b)(6) witness, attached as Exhibit 6.

[41] PM USA, Montana NPM Share—STARS, attached as Exhibit 7 (filed under seal due to assertions of confidentiality by Philip Morris).

actions in order to maintain the façade of a "bona fide dispute."

84. Third, much of Montana's enforcement record is in the public domain. For example, the Montana Tobacco Product Directory has been online since 2003. The Defendants can easily compare the approved NPM manufacturers and NPM brands with the NPM brands sold in the State as captured by the comprehensive data they collect from wholesalers and retailers in Montana to identify and quantify any significant sales of NPM brands in violation of the Qualifying Statute. If the Defendants have ever seen valid evidence of such violations—much less evidence of systemic violations—they have not brought it to Montana's attention.

85. Fourth, all court cases filed by Montana against NPMs, wholesalers, and other market participants in connection with violations of the Qualifying Statute are also part of the public record. The vast majority of these cases are filed in this Court.

86. Fifth, the Defendants' previously-described voluminous data come from virtually all of the same wholesalers from whom Montana also obtains data as part of its enforcement program. As such, the Defendants see almost exactly the same PM and NPM sales and the same PM vs. NPM market shares in their data that Montana sees in its data. Moreover, the Defendants even audit these wholesalers on a regular basis and thus again see that the NPM presence in Montana is accurately monitored by the State and remains far lower than the NPM presence in the national market. Moreover, the Defendants have never identified any of the audited wholesalers as problematic or provided a copy of an audit to Montana that suggested any enforcement issues.

87. Sixth, both Philip Morris and R.J. Reynolds have historically expended

substantial resources to retain lobbyists in the State who track tobacco activities and appear before virtually every legislative session. For example, the parent company of Philip Morris, Altria, alone spent over $17 million to defeat the November 2018 Initiative 185 ("I-185") to raise the tobacco tax and to institute a tax on vaping products. Altria then continued to expend additional funds for lobbying the Montana legislature in 2019. Similarly, in late 2018, the parent company of R.J. Reynolds, RAI Corporation, contributed $300,000 to defeat I-185 in addition to the funds it expended on the 2019 legislature. Indeed, both OPMs routinely devote substantial resources to track Montana's legislative activities, which are an element of Montana's enforcement. *See* Montana Commissioner of Political Practices, *Lobbyist and Principal Database*, https://app.mt.gov/cgi-bin/camptrack/lobbysearch/lobbySearch.cgi.

88. Seventh, the Defendants have obtained large volumes of documents and information from other MSA States regarding Montana's participation in coordinated multi-state enforcement actions against specific NPMs and multi-state licensed wholesalers—actions that span numerous years and several continents.

89. Eighth, the Defendants have further obtained hundreds of thousands of pages in discovery in the 2006–2012 litigation (of the 2003 "dispute") and the 2017–2018 litigation (of the 2004 "dispute") and deposed five key Montana witnesses knowledgeable about Montana's enforcement program over many years. If the Defendants believed that they had found any evidence within that body of documents and deposition transcripts that indicated a material violation of the Qualifying Statute by an NPM that Montana failed to detect or failed to take enforcement action against, such hypothetical evidence was never

mentioned by the Defendants,[42] who abandoned both "disputes" to avoid their day in court.

90. Finally, documents produced by Philip Morris in the 2017–2018 litigation also show that Defendants clearly recognized that Montana's passage of Complementary Legislation (which created the Tobacco Product Directory) [43] in early 2003 further strengthened Montana's already robust enforcement of its Qualifying Statute. Enacting Complementary Legislation radically enhanced the enforcement landscape in Montana, and Philip Morris clearly recognized this. For example, a slide from an internal Philip Morris presentation dated October 19, 2004, shows that the company was aware of the low NPM market share in Montana to begin with and was tracking its further decline following Montana's passage of Complementary Legislation.[44] Specifically, the slide contains a graph with two lines: one line representing the monthly NPM market share in Montana, and a second line representing the monthly NPM market share in other MSA States that had not yet passed Complementary Legislation as of the time of Philip Morris's analysis. The graph shows the two lines moving closely together until April 2003 and diverging after that date, with the NPM market share in Montana declining over time, while the NPM market share in the other MSA States without Complementary Legislation increases over time and eventually stabilizes at a level nearly twice that of Montana's NPM market share.

[42] *See* Discovery Responses of Philip Morris, R.J. Reynolds, and Certain SPMs, Exhibit 3.

[43] Complementary Legislation is a set of additional statutes that Montana voluntarily enacted in 2003 specifically to expand its set of available enforcement tools and further bolster its effective enforcement of the Qualifying Statute. *See Montana's Brief in Support of Motion for Summary Judgment* filed in this action on April 13, 2018.

[44] PM USA, Montana NPM Share—STARS, attached as Exhibit 7 (filed under seal due to assertions of confidentiality by Philip Morris).

91. Another internal Philip Morris presentation shows its estimates of *state-specific* NPM market share as of June 2003 ranging from 0.0% in some MSA States to 22.5% in other MSA States.[45] Montana is near the bottom of this range, with an NPM market share of only 0.6%. In contrast, the IA-calculated *national* NPM market share in 2003 on which the Defendants admittedly based their withholding of MSA payments was 5.9%[46], nearly ten times Philip Morris's internal estimate of Montana's NPM market share. In fact, yet another internal Philip Morris presentation explicitly states that "NPM sales [were] concentrated in limited number of states."[47] The Philip Morris documents—along

[45] PM USA, Enacted NPM Legislation in 2003 Prior to June, attached as Exhibit 8 (filed under seal due to assertions of confidentiality by Philip Morris).

