UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

UNITED STATES OF AMERICA,	)	
Plaintiff,	)	**Civil Action No. 99-2496 (GK)**
v.	)	
PHILIP MORRIS USA INC., *et al.*,	)	
Defendants.	)	

DEFENDANTS' SUBMISSION CONCERNING ORDER #1015'S POINT-OF-SALE DISPLAY REQUIREMENTS

In Order #14, the Court requested that the parties outline their respective positions on the retail point-of-sale display requirements contained in Order #1015 and subsequently vacated and remanded by the D.C. Circuit ("POS requirements"). For the reasons set forth below, Defendants Altria Group Inc., Philip Morris USA Inc., R.J. Reynolds Tobacco Company (individually and as successor to Brown & Williamson Tobacco Corporation), and Lorillard Tobacco Company respectfully urge the Court to follow the D.C. Circuit's suggestion and decline to impose Order #1015's POS requirements in their entirety.[1]

The D.C. Circuit's mandate was clear: the POS requirements in Order #1015, as originally formulated, cannot lawfully be imposed because they impair the rights of third-party retailers, who are not parties to this case and who stand to suffer significant economic harm if the

[1] For the reasons set forth in their Motion for Vacatur [D.N. 5881], Defendants maintain that the Family Smoking Prevention and Tobacco Control Act eliminates this Court's jurisdiction to order any corrective statements and that, at a minimum, this Court should defer to the FDA's primary jurisdiction over communications regarding the health risks and addictiveness of smoking. That motion, if granted, would moot any particular issues relating to POS displays.

requirements are imposed. These facts, which underpinned the D.C. Circuit's decision to vacate the POS requirements, have not changed.

Since remand, the Government has suggested that this Court circumvent the D.C. Circuit's mandate by ordering Defendants to amend their existing contracts with retailers, or enter into new contracts, to require retailers to implement the POS requirements. *See, e.g.*, Tr. of 2/24/11 Hearing at 33. But this suggestion does nothing to get around the legal obstacle flagged by the D.C. Circuit. Indeed, what the Government suggests is precisely what the D.C. Circuit has already rejected. Order #1015 itself already compelled Defendants to use their contracts with retailers to require them to post POS displays. The POS provision that was vacated by the D.C. Circuit operated directly on Defendants to "require" them to use their contracts with retailers to compel the latter to display the POS signage on pain of economic sanctions for retailers who failed to do so. The D.C. Circuit concluded that this order, even if formally directed only at Defendants, improperly invaded the rights of absent third parties. The Government has suggested that additional inquiry into Defendants' contracts with retailers may lead to a lawful POS order, but no amount of contractual modification—or additional discovery into the terms of Defendants' contractual relationships with retailers—can avoid the problem of economic injury to third parties identified by the D.C. Circuit. Nor can this Court amend the POS requirements of Order #1015 to apply *directly* to retailers because due process prohibits this Court from adjudicating the rights of nonparties to this litigation. *See, e.g.*, *Martin v. Wilks*, 490 U.S. 755 (1989). Even if some retailers decide to participate in this Court as *amici curiae*, they will remain nonparties to this dispute who cannot be required to intervene or otherwise be subjected to remedies imposed by this Court.

Moreover, even on its own terms, the Government's POS proposal still fails to take account of the complex contractual relationships between Defendants and retailers, disregards Defendants and retailers' First Amendment rights, and ignores the innumerable logistical problems that would make imposing such burdensome requirements unmanageable, unworkable, and unconstitutional. In fact, the only thing that has changed since the D.C. Circuit's opinion is Congress's enactment of the Family Smoking Prevention and Tobacco Control Act ("FSPTCA"), Pub. L. No. 111-31, 123 Stat. 1776 (2009). Under the FSPTCA, the Food & Drug Administration ("FDA") is in the process of requiring new textual and graphic health warnings and launching a multi-million-dollar public health campaign about the risks of smoking. In light of this new federal regulatory framework, as well as additional information about smoking and health that may be disseminated in other formats if this Court requires a corrective statement campaign, the POS requirements are wholly unnecessary and unwarranted.

HISTORY OF THE POS REQUIREMENTS OF ORDER #1015

Order #1015 provided the following:

> Each of the corrective statements approved pursuant to Section III(B)(¶ 5) of this Final Judgment and Remedial Order shall also be designed by Defendants for inclusion in a Countertop Display and Header Display at retail point-of-sale. Each Defendant that utilizes a Retail Merchandising Program shall require retailers who participate in such program to display each Countertop Display in a position of prominent visibility for the entire four month period, until it is replaced by a subsequent Countertop Display during the two-year duration set forth in Section III(B)(¶ 7)(a) of this Order. Each Defendant that utilizes a Retail Merchandising Program shall require retailers who participate in such program to display each Header Display in an equivalent position with any other brand advertising header for the entire period on the same schedule, whether monthly or quarterly, that any other brand advertising header is utilized. The Header Display shall be of at least equivalent size as any other brand advertising header or headers provided by Defendants. During the two year period set forth in Section III(B)(¶ 7)(a) of this Order, each Defendant shall include each of the five Court approved corrective statements in a Countertop Display and Header Display at least once. Each Defendant shall suspend from its Retail Merchandising Program for a period of one year any retailer that fails to comply with this provision.