[46] *PricewaterhouseCoopers* Notice ID 0241, Attachment 11(a), reports the PMs' combined national market share for sales year 2003 to be over 94.1%, with the residual 5.9% representing the national NPM market share (not attached).

[47] PM USA, Recent Proliferation of NPM Brands, attached as Exhibit 9 (filed under seal due to assertions of confidentiality by Philip Morris).

with many others—further demonstrate that the Defendants knew at the time of their withholdings that Montana's market is not accurately represented by the national numbers, and that withholding of MSA payments from Montana on the pretext of national market share loss is unjustified.

92. Like Philip Morris, OPM Brown & Williamson—now part of R.J. Reynolds—also tracked state-specific NPM market shares before and after the passage of Complementary Legislation. A slide from an internal Brown & Williamson presentation dated March 8, 2004, reports that: (1) Montana's NPM market accounted for only 0.3% of the national NPM market (which suggests that national market shares are not indicative of Montana-specific trends and vice versa); (2) Montana's NPM market share was low to begin with, at under 2.5%; and (3) Montana saw an "immediate impact" of the additional legislation in the form of 0.31 percentage point decline in its already low NPM market share (from 2.48% down to 2.17%).[48] The same presentation admits that two-thirds of the national NPM volume was accounted for by only "14 important states," of which three are non-MSA States (PSS Florida, Texas, and Mississippi) and ten are Term Sheet States. Not surprisingly, Montana was not among the "14 important states" that Brown & Williamson identified as the drivers of the national NPM market share.

93. Similarly, a transcript from R.J. Reynolds' Financial Release Conference call conducted on January 28, 2003 expressed R.J. Reynolds' view that the Complementary Legislation enacted by Montana in 2003 effectively made the Qualifying Statute "self-

[48] Brown & Williamson, States w/ Both Legislations in Effect: Strong Evidence of Impact, attached as Exhibit 10 (filed under seal due to assertions of confidentiality by R.J. Reynolds).

enforcing" going forward:

> The original statute that was the model statute attached to the MSA required state enforcement, and a number of states have begun to enforce that statute; in fact, hundreds of lawsuits have been filed against Non-Participating Manufacturers by the AGs across the country. The benefit of this new statute [known as Complementary Legislation] is that in order to put tax stamps on the product, the wholesaler has to have a certification from the state that the NPM is in compliance with its escrow payments. So it's self-enforcing, and the AGs don't have to do anything further. [Emphasis added.][49]

This statement by an R.J. Reynolds executive shows the Defendants held the same view that Montana holds—that violations of Montana's Qualifying Statute—to the extent that they ever took place at all—became essentially non-existent after the enactment of Montana's Complementary Legislation in 2003. Therefore, the Defendants' assertions of annual "disputes" over Montana's enforcement for each and every year after 2003, with no factual basis to support such assertions, are made in bad faith. The continued assertion of such "disputes" in the face of substantial available evidence that contradicts the Defendants' allegations against Montana is fraudulent.

The Defendants Assert Unreasonable and Unsupportable Positions in Furtherance of Their Dispute, Dissemble, and Delay Scheme

A. The Defendants' Tactic to Delay Resolution of their "Disputes" with Montana

94. First, the Defendants continuously seek to delay the resolution of their fabricated "disputes" with Montana in order to deprive the State of the benefits of the MSA contract, increase the financial and logistical burden on Montana, and thus erode

[49] R.J. Reynolds Tobacco (RJR) Q4 2002 Financial Release Conference Call Event Transcript, attached as Exhibit 11.

Montana's bargaining power in potential negotiations to resolve the "disputes." In the 20 plus-year history of the MSA, the Defendants have never initiated an action to prove their allegations against Montana despite relying on those unproven allegations to withhold tens of millions in MSA payments.

95. As part of their delay tactic, in 2010 the Defendants even bid to stay the first litigation over the 2003 "dispute." As the Montana Supreme Court *Writ of Supervisory Control* concurring opinion overturning the District Court stay aptly noted:

> The problem with any litigation is that the further away in time one gets from the act, the harder it is to prove. Witnesses may become unavailable; evidence may be lost or degraded; the claim becomes stale. Forcing Montana to await the resolution of the nationwide arbitration in another two to three years inherently prejudices the State from an evidentiary standpoint.[50]

Witnesses leave State employment and may move to other States, and even to other countries. Inevitably some will die. Memories fade and documents may be misplaced or their contents become unclear without explanatory testimony. Even though the Court has ruled that the Defendants bear the burden of proving Montana's alleged enforcement deficiencies, the passage of time makes it progressively more difficult for Montana to rebut the Defendants' allegations. The Defendants' continued use of delay tactics, even after being called out for their "prevaricate, dissemble, and delay"[51] approach by the Montana Supreme Court, demonstrates their lack of good faith.

[50] OP 11-0150 at 13.

[51] *Id*.

B. The Defendants' Tactic to Delay Payment to Montana *After* Resolution of their "Disputes" with Montana

96. Second, the Defendants assert that even if their "disputes" with Montana were all fully and finally resolved in Montana's favor, payment to Montana of the improperly-withheld amounts *still* has to be delayed until resolution of the Defendants' pending disputes for the years in question with all other MSA States.[52] This is demonstrably false. In 2018, when the Defendants approached Montana about settling the dispute over the 2004 payment before trial, Montana demanded that full payment of the funds withheld for 2004 be made immediately, including interest. Montana's position was that absent timely payment by the Defendants, the parties would go to trial. Defendants then promptly made payment to Montana of the withheld amounts for 2004 plus interest, demonstrating that making Montana whole is not contingent upon resolution of their disputes with other MSA States. The Defendants' assertion to the contrary is motivated solely by the attempt to further delay Montana's payments and to ensure that Defendants' contractual MSA obligations to Montana are never fully paid-up.