United States v. Philip Morris USA, Inc., 449 F. Supp. 2d 1, 939-40 (D.D.C. 2006) (¶ 7(b)). Further, under Order #1015, the Countertop Displays must be at least thirty inches high and eighteen inches wide "within the line-of-sight of any customer who is standing in line for the register." *Id.* at 946.

On appeal, the D.C. Circuit vacated and remanded Order #1015 because, among other things, this portion of Order #1015 was unjustified. *United States v. Philip Morris USA*, 566 F.3d 1095, 1141 (D.C. Cir. 2009). The D.C. Circuit recognized that the "[r]etailers affected by this order—none of whom were involved in the litigation in any way—did not receive notice of this remedy or an opportunity to present evidence or arguments to the district court regarding the impact the injunction would have on their business." *Id.* Nor, the D.C. Circuit observed, did this Court "consider[] the impact of this program on affected retailers." *Id.* The court emphasized that, "[e]ven though not explicitly bound by the terms of an injunction on pain of contempt, third parties may be so adversely affected by an injunction as to render it improper." *Id.* at 1142 (citing *Cook Inc. v. Boston Scientific Corp.*, 333 F.3d 737, 744 (7th Cir. 2003)). The D.C. Circuit therefore directed this Court to "evaluate and 'mak[e] due provision for the rights of innocent persons,' either by abandoning this part of the remedial order or by crafting a new version reflecting the rights of third persons." *Id.* (quoting 18 U.S.C. 1964(a)).

FACTUAL BACKGROUND

There are over 340,000 retailers of Defendants' tobacco products nationwide. These retailers include stores of all different sizes and types (big box, supermarket, convenience store, bodega, news-stand), locations (rural, urban, suburban), sales volumes, and consumer bases. Declaration of Miguel Martin ("Martin Decl.") ¶ 15, attached as Exhibit 1; Declaration of John D. Boehm ("Boehm Decl.") ¶ 8, attached as Exhibit 2; Declaration of Kathy Sparrow ("Sparrow Decl.") ¶ 7, attached as Exhibit 3; *see also* Defendants' Praecipe Regarding Independent Third-

Parties Who Should Be Asked To File Briefs Concerning Point-Of-Sale Displays [D.N. 5887]. For example, there are over 190,000 retail stores that are under contract with PM USA as part of its "Retail Leaders" merchandising program. Martin Decl. ¶ 15; *see also* Boehm Decl. ¶ 8 (RJRT has approximately 150,000 retailers participating in its retail merchandising program). At the same time, however, there are also over 150,000 retailers that sell PM USA cigarettes but are *not* part of PM USA's Retail Leaders program and thus, unless they participate in other Defendants' programs, would not be implicated by Order #1015's requirements. Martin Decl. ¶ 16; *see also* Boehm Decl. ¶ 9 (110,000 retailers sell RJRT products without participating in RJRT's retail merchandising program).

Merchandising programs are voluntary and any party can terminate them, often on short notice. Martin Decl. ¶ 7 (Retail Leaders contracts can be terminated on 30 days notice); Boehm Decl. ¶ 7 (RJRT retail merchandising contracts can be terminated on 10 days notice); Sparrow Decl. ¶ 9 (Lorillard retail merchandising contracts are cancellable by either party upon notice). In general, a retailer who agrees to a merchandising program, such as PM USA's Retail Leaders agreement, agrees to merchandise and advertise PM USA products in a certain manner. Martin Decl. ¶ 8; Boehm Decl. ¶ 24; Sparrow Decl. ¶ 3. These contracts are complex and set forth in detail the numerous benefits and obligations of the parties. For instance, PM USA's Retail Leaders agreement sets forth requirements relating to where PM USA signage should be placed and the terms under which PM USA cigarette promotions must be delivered to adult smokers. Martin Decl. ¶ 8; *see also* Boehm Decl. ¶ 24 (same for RJRT retail merchandising program); Sparrow Decl. ¶ 4 (same for certain Lorillard programs). Other important requirements include provisions relating to reporting of sales information, contraband prevention, and required compliance with all applicable laws. Martin Decl. ¶ 8; Boehm Decl. ¶ 6; Sparrow Decl. ¶ 3.

These contracts also provide significant direct and indirect financial incentives for retailers. PM USA's Retail Leaders' program, for instance, provides direct financial incentives by paying a certain amount to the retailer based on the number of cartons sold and indirect financial incentives by making retailers eligible to receive price promotions on select PM USA brands that must be passed on to the adult consumer. Martin Decl. ¶ 14; *see also* Boehm Decl. ¶ 10; Sparrow Decl. ¶ 4. Payments to retailers through programs such as these can constitute a substantial portion of many retailers' annual revenue, and which are an important part of their business model. Martin Decl. ¶ 14; *see also* Sparrow Decl. ¶ 4 (payments under Lorillard merchandising program can be a significant source of revenue, particularly for smaller retailers).[2]

The POS requirements of Order #1015 would fundamentally change the nature of Defendants' complex contractual relationships with retailers. Martin Decl. ¶¶ 17-19; Boehm Decl. ¶¶ 13-19; Sparrow Decl. ¶¶ 6-9. The requirements would both alter the physical layout of retailers' stores and impair their abilities to conduct business as they wish within legal boundaries. Martin Decl. ¶ 18; Boehm Decl. ¶ 14; Sparrow Decl. ¶ 7. The requirements would reduce the amount of countertop space available to retailers, which is some of the most valuable space in their stores. Martin Decl. ¶ 29; Boehm Decl. ¶ 18; Sparrow Decl. ¶ 7. This space is often used for sales, promotions, and displays of an array of products *other* than cigarettes.

[2] At the same time, such merchandising programs also provide a benefit to Defendants. In particular, they play an essential role in Defendants' ability to promote their products and communicate with adult smokers in a meaningful way. Martin Decl. ¶¶ 10-13; Boehm Decl. ¶¶ 11-12; Sparrow Decl. ¶ 3. Indeed, cigarette advertising in the United States is subject to very significant restrictions that are not common to other consumer goods. Martin Decl. ¶ 10; Boehm Decl. ¶ 11. Among other things, federal law prohibits the advertising of cigarettes via television or radio. Martin Decl. ¶ 10; Boehm Decl. ¶ 11. In addition, the FSPTCA established additional and comprehensive restrictions on the sale, promotion, and distribution of tobacco products. Martin Decl. ¶ 11. Defendants thus view the retail environment as an essential opportunity to communicate with adult smokers about their products. Martin Decl. ¶ 13; Boehm Decl. ¶ 12; Sparrow Decl. ¶ 3.

Martin Decl. ¶ 29; Boehm Decl. ¶ 18. In fact, over 97 percent of retailers who have contracted with PM USA have chosen an option that prohibits them from placing cigarette brand advertising on their countertops, which reduces the visibility of such advertising to underage consumers and allows retailers to sell and advertise a range of other consumer products in that space. Martin Decl. ¶ 9. In addition, the requirements could create security problems by obstructing the ability of store clerks to see the entire store, which in turn, may result in higher risks of theft and robbery and reduced capacity to observe stocking and display issues. Martin Decl. ¶¶ 28-30; Boehm Decl. ¶ 17; Sparrow Decl. ¶ 7. Under Order #1015, retailers are to be suspended from participating in a merchandising program if they fail to comply with any of the POS-related requirements.

The POS requirements also would have an adverse impact on the value of merchandising contracts for Defendants. Martin Decl. ¶ 20; Boehm Decl. ¶ 21; Sparrow Decl. ¶¶ 6-7, 9. Among other things, the requirements would frustrate Defendants' ability to ensure that responsible sales practices, such as We Card requirements, are followed by retailers, because the POS signage required by this Court would occupy areas in which PM USA encourages We Card postings, and would substantially interfere with Defendants' efforts to market to and communicate with their adult consumers in the POS environment. Martin Decl. ¶¶ 21, 22-24; *see also* Boehm Decl. ¶¶ 24-25; Sparrow Decl. ¶¶ 3, 6-9.

ARGUMENT

Defendants respectfully submit that, for multiple reasons, this Court should follow the suggestion of the D.C. Circuit and decline to impose Order #1015's POS requirements in their entirety. *First*, none of the grounds for the D.C. Circuit's POS mandate has in any way changed, and the Court should reject any attempts by the Government to evade that mandate. The D.C. Circuit has already squarely rejected the precise approach urged by the Government now, which

would indirectly target retailers by requiring Defendants to modify their retailer contracts to include POS requirements. And the only other conceivable approach—a court order directly requiring nonparty retailers to adhere to POS requirements—would be flatly unconstitutional. Moreover, the FDA's extensive authority to regulate matters of smoking and health—including its imposition of new textual and graphic warnings on cigarette packages and advertising—as well as the corrective statements that this Court may order, eliminate any need for imposing POS requirements or for addressing the difficult legal and practical issues generated by such requirements.