97. As the Montana Supreme Court unambiguously articulated in *Bullock*, and reiterated in the Writ of Supervisory Control denying the stay in the District Court for the 2003 NPM proceeding:

> … the fact remains that the question of whether Montana diligently enforced its Qualifying Statute does not depend, in any way, on what the other Settling States have or have not done. If Montana diligently enforced a Qualifying Statute, the NPM Adjustment does not apply to it; whether the other Settling States did the same is immaterial.[53]

[52] March 8, 2018 Leibenstein Letter, Exhibit 1.

[53] *State ex rel. Bullock v. Philip Morris, et al.*, 2009 MT 261, ¶ 25.

C. The Defendants' Tactic to Deprive Montana of the "Time Value of Money" Due on the Delayed Payments

98. Third, R.J. Reynolds has gone so far as to claim that the Defendants are entitled to the interest on the withheld amounts (i.e., the earnings on the funds locked into the DPA away from the States' reach) *even when a State like Montana prevails in a "dispute."* R.J. Reynolds asserted this position in an August 10, 2017 brief filed in the second national arbitration against other MSA States.[54]

99. The contention that the Defendants are entitled to the interest that has accrued on the withheld amounts over the period of the "dispute" contravenes the plain language of the MSA and lacks any basis in contract, tort, trust, equity or any other aspect of Montana law. Moreover, that contention plainly contradicts common sense—the DPA is simply a type of escrow account, and like any escrow account it accrues earnings, which are eventually disbursed on the principle "earnings follow principal." The Defendants' attempts to now argue for scenarios in which the DPA principal goes rightfully to the State while the earnings go to them is nothing but an opportunistic attempt to rob States like Montana of the time value of the withheld money even when the State finally recovers the principal amounts withheld over a decade later.

[54] Upon learning of this, Montana addressed a letter to the Arbitration Panel pointing out that Montana's interest could be affected by a ruling on that issue and that Montana had not been properly made a party to any arbitration of the issue. As Mr. Leibenstein's March 8, 2018 letter indicates, the Defendants latched onto this statement and claim that it is an admission that disputes over "releases from the DPA" are subject to arbitration. The Defendants habitually misrepresent Montana's positions on various subjects in an effort to force Montana into the significantly more expensive, slower, and undeniably chaotic arbitration. *See State ex rel. Bullock v. Philip Morris* 2009 MT 261, ¶19 ("We reject the PMs' attempts to repackage the dispute in this case as something it clearly is not.").

100. The Defendants' ultimate goal in delaying resolution of their "disputes" with Montana, delaying payment to Montana after resolution of the "disputes," and depriving Montana of the "time value of money" due on the delayed payments is to eventually force Montana into joining the previously-described Term Sheet. Joining the Term Sheet, however, would be detrimental to the interests of Montana's citizens as it would (1) require Montana to voluntarily relinquish approximately $14 million[55] of the more than $43 million that the Defendants have withheld from Montana to date, (2) impose further onerous and unreasonable enforcement obligations on Montana (aimed at expending State resources to reduce the NPM presence and protect the Defendants' market share in Montana), and (3) give the Defendants the express right to unilaterally reduce their MSA payment obligations to Montana going forward. To be clear, it is <u>not</u> Montana's obligation under the MSA (nor under any statute) for the State to protect the market share of the Defendant tobacco companies.

101. In its 2018 Annual Report, Philip Morris's parent company, Altria, characterized the Term Sheet that, through the above-described delay tactics and schemes, the Defendants successfully forced upon 36 MSA States to date[56] as follows:

[55] So far, there are six different "tranches" of MSA States within the Term Sheet, and Term Sheet States in the different tranches relinquish different percentages of the money withheld from them. The amount Montana would have to relinquish if it were to join the Term Sheet would depend on a variety of factors. $14 million is a rough approximation of the amount Montana would likely give up for the years through 2016 if it signed the Term Sheet.

[56] The fraudulent circumstances under which many MSA States were coerced into signing the Term Sheet are evident from the fact that some of those States' enforcement has never been contested in the national arbitration, as well as by the fact that the Defendants have aggressively fought for the opportunity to *defend* the enforcement of any TSS of their choosing in future reallocation disputes with the Arbitrating States—that is for the opportunity for the tobacco

> Both the New York settlement and the multi-state ["Term Sheet"] settlement also contain provisions resolving certain disputes regarding the application of the NPM Adjustment going forward, although the applicability of those provisions with respect to the signatory states that joined the multi-state settlement after 2017 is contingent on satisfaction, in the PMs' sole discretion, of certain conditions. [57]

In other words, through the Term Sheet the Defendants granted themselves "sole discretion" to decide when and which TSS will be subject to NPM Adjustments going forward. Using the described delay tactics and schemes, the Defendants are now trying to similarly exhaust Montana until it surrenders into accepting the same bad deal.

102. In the final analysis, the Defendants have withheld more than $43 million from Montana solely on the grounds that they lost market share to their NPM competitors *nationally* (i.e., in states other than Montana), and insist on holding those funds hostage until Montana caves and agrees not only to relinquish a substantial portion of the funds that it is owed but also to accept expanded ongoing enforcement obligations that would impose an additional toll on State resources *in perpetuity* for the sole benefit of the tobacco companies' economic bottom line. The Defendants' scheme is a win-win for them: either the Defendants successfully coerce Montana into protecting their market share year after year, or they unilaterally reduce the amounts they agreed to pay Montana under the MSA for their decades of lethal deception.