Second, whether imposed indirectly or directly on retailers, the POS requirements would violate retailers' rights by compelling them to communicate messages with which they may not agree while, at the same time, reducing the value of retailers' contracts with Defendants and forcing them to endure potentially significant economic hardship. *Third*, the ambiguous provisions of the POS requirements do not adequately consider the variety of retailers affected or the manner in which compliance will be determined and therefore violate both Fed. R. Civ. P. 65 and due process. *Fourth*, by eroding one of the few, and most meaningful, avenues for Defendants to communicate with adult customers, the POS requirements would violate Defendants' First Amendment rights. [3]

[3] Defendants maintain and incorporate here their legal and factual objections to the content of the Government's proposed corrective statements. Regardless of the format in which they appear, those statements would violate the D.C. Circuit's mandate, the First Amendment, RICO, and due process because, among other reasons, they are not limited to "purely factual and uncontroversial information" aimed at ""preventing and restraining" future RICO violations. *See* Defs.' Resp. to the Gov't's Proposed Corrective Statements, at 6-13, 18-23 [D.N. 5881]; Defs.' Reply in Support of Resp. to the Gov't's Proposed Corrective Statements, at 1-11 [D.N. 5893].

I. THE COURT SHOULD FOLLOW THE D.C. CIRCUIT'S MANDATE AND DECLINE TO IMPOSE THE POS REQUIREMENTS IN THEIR ENTIRETY

In striking down the imposition of Order #1015's POS requirements through Defendants' contracts with third-party retailers, the D.C. Circuit emphasized that the "[r]etailers affected by this order—none of whom were involved in the litigation in any way—did not receive notice of this remedy or an opportunity to present evidence or arguments to the district court regarding the impact the injunction would have on their businesses." *Philip Morris USA Inc.*, 566 F.3d at 1141. Nor, according to the D.C. Circuit, did this Court independently "consider[] the impact of this program on affected retailers." *Id.* at 1142. Because the POS requirements, as envisioned, would "so adversely affect[]" these third-party retailers "as to render [the requirements] improper," the D.C. Circuit vacated the portion of Order #1015 in its entirety. *Id.* at 1141-42. As the D.C. Circuit stated: "the district court exceeded its authority by failing to consider the rights of retailers and crafting an injunction that works a potentially serious detriment to innocent persons not parties to or otherwise heard in the district court proceedings." *Id*. at 1142.

The D.C. Circuit's mandate was required under well-established principles of law. RICO explicitly requires the Court to "mak[e] due provision for the rights of innocent persons" when entering an injunction. 18 U.S.C. § 1964(a). And the Supreme Court has long made plain that due process prohibits a court from adjudicating the rights of absent third parties. *See*, *e.g.*, *Martin v. Wilks*, 490 U.S. 755 (1989); *Regal Knitware Co. v. NLRB*, 324 U.S. 9, 13 (1945) (courts "may not grant an enforcement order or injunction so broad as to make punishable the conduct of persons who act independently and whose rights have not been adjudged according to law"); *Chase Nat'l Bank v. City of Norwalk*, 291 U.S. 431, 441 (1934) ("Unless duly summoned to appear in a legal proceeding, a person not a privy [of a party] may rest assured that a judgment recovered therein will not affect his legal rights.").

Nothing has occurred since the D.C. Circuit's opinion that would render these same POS requirements proper now. The affected retailers remain nonparties to this lawsuit, and there has been no suggestion that the POS requirements—whether imposed indirectly or directly—would be any less economically harmful to retailers. Notwithstanding the D.C. Circuit's clear holding that the POS requirements impermissibly infringe the rights of third-party retailers, the Government—in an apparent attempt to circumvent the D.C. Circuit's mandate—seems to suggest that this Court can order Defendants to amend their existing contracts or enter into new contracts with retailers in a manner that would impose the same POS requirements as Order #1015. Tr. of 2/24/11 Hearing at 33 (D. Crane-Hirsch: "[Defendants' contracts with retailers] appear to include clauses that would let them be amended or terminated very swiftly. Some discovery to how those contracts play out in real life may be helpful."). But the Government's proposal of compelling Defendants to modify their retailer contracts to include provisions requiring retailers to post POS signage is precisely the approach that the D.C. Circuit rejected as an impermissible impairment of nonparties' rights. No amount of discovery into Defendants' retail contracts could alleviate this fundamental flaw in the Government's proposal.

Nor could the POS requirements be modified to apply directly to nonparty retailers because due process prohibits this Court from adjudicating the rights of third parties or imposing remedies against them. *See Martin*, 490 U.S. at 759, 762 (holding that a group of firefighters could challenge a consent decree to which they were not a party, even if they "were aware that the underlying suit might affect them" and "chose to pass up an opportunity to intervene" because "a person cannot be deprived of his legal rights in a proceeding to which he is not a party"). Nor can this Court compel nonparty retailers to appear in this case because third parties are under no obligation to intervene to safeguard their rights. *See Chase Nat'l Bank*, 291 U.S. at

441 ("[t]he law does not impose upon any person absolutely entitled to a hearing the burden of voluntary intervention in a suit to which he is a stranger"); *see also*, *e.g.*, *Holland v. Nat'l Mining Ass'n*, 309 F.3d 808, 813 (D.C. Cir. 2002) ("Joinder as a party, rather than knowledge of a lawsuit and an opportunity to intervene, is the method by which potential parties are … bound by a judgment or decree.") (internal quotations omitted).

In any event, there is simply no need for this Court to grapple with the legal and practical difficulties generated by the Government's POS proposal. The objectives of this Court's POS requirements are already fulfilled by the FDA's extensive new programs to disseminate information about the health risks and addictiveness of smoking to the public.

Since this Court issued Order #1015, the regulatory framework governing cigarettes and public-health communications about smoking has changed dramatically. The FSPTCA granted the FDA broad regulatory authority over the design, manufacturing, and advertising of tobacco products. Under that law, cigarette packages and advertising must bear a series of new rotating warnings about the health risks and addictiveness of smoking. *See* § 201(a). The warnings must comprise the top half of both the front and the back of all cigarette packages "in a manner that contrasts, by typography, layout, or color, with all other printed material on the package." *Id.* These warnings likewise must comprise the top 20 percent of all tobacco advertisements, including advertisements that appear at the point of sale. *Id.* The warnings will state, among other things, "WARNING: Cigarettes are addictive," "WARNING: Tobacco smoke can harm your children," "WARNING: Cigarettes cause fatal lung disease," "WARNING: Cigarettes cause cancer," and "WARNING: Smoking can kill you." *Id.* Moreover, the FDA has published for comment 36 proposed graphic warnings that, according to the FDA, "are designed to clearly

and effectively convey the negative health consequences of smoking" to the public. 75 Fed. Reg. 69,524, 69,526 (Nov. 12, 2010).

In addition, the FDA has launched an extensive public health campaign designed to disseminate information about the health risks and addictiveness of smoking. During Fiscal Year 2011 alone, for example, the FDA intends to spend more than $45 million to "develop and disseminate public education campaigns to decrease initiation of tobacco product use" and to "create and launch a tobacco health literacy program … targeted at various populations, with a special emphasis on educating youth and adolescents across racial, ethnic, cultural, and social demographics." FDA, FY 2011 Congressional Budget Request, 282, available at http://www.fda.gov/downloads/AboutFDA/ReportsManualsForms/Reports/BudgetReports/UCM202324.pdf. For Fiscal Year 2012, the FDA has requested more than $45 million in additional funds to communicate "to all segments of the public, especially young people, about tobacco products and the dangers their use poses to themselves and others." FDA, FY 2012 Justification of Estimates for Appropriations Committees, 401, available at http://www.fda.gov/downloads/AboutFDA/ReportsManualsForms/Reports/BudgetReports/UCM243370.pdf. And, apart from the FDA's new and extensive involvement in smoking-and-health issues, this Court's Order already requires that its corrective statements about the health risks and addictiveness of smoking be widely disseminated outside the POS context.

In light of these alternative avenues for disseminating information about smoking and health to the public, there is simply no need for an *additional* requirement that the corrective statements also be displayed on countertops and headers at the point of sale. This is especially so given (as explained below) the enormous costs and burdens the requirements would impose on innocent third-party retailers who have never been found liable for any wrongdoing, the

unmanageability of the requirements, and the fact that they are riddled with serious legal infirmities. For all these reasons, this Court should decline to impose Order #1015's POS requirements.

II. THE POS REQUIREMENTS WOULD VIOLATE THE RIGHTS OF INNOCENT THIRD-PARTY RETAILERS

As the D.C. Circuit recognized when it vacated the POS requirements of Order #1015, those requirements are unlawful and unconstitutional because they impair the economic and First Amendment rights of retailers who are not parties to this case. This is so whether those requirements are imposed on third-party retailers indirectly through Defendants' contracts or directly. In light of these intractable shortcomings in the POS requirements, this Court should follow the D.C. Circuit's suggestion and decline to impose those requirements.