103. To be clear, with this action, the State of Montana is not requesting that the Defendants be ordered to release the funds locked in the DPA, but rather that the

company Defendants to *defend* the enforcement of the very same States whose enforcement they previously disputed with the sole goal of pressuring those States' to join the Term Sheet.

[57] http://investor.altria.com/Cache/1001250336.PDF, p. 80 (emphasis added).

Defendants be ordered to make Montana whole with respect to their unpaid MSA obligations for 2006–present regardless of the funding source for these outstanding payments.

COUNT I—BREACH OF THE DUTY OF GOOD FAITH AND FAIR DEALING—CONTRACT CLAIM

104. The State realleges and incorporates all preceding paragraphs here.

105. Under Montana law, "every contract, regardless of type, contains an implied covenant of good faith and fair dealing." *Story v. City of Bozeman*, 242 Mont. 436, 450, 791 P.2d 767, 775 (1990). "In essence, the covenant is a mutual promise implied in every contract that the parties will deal with each other in good faith, and not attempt to deprive the other party of the benefits of the contract through dishonesty or abuse of discretion in performance." *Beaverhead Bar Supply v. Harrington*, 247 Mont. 117, 124, 805 P.2d 560, 564 (1991) (citing *Story*, 242 Mont. at 450, 791 P.2d at 775).

106. The MSA and the Consent Decree incorporating it are written contracts to which the State of Montana and all of the Defendants are parties.

107. A breach of the covenant of good faith and fair dealing is a breach of the contract, even if no express term of the contract is breached. *Story*, 242 Mont. at 450.

108. The Defendants have breached, and continue to breach, the covenant of good faith and fair dealing by engaging in conduct that includes, but is not limited to:

a. Withholding money due and owing to Montana under the MSA for each and every year from 2006 through the present;

b. Withholding those funds based on the allegation that Montana did not

enforce its Qualifying Statute for each and every year,[58] with no reasonable basis for making that allegation for any year;

c. Alleging that Montana did not enforce its Qualifying Statute when the Defendants have never identified to Montana any evidence of an actual violation of the Qualifying Statute by an NPM that Montana failed to detect or failed to enforce against, much less evidence of systematic failures to justify the allegations of lack of enforcement;

d. Asserting that Montana must litigate these unsupported allegations for each year in order to recover the withheld payments that are rightfully owed under the MSA;

e. Claiming that the Defendants do not know anything about Montana's enforcement (other than it was purportedly deficient) until litigation is initiated and discovery has commenced, despite their established practices of gathering detailed sales data and market information directly from Montana's wholesalers and retailers, their own employees and contractors, other MSA States and NAAG, document and data production in connection with MSA Significant Factor proceedings, publicly available sources, and public records requests—none of which require the commencement of litigation;

f. Forcing Montana to initiate *every* litigation to resolve the asserted "disputes" before it could recover the money it is owed under the MSA, at significant

[58] Currently, the Defendants are withholding part of their MSA payments for the years 2006–2016. They will withhold additional amounts for the years after 2016 over the course of this litigation.

expense to Montana;

g. Asserting that even when Montana's enforcement is not in dispute, Montana still cannot recover the withheld payments unless and until Defendants' other disputes with all other MSA States over the payment year in question are resolved with finality;

h. Contending that even when Montana's enforcement is no longer in dispute, Montana is still not entitled to full interest on the MSA payments improperly withheld from it for over a decade.

109. The Defendants claim discretion under the MSA as to which States they assert disputes against, when they choose to assert those disputes, when they disclose the evidentiary basis for their asserted disputes, and how quickly the States whose disputes are resolved recover the money withheld from them.

110. The Defendants exercise their claimed discretion in bad faith in order to deprive the people of Montana of the benefit of the MSA contract they entered into to end Montana's initial litigation over the Defendants' decades-long deceit.

111. According to the IA, so far the Defendants have collectively withheld $42,726,519.65 of the payments they owe to Montana by locking that money out of the States' reach in the DPA, which allows the Defendants to maintain exclusive control over when funds are ultimately released to Montana.[59]

[59] *See* Exhibit 5: *PricewaterhouseCoopers* Notice ID 0576 – DPA Balances as of April 20, 2019 (sheets 4 and 11). Notice ID 0576 details the amounts put into the DPA on the basis of the asserted "dispute" over the NPM Adjustment.

112. Three Defendants—Farmer's, Liggett, and Vector—have withheld payments both by locking part of their "disputed" amounts into the DPA and also by simply refusing to pay some of what they owe.[60] Montana is currently collecting the information necessary to quantify the exact amounts that those three Defendants have simply refused to pay.

113. Until the Defendants' bad faith scheme is stopped, the amounts owed to Montana under the MSA and withheld *indefinitely* will continue to grow.

114. The Defendants' deliberate withholding of MSA payments that are contractually due to Montana and to every other MSA State for every year by *automatically* alleging "disputes" over enforcement without consideration of any individual State's enforcement during the year subject to payment is comparable to an insurer who habitually refuses to pay on *any* claim made to it without conducting an investigation, simply by alleging a "dispute" over *every* claim without evidence to suggest that a claim is not properly due and owing, all while being in possession of vast amounts of information and evidence supporting the validity of the claims. This is the very definition of bad faith.