A. The POS Requirements Would Impose Substantial Economic Burdens on Third-Party Retailers

As the D.C. Circuit recognized, the POS requirements would impose substantial economic burdens on the third-party retailers across the country that would be required to post corrective statements in their stores. *Philip Morris USA Inc.*, 566 F.3d at 1141; *see also generally* Brief of *Amicus Curiae* National Association of Convenience Stores (NACS) at 5-7. This is the case for multiple reasons.

First, by fundamentally altering the physical layout of each retailer's store, the requirements would prevent retailers from operating their businesses in what they deem to be the most revenue-maximizing way. Martin Decl. ¶ 18; Boehm Decl. ¶ 14; Sparrow Decl. ¶ 7. For example, placing 30-inch by 18-inch signs on countertops—some of the most valuable space in retailers' stores—is likely to impair retailers' business with regard not only to cigarettes but also to the many other products that a typical retailer sells. Martin Decl. ¶ 18; Boehm Decl. ¶ 18. Indeed, many retailers have chosen a contract option that prohibits cigarette brand advertising on

countertops, but allows them to advertize and sell a range of other products in that space (*e.g.*, gum, candy). Martin Decl. ¶ 9. The POS requirements, however, would interfere with this valuable and otherwise cigarette-free countertop space by mandating that retailers use it to display corrective communications and thereby reducing the space available for non-cigarette products. This alone could significantly decrease retailers' sales revenues.

Second, such fundamental changes to retailers' businesses would reduce the overall value of retailers' merchandising contracts with Defendants. Retailers would observe that their competitors, who are not on contract, could exploit a substantial competitive advantage in that they will not have enormous signs on the countertops or incongruous headers on cigarette fixtures. Martin Decl. ¶ 19; Boehm Decl. ¶ 19. For some, this reduction in value could lead them to feel compelled to terminate or not renew their contracts with Defendants. By foregoing these contracts, such retailers would lose the direct payments they receive from Defendants based on the number of cigarettes they purchase—which can represent a substantial portion of their expected annual revenue. Martin Decl. ¶ 14, 17; Boehm Decl. ¶ 10; Sparrow Decl. ¶ 4. They also would go without the indirect incentives contained in these contracts, typically in the form of price promotions, which in turn can result in increased sales. Martin Decl. ¶ 14, 17; Boehm Decl. ¶ 10; Sparrow Decl. at ¶ 4

Third, the POS requirements would impose burdens on retailers as they struggle to interpret and comply with the requirements' blanket and vague terms. As discussed *infra* Section III, the POS requirements purport to apply without variation to hundreds of thousands of different retail establishments of various types, sizes and designs. Martin Decl. ¶ 26; Boehm Decl. ¶ 8; Sparrow Decl. ¶ 7. Many of these establishments would simply be unable to comply fully with the POS requirements due to resource or physical space constraints. Martin Decl. ¶

27; Boehm Decl. ¶ 16; Sparrow Decl. ¶ 7. Even for those who otherwise could comply, the terms of the requirements are sufficiently vague to leave serious questions about what exactly is required. Martin Decl. ¶ 33; Boehm Decl. ¶ 27; Sparrow Decl. ¶ 8. From the retailers' perspective, such efforts to ensure compliance—which would be undertaken in the context of severe penalties for noncompliance—could be both costly and time-consuming. Decl. ¶ 33; Boehm Decl. ¶ 27; Sparrow Decl. ¶¶ 7-8.

As NACS explained before the D.C. Circuit, imposing upon innocent third-party retailers the substantial economic burdens described above would violate their rights under both the Due Process Clause and the prohibition on uncompensated government takings under the Fifth Amendment. NACS Brief at 16-19, 22-25. There are no modifications to the POS requirements that could alleviate these constitutional infirmities—or reconcile those requirements with this Court's obligation under RICO to make "due provision for the rights of innocent persons" (18 U.S.C. § 1964(a))—because the requirements necessarily impose burdens on nonparties to this litigation.

B. The POS Requirements Would Violate Third-Party Retailers' First Amendment Rights by Compelling Speech in Their Stores

The POS requirements also would violate third-party retailers' First Amendment right not to be compelled to speak. On their face, the requirements would force retailers—who have never been accused of, much less found liable for, any wrongdoing in this case—to showcase in their stores corrective statements with which they may not agree. The law is clear that the First Amendment protects "both the right to speak freely and the right to refrain from speaking at all." *Wooley v. Maynard*, 430 U.S. 705, 714 (1977); *see also United States v. Nat'l Soc'y of Prof'l Eng'rs*, 555 F.2d 978, 984 (D.C. Cir. 1977) (the First Amendment prohibits "forc[ing] an association of individuals to express as its own opinion judicially dictated ideas"), *aff'd*, 435 U.S.

679 (1978). Such compelled speech is subject to strict scrutiny, and is therefore unconstitutional unless it furthers a compelling governmental interest by the least restrictive means available. *United States v. Playboy Entm't Grp., Inc*., 529 U.S. 803, 813 (2000); *Sable Commc'ns of Cal., Inc. v. FCC*, 492 U.S. 115, 126 (1989); *Entm't Software Ass'n v. Blagojevich*, 469 F.3d 641, 653 (7th Cir. 2006) (invalidating a state law that required videogame retailers to post signs and display brochures explaining videogame rating standards because the law required retailers "to communicate that any video games in the store can be properly judged pursuant to th[ose] standards," which was an assertion with which retailers might disagree). To be sure, the Supreme Court has recognized a narrow exception to strict scrutiny for mandated commercial disclosures that are "purely factual and uncontroversial," but that exception applies only if the disclosures are "reasonably related to [the Government's] interest in preventing deception of consumers" and do not impose restrictions that are "unjustified or unduly burdensome." *Zauderer v. Office of Disciplinary Counsel*, 471 U.S. 626, 651 (1985).

Here, even if the Government's proposed corrective statements were "purely factual and uncontroversial"—which, as explained in Defendants' corrective statements briefing, they are not—the POS requirements would nevertheless fail this First Amendment standard. There are numerous less burdensome ways for the Government to disseminate public-health information to smokers. As discussed above, there is an extensive public health campaign already being undertaken by the FDA, an extensive new regulatory regime under the FSPTCA that includes new textual and proposed graphic warnings, and numerous other means available for communicating any corrective statements outside the POS context. The POS requirements would have little, if any, added benefit for consumers, and whatever added benefit they might have is far outweighed by the burden that the requirements impose on the First Amendment

rights of nonparty retailers, who would be compelled to disseminate inflammatory and disputed statements about Defendants' past conduct with which the retailers themselves might disagree, as well as by the economic burdens that the POS requirements impose on the retailers, *see supra* at pgs. 12-13. [4]

III. THE POS REQUIREMENTS CANNOT BE IMPOSED CONSISTENT WITH THE REQUIREMENTS OF RULE 65 AND DUE PROCESS

The vague and ambiguous requirements imposed by the POS provisions of Order #1015 would also violate Federal Rule of Civil Procedure 65(d) and due process by leaving Defendants to speculate about the measures that they would need to take to comply with this aspect of the Court's injunctions.

Federal Rule of Civil Procedure 65(d), as well as background principles of due process and fundamental fairness, require that an injunction set forth manageable standards that enable a party bound by the injunction to know precisely what it must do to comply with the court's order. As the Supreme Court has emphasized, "the specificity provisions of Rule 65(d) are no mere technical requirements. The Rule was designed to prevent uncertainty and confusion on

[4] The Government apparently believes that one way to reduce the hardship on retailers—at least with respect to the expected loss of revenue associated with diminished countertop space—would be for the Court to require Defendants to compensate retailers for that loss. Tr. of 2/24/11 Hearing at 33 (D. Crane-Hirsch: indicating that the Government intends to seek discovery regarding whether the Court should "compel the defendants to reimburse convenience stores for the value of that countertop display space"). Any such a requirement, however, would be insufficient to address the entirety of the undue economic and legal burdens that the POS requirements would impose on retailers. For one thing, such a requirement would be utterly unable to account for all of the direct and indirect financial impacts of the POS requirements, as described above. Furthermore, the proposal would violate the very same compelled speech principles just articulated. As the Government would have it, Defendants would be forced to compensate retailers in order to pave the way for the Court to compel retailers to communicate messages with which Defendants, and inevitably at least some retailers, do not agree. Such roundabout inducement cannot change the fundamental fact that Defendants and retailers would be compelled by this Court to speak against their will, which is something the First Amendment does not permit.

the part of those faced with injunctive orders." *Schmidt v. Lessard*, 414 U.S. 473, 476 (1974). The Court explained that, "[s]ince an injunctive order prohibits conduct under threat of judicial punishment, basic fairness requires that those enjoined receive explicit notice of precisely what conduct is outlawed." *Id.*