COUNT II—BREACH OF THE DUTY OF GOOD FAITH AND FAIR DEALING—TORT CLAIM

115. The State realleges and incorporates all preceding paragraphs here.

116. Montana is in an inherently inequitable position relative to the Defendants.

[60] *See* Exhibit 5: *PricewaterhouseCoopers* Notice ID 0577 and 0578 – Summary of Amounts Due and Payments Made 2000–2019. Notice IDs 0577 and 0578 detail the history of Farmer's, Liggett, and Vector's underpayments. Montana is currently investigating how much of those underpayments are attributable to those three Defendants' assertion of a "dispute" with Montana and how much is due to other asserted disputes.

There are over 30 PMs (including Fortune 500 company Philip Morris) with resources far exceeding the State's. Montana's entire state budget is $6.4 billion per year, only a tiny fraction of which is devoted to MSA and tobacco litigation—and no fraction of which should be devoted to litigation of sham "disputes." Philip Morris's parent company, Altria, has annual revenues of about four times Montana's total annual budget; R.J. Reynolds' parent company, RAI Corporation, alone has annual revenues that are twice Montana's total annual budget; and the list goes on. The Defendants had at least 18 identified attorneys working on the 2017-2018 litigation over the 2004 "dispute" with Montana and countless other attorneys and staff working behind the scenes on Montana's case.

117. The motivation of the parties for entering into the landmark 1998 tobacco MSA was non-commercial and not for profit. Rather, the payment provisions under the MSA (adopted and incorporated in this Court's Consent Decree) were designed to provide reimbursement for part of the financial toll imposed on the State every year in the form of smoking-related healthcare costs. These payments were precisely for "security" and "future protection," much like the payment provisions in an insurance agreement.

118. Ordinary contract damages are not sufficient here because the Defendants' conduct constitutes a scheme to defraud the State. Simply allowing the Defendants to pay what they owe, many years after the withheld amounts were originally due and owing to the State, would not hold the Defendants accountable for their actions, nor would they make the State whole. If ordered to pay only ordinary contract damages (without punitive damages), the Defendants will continue to employ the same scheme in future years because the worst that could happen to them would be that they are eventually obligated by the

Court to pay what they were obligated to pay in the first place under the MSA, and thus there would be no downside to their bad acts. At the same time, the State has already incurred, and will continue to incur, substantial attorneys' fees and costs in connection with litigating "disputes" asserted by the Defendants before it can recover the payments properly due and owing to Montana that were withheld without justification.

119. The State is vulnerable to the Defendants' deliberate delay tactics and calculated schemes. The Defendants fully control what portion of the MSA payments due each year they make on time, fully control what payments are allegedly in "dispute," fully control the timing of all enforcement "disputes" with Montana, and they also fully control when payment of any withheld amount is finally paid to a given MSA State upon resolution of (or, in Montana's case, upon the Defendants' abandonment of) their "dispute" against that State. The Defendants' control over the withheld payments and over the timing of the disputes they choose to assert against Montana forces Montana into an untenable situation with "disputes" being litigated more than 14 years after the year in question. Under the status quo, the time lag between the year subject to a "dispute" and the expected conclusion of that "dispute" grow with each passing year. Moreover, while Defendants can assert endless "disputes" by merely saying so and without regard for the evidence necessary to justify a "dispute," the State is forced to watch its evidence degrade with every passing year as memories fade, witnesses become unavailable, and documents are inevitably lost. Simply put, the Defendants unilaterally control the timing of their asserted "disputes" and have established a pattern of deliberately delaying the resolution of such "disputes" and delaying payments even after the "disputes" are resolved, yet the Defendants are not

appreciably impacted—if at all—by the delays they cause. In contrast, Montana has very little control over the timing and resolution speed of the Defendants' "disputes," yet it is greatly harmed by each delay. This again puts the parties in inherently unequal positions.

120. The Defendants are not only aware of the State's vulnerability to and harm suffered from the delays but are openly committed to the strategy of deliberately extending such delays and taking advantage of the State's vulnerability. As this Court has recognized, Montana—like most states—is not immune to budgetary constraints.[61] When the Defendants indefinitely withhold millions of dollars due to the State each year in the face of the State's budgetary constraints, and then approach the State with proposals to join the bad deal known as the "Term Sheet," they engage in extortion that takes aim at Montana's limited resources and victimizes Montana's citizens. The Defendants are betting on the State's budget shortfall to predictably increase over time while they continue to perpetrate their delay tactics, so that eventually even a bad deal (e.g., one that releases to the State approximately $0.50 on each $1.00 owed for certain years) becomes acceptable, and Montana succumbs to joining the Term Sheet.

121. This exact scheme has worked for the Defendants many times in the recent past. Despite the majority of MSA States originally rejecting the Term Sheet, the Defendants remained relentless with their delay tactics and, between 2012 and 2018, succeeded in gradually forcing 36 MSA States to join the Term Sheet. The Defendants'

[61] *See* Order on Plaintiff's Partial Summary Judgement Motions (Burden of Proof and Diligently Enforce) and Summary Judgment Motion, filed in this cause number May 9, 2018 (Montana has no mitigation duty under controlling Montana law if it was financially unable to diligently enforce the Qualifying Statute).

assertions of "disputes" over Montana's enforcement every year are simply a manifestation of the same delay-based extortion strategy, aimed at coercing Montana into becoming the 37th TSS.

COUNT III—BREACH OF THE DUTY OF GOOD FAITH AND FAIR DEALING—CONSPIRACY CLAIM

122. The State realleges and incorporates all preceding paragraphs here.

123. The Defendant OPMs Philip Morris and R.J. Reynolds account for the vast majority of the withheld MSA payments from Montana. These two Defendants have consciously and intentionally developed a scheme to knowingly and unlawfully deprive the State of settlement payments owed to it under the MSA. Philip Morris and R.J. Reynolds have done so in breach of the covenant of good faith and fair dealing. Upon information and belief, these two Defendants are the progenitors of the scheme described above.

124. The Defendant SPMs have adopted and incorporated the scheme, developed by the OPMs Philip Morris and R.J. Reynolds and benefit from it.

125. All Defendant PMs have collectively reached a meeting of the minds on the common object of unlawfully depriving the State of settlement payments owed to it under the MSA in breach of the covenant of good faith and fair dealing.

126. The Defendant PMs coordinated their litigation efforts over the "disputes" surrounding the 2003 and 2004 payments. For example, in the course of Montana's 2017-2018 litigation over the withheld 2004 payment, Counsel for R.J. Reynolds conducted all meet-and-confer discussions regarding discovery, and conducted and defended all

depositions taken except the 30(b)(6) depositions of Phillip Morris. Counsel for R.J. Reynolds led all negotiations and spoke on behalf of the other Defendants during litigation, with limited exception.

127. The Defendant PMs all engage in the coordinated practice of (1) asserting "disputes" in connection with each annual payment, (2) knowingly withholding payments due to Montana, (3) requiring Montana to initiate all litigation to recover the withheld payments, and (4) insisting that Montana does not receive any payment for any year—*even when Montana's enforcement is not in dispute*—until all pending disputes with the other MSA States for that year are resolved with finality.

128. Despite being signed solely by Counsel for R.J. Reynolds, the March 8, 2019 Leibenstein letter **was sent on behalf of all Defendants**. As noted above, that letter (1) asserts that Defendants are entitled to withhold a portion of Montana's MSA payments simply because they have lodged "disputes" of Montana's enforcement for all years, and (2) insists that *even in the absence of any "disputes" with Montana*, payment of the amount withheld from Montana cannot happen before final resolution of all of the Defendants' pending disputes with all other MSA States.

129. It is clear that the Defendants' scheme to defraud Montana from millions in MSA payments due to the State is the product of an agreement among the Defendants to act in concert by asserting pro-forma "disputes" against Montana and by withholding ever-growing amounts of money from Montana on the pretext of those "disputes" without actually intending to litigate the asserted "disputes" through trial.

130. The Defendants have conspired to breach, and continue to conspire to breach,

the covenant of good faith and fair dealing. Accordingly, the actions of each Defendant in furtherance of the conspiracy are attributable to all of the Defendants jointly and all are liable for the wrongful acts of co-conspirators.

COUNT IV—MONTANA FALSE CLAIMS ACT—
Mont. Code Ann. § 17-8-403(1)(d)

131. The State realleges and incorporates all preceding paragraphs here.

132. A person, including a corporation, is liable for violation of the Montana False Claims Act if they have possession, custody, or control of public money used or to be used by the governmental entity and knowingly delivers or causes to be delivered less than all of the money.

133. "Knowingly" means that a person, with respect to information, does any of the following:

(i) has actual knowledge of the information;

(ii) acts in deliberate ignorance of the truth or falsity of the information; or

(iii) acts in reckless disregard of the truth or falsity of the information.

A specific intent to defraud is not required.

134. The Defendants have "control" over Montana's MSA payments. They decide what portions of the payments are withheld and when, and have proven that nothing prevents them from paying previously withheld amounts any time they wish.

135. The withheld MSA payments are "money to be used by the governmental entity." It is money that goes predominantly to the Montana Department of Health and Human Services to pay for, among other things, smoking prevention and cessation

programs and the Children's Health Insurance Program.

136. The Defendants knowingly cause "less than all of the money" to be delivered to the State by locking some of it in the DPA and by simply refusing to pay the rest. The Defendants do this by asserting "disputes" over Montana's enforcement that they know are baseless and by knowingly engaging in tactics designed to delay the resolution of such "disputes," making it impossible for the State to ever obtain full payment of all of the Defendants' outstanding MSA obligations.

137. The Defendants knowingly cause the State to spend large sums of taxpayer dollars to litigate for the recovery of the improperly withheld MSA payments.

138. As such, the Defendants are liable for violating the Montana False Claims Act.

COUNT V—MONTANA FALSE CLAIMS ACT
Mont. Code Ann. § 17-8-403(1)(g)

139. The State realleges and incorporates all preceding paragraphs here.

140. A person, including a corporation, is liable for violation of the Montana False Claims Act if they knowingly make, use, or cause to be made or used a false record or statement material to an obligation to pay or transmit money or property to a governmental entity.

141. "Obligation" is defined in the Montana False Claims Act to include an express contractual relationship.

142. The MSA, and the Consent Decree incorporating it, created an express contractual relationship between the State and the Defendants. The Defendants have an

express obligation to make payment to Montana under the MSA and the Consent Decree.

143. "Knowingly" means that a person, with respect to information, does any of the following:

(i) has actual knowledge of the information;

(ii) acts in deliberate ignorance of the truth or falsity of the information; or

(iii) acts in reckless disregard of the truth or falsity of the information.

A specific intent to defraud is not required.

144. The Defendants allege that Montana did not enforce its Qualifying Statute for each and every year 2006–present.[62] These allegations are made either in deliberate ignorance of the truth or falsity of the information, in reckless disregard of the truth or falsity, or with actual knowledge that it is false.

145. The Defendants have withheld, and continue to withhold, payments from Montana for each and every year, 2006–present, without any apparent basis to believe Montana substantially failed to detect or to enforce against violations of the Qualifying Statute by any NPMs.

146. The Defendants' allegations that Montana did not enforce its Qualifying Statute are material to their obligation to make annual MSA payments to the State. But for the Defendants' "disputes," which they know to be baseless, Montana would have received its full MSA payments for all years.

[62] March 8, 2018 Leibenstein Letter, attached as Exhibit 1. This letter reiterates and reaffirms the Defendants' long-standing and unsubstantiated allegations that Montana did not enforce its Qualifying Statute, which were originally made under the Defendants' incorrect assertion that Montana had the burden of proving enforcement of its Qualifying Statute.

147. As such, the Defendants are liable for violating the Montana False Claims Act, and are subject to treble damages, penalties, fees, costs, and expenses.

COUNT VI—MONTANA FALSE CLAIMS ACT—
Mont. Code Ann. § 17-8-403(1)(g)

148. The State realleges and incorporates all preceding paragraphs here.

149. A person, including a corporation, is liable for violation of the Montana False Claims Act if they knowingly and improperly avoid or decrease an obligation to pay or transmit money to a governmental entity.

150. This provision is violated by improperly avoiding or decreasing an obligation to pay, whether any false statement is made or not. *United States ex rel. Harper v. Muskingum Watershed Conservancy Dist.*, 842 F.3d 430, 436 (6th Cir. 2016).

151. The Defendants avoid or decrease their obligation to pay money to the State by (1) alleging that Montana did not enforce its Qualifying Statute for each and every year 2006–present, (2) withholding money on the basis of these allegations without ever initiating proceedings to prove their allegations, and (3) claiming that Montana's MSA payments cannot be made in full until the Defendants resolve all of their pending disputes over a given payment year with all other MSA States.

152. The Defendants improperly avoid or decrease their MSA payment obligations through allegations made in bad faith, without actual evidence, and absent reasonable belief that Montana failed to enforce its Qualifying Statute.

153. The Defendants improperly avoid or decrease their MSA payment obligations solely on the basis of *national* data that indicates nothing about Montana's

enforcement.

154. The Defendants' non-payment of their MSA obligations to Montana is improper because the asserted "disputes" are just a pretense for withholding an ever-growing amount from the State with the expectation that Montana would eventually succumb to the pressure of joining a secondary settlement and would give up its rightful ownership of a substantial portion of the outstanding millions due to it from the Defendants.

155. It is the Defendants who claim entitlement to an NPM Adjustment for every year that would reduce their MSA payment obligations for that year. This adjustment is *contingent* in that it reduces the Defendants' MSA payment to Montana *if and only if* the Defendants can prove that Montana did not enforce its Qualifying Statute. It is incumbent upon the Defendants—assuming, *arguendo*, that they have a reasonable basis for disputing Montana's enforcement—to meet their burden of proving that they are entitled to reduce Montana's MSA payments, yet in the entire twenty-year history of the MSA, the Defendants have never once done so.

156. The Defendants have knowingly engaged in the course of conduct described above to avoid paying their full contractual obligations to Montana. The Defendants have violated, and continue to violate, the Montana False Claims Act and are subject to treble damages, penalties, fees, costs, and expenses.

COUNT VII—MONTANA FALSE CLAIMS ACT—
Mont. Code Ann. § 17-8-403(1)(c)—
CONSPIRACY

157. The State realleges and incorporates all preceding paragraphs here.

158. The Defendant OPMs Philip Morris and R.J. Reynolds account for the vast majority of the withheld MSA payments from Montana. These two Defendants have consciously and intentionally developed a scheme to knowingly and unlawfully deprive the State of settlement payments owed to it under the MSA. Philip Morris and R.J. Reynolds have done so in violation of Mont. Code Ann. §§ 17-8-403(1)(d) and (1)(g). Upon information and belief, these two Defendants are the progenitors of the scheme described above.

159. The Defendant SPMs have adopted and incorporated the scheme, developed by the OPMs Philip Morris and R.J. Reynolds.

160. All Defendant PMs have collectively reached a meeting of the minds on the common object of unlawfully depriving the State of settlement payments owed to it under the MSA and in violation of Mont. Code Ann. §§ 17-8-403(1)(d) and (1)(g).

161. The Defendant PMs coordinated their litigation efforts over the "disputes" surrounding the 2003 and 2004 payments. For example, in the course of Montana's 2017-2018 litigation over the withheld 2004 payment, Counsel for R.J. Reynolds conducted all meet-and-confer discussions regarding discovery, and conducted and defended all depositions taken, except the 30(b)(6) depositions of Phillip Morris. Counsel for R.J. Reynolds led all negotiations and spoke on behalf of the other Defendants during litigation, with limited exception.

162. The Defendant PMs all engage in the coordinated practice of (1) asserting "disputes" in connection with each annual payment, (2) knowingly withholding payments due to Montana, (3) requiring Montana to initiate all litigation to recover the withheld

payments, and (4) insisting that Montana does not receive any payment for any year—*even when Montana's enforcement is not in dispute*—until all pending disputes with the other MSA States for that year are resolved with finality.

163. Despite being signed solely by Counsel for R.J. Reynolds, the March 8, 2019 Leibenstein letter **was sent on behalf of all Defendants**. As noted above, that letter (1) asserts that Defendants are entitled to withhold a portion of Montana's MSA payments simply because they have lodged "disputes" of Montana's enforcement for all years, and (2) insists that *even in the absence of any "disputes" with Montana*, payment of the amount withheld from Montana cannot happen before final resolution of all of the Defendants' pending disputes with all other MSA States.

164. It is clear that the Defendants' scheme to defraud Montana from millions in MSA payments due to the State is the product of an agreement among the Defendants to act in concert by asserting pro-forma "disputes" against Montana and by withholding ever-growing amounts of money from Montana on the pretext of those "disputes" without actually intending to litigate the asserted "disputes" through trial.

165. The Defendants have conspired to violate, and continue to conspire to violate, the Montana False Claims Act, and are subject to treble damages, penalties, fees, costs, and expenses.

COUNT VIII—DECLARATORY AND ENFORCEMENT RELIEF

166. The State realleges and incorporates all preceding paragraphs here.

167. The MSA and the Consent Decree incorporating it expressly authorize the

State to request and this Court to issue Declaratory or Enforcement Orders to implement and enforce the MSA and the Consent Decree.

168. The Defendants are not entitled to unilaterally reduce their payment to Montana unless and until they bring proceedings, based on actual, Montana-specific evidence, that Montana did not enforce its Qualifying Statute for the year in question.

169. The State seeks a Declaratory Order or an Enforcement Order that prohibits the Defendants from preemptively reducing their annual MSA payments to Montana before they bring proceedings, based on actual, Montana-specific evidence, that Montana did not enforce its Qualifying Statute for the year in question.

PUNITIVE DAMAGES

170. The State realleges and incorporates all preceding paragraphs here.

171. The foregoing acts by the Defendants were committed with actual fraud or actual malice.

172. The Defendants possess immense information and resources for gathering further information regarding Montana's enforcement efforts.

173. The Defendants allege that Montana did not enforce its Qualifying Statute with actual knowledge of the falsity of this allegation.

174. The Defendants either do not have any actual evidence or information about specific violations of Montana's Qualifying Statute by an NPM that the State failed to detect or failed to enforce against, or have such information but have withheld it from the State for the sole purpose of depriving the State of part of its annual MSA payment.

175. Specifically, to the extent that the Defendants are aware of any undetected on unaddressed violation of Montana's Qualifying Statute by an NPM, they have concealed such information from the State in order to "dispute" Montana's enforcement for purposes of depriving Montana of part of its annual MSA payments. The Defendants either knew that their "disputes" of Montana's enforcement are baseless, or intentionally concealed information from Montana regarding concrete instances of alleged enforcement failures.

176. Alternatively, the Defendants deliberately proceeded to act in conscious or intentional disregard or indifference to the high probability of injury to Montana. For example, if timely made, the Defendants' outstanding MSA payments would have been used in part to provide CHIP health insurance for more Montana children and for a longer period of time. Interest alone does not compensate Montana for the non-monetary cost of the Defendants' actions, which, for example, prevented the State from insuring between 200 and 300 more children every year starting in 2006, with insurance coverage continuing through the present. The importance of funding public health programs, which Defendants are required to pay because of the burden their harmful product places on public health funding, and the dire consequences that can result from inadequate funding cannot be overstated.

PRAYER FOR RELIEF

Based on the foregoing, the State of Montana respectfully requests judgment in its favor for:

1. Actual damages of $42,726,519.65 from Defendants Philip Morris USA, R.J.

Reynolds, Commonwealth Brands, Inc., Farmer's Tobacco Company of Cynthiana, Inc., ITG Brands, LLC, Japan Tobacco International USA, Inc., King Maker Marketing, Inc., Kretek International, Inc., Liggett Group, LLC., Peter Stokkebye Tobaksfabrik A/S, Premier Manufacturing Incorporated, Santa Fe Natural Tobacco Company, Inc., Scandinavian Tobacco Group Lane Ltd, Sherman 1400 Broadway N.Y.C., Inc., Tabacalera del Este, S.A. ("TABESA"), Vector Tobacco Inc., the Von Eicken Group, and Wind River Tobacco Company, LLC, any other withholdings determined at trial, and all future withholdings through the DPA, plus any amounts withheld after the commencement of this enforcement action;

2. Actual damages from Defendants Farmer's, Liggett, and Vector in an amount to be determined upon completion of Montana's investigation into the amounts that those three companies have refused to pay (and have not even placed into the DPA), plus any amounts they refuse to pay after the commencement of this enforcement action;

3. Treble damages;

4. Punitive damages;

5. Maximum statutory penalties under the Montana False Claims Act for each individual instance in which a Defendant has withheld part of Montana's MSA payment for a given year on the grounds of a "dispute" over Montana's enforcement during the year subject to payment when the Defendant had no actual evidence to support its "dispute';

6. Attorneys' fees;

7. Costs;

8. Expenses;

9. Pre-judgment interest;

10. Post-judgment interest;

11. Declaratory and injunctive relief; and

12. Any further relief the Court determines to be just and necessary.

JURY DEMAND

The State of Montana demands a jury trial on all issues triable of right by a jury.

Dated this 10th day of April, 2020.

ATTORNEY GENERAL
TIMOTHY C. FOX

I certify that on the 13th day of April, 2020, a copy of the foregoing was served upon the following by email:

Company: Farmer's Tobacco W. Scott Mitchell Holland & Hart LLP smitchell@hollandhart.com Christie A. Moore Dentons US LLP Christie.moore@dentons.com **Company: RJ Reynolds Tobacco** Tom Dutton Paul T. Fox Greenberg Traurig duttont@gtlaw.com foxp@gtlaw.com	**Company: Certain Subsequent Participating Manufacturers** Elizabeth McCallum Robert Brookhiser BakerHostettler emccallum@bakerlaw.com rbrookhiser@bakerlaw.com Carl W. Mendenhall Sean M. Morris Worden Thane PC cmendenhall@wordenthane.com smorris@wordenthane.com **Company: Philip Morris USA**

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By: _____