The POS provisions of Order #1015 do not meet these requirements. For example, the requirements fail to take into account the many different types of retailers to which its terms would apply. Retailers vary dramatically. Martin Decl. ¶ 26; Boehm Decl. ¶¶ 8, 15; Sparrow Decl. ¶ 7. Some retailers are extremely large, sophisticated operations with significant floor and counter space; by contrast, others are tiny bodegas with essentially no counter space and limited rack space. Martin Decl. ¶ 26; Boehm Decl. ¶ 15; Sparrow Decl. ¶ 7. Some have thousands of employees and others just one or two. Martin Decl. ¶ 26; Boehm Decl. ¶ 15. Some stores are no more than news-stands with a tiny fixture and one square foot of counter space. Martin Decl. ¶ 26; Boehm Decl. ¶ 15; Sparrow Decl. ¶ 7. Some stores have very high counters, some have very low counters, and some have no counters at all, rendering compliance with the Countertop Display requirement impossible. Martin Decl. ¶ 26; Sparrow Decl. ¶ 7. The range of stores is tremendous, and the retailers' abilities physically to comply with the POS-display requirements will depend on each individual store's specifications and circumstances. Martin Decl. ¶ 26; Boehm Decl. ¶ 15; Sparrow Decl. ¶ 7. Yet the POS requirements would apply equally to *all* of these entities without taking into account any of these real-world differences.

Under these circumstances, it is not at all clear what standard is to be used in determining Defendants' compliance with the POS requirements. This is hardly an inconsequential question, as Defendants face potential contempt sanctions for any failure to comply with this Court's injunctions but they are left to guess, for example, about what it means for a Countertop Display

to be displayed "in a position of prominent visibility." *Philip Morris USA, Inc.*, 449 F. Supp. 2d at 939 (¶ 7(b)). Or for Header Displays to be posted "in an equivalent position with any other brand advertising header for the entire period on the same schedule, whether monthly or quarterly, that any other brand advertising header is utilized." *Id.* at 940 (¶ 7(b)). These and other requirements leave both Defendants and third-party retailers uncertain as to what is required of them under the terms of Order #1015—an issue this Court would be called upon to resolve for hundreds of thousands of different contracts and retailers—and expose Defendants to contempt if either they, or a retailer, misinterpret or retailers otherwise fail to abide by this vague mandate. Neither Rule 65(d) nor due process tolerates such ambiguity.

IV. THE POS REQUIREMENTS WOULD VIOLATE DEFENDANTS' FIRST AMENDMENT RIGHTS BY FURTHER RESTRICTING THE AVENUES AVAILABLE FOR ADVERTISING THEIR PRODUCTS

By commandeering the most important advertising space in retail stores, the POS requirements would seriously impair one of the few remaining avenues for Defendants to communicate with consumers and therefore violate Defendants' First Amendment rights.

Today, there are very few avenues that Defendants have for communicating with their adult consumers. Federal law prohibits Defendants from radio and television advertising. *See* 15 U.S.C. § 1335. The FSPTCA severely restricts magazine, direct mail and point-of-sale advertising. *See* 21 C.F.R. §§ 1140.30, 1140.32 (promulgated pursuant to FSPTCA § 102).[5] And under the MSA, Defendants are subject to numerous other advertising restrictions, including

[5] The FDA has announced that it will not "commence enforcement actions" under § 1140.32(a), which requires certain labeling and print advertising to appear in a black-and-white text only format, pending litigation in which a federal court has concluded that the section is unconstitutional and has enjoined the FDA from enforcing it against the parties to that litigation. *See* FDA, Guidance for Industry and Food and Drug Administration Staff: Enforcement Policy Concerning Regulations Restricting Sale and Distribution of Cigarettes, 75 Fed. Reg. 25271 (May 7, 2010); *see also Commonwealth Brands v. United States*, 678 F. Supp. 2d 512 (W.D. Ky. 2010), *appeal docketed*, No. 10-5234 (6th Cir. March 9, 2010).

a ban on billboards and transit advertisements. *See* Master Settlement Agreement at § III(d) (JD-045158). Absent the ability to utilize such traditional forms of marketing, in-store merchandizing and promotional opportunities are among Defendants' few remaining ways of marketing to and communicating with adult customers. Martin Decl. ¶ 22; Boehm Decl. ¶¶ 11, 23. The POS-display requirements would eviscerate this remaining outlet for Defendants' commercial speech. *See, e.g.,* Martin Decl. ¶¶ 10-12, 22-24; Boehm Decl. ¶¶ 11-12, 23-25; Sparrow Decl. ¶¶ 3; 6-7, 9.

This would be a clear violation of Defendants' First Amendment rights to advertise their products to adult consumers. *See Central Hudson Gas & Electric Corp. v. Public Service Comm'n of New York*, 447 U.S. 557 (1980). Indeed, in many respects, the restrictions imposed by the POS requirements are analogous to the advertising restrictions invalidated in *Lorillard Tobacco Co. v. Reilly*, 533 U.S. 525, 565-66 (2001), where the Supreme Court struck down a ban on outdoor tobacco advertisements within 1,000 feet of a school or playground, because it effectively denied tobacco manufacturers and retailers the ability to communicate with adult tobacco consumers. As the Court explained, "tobacco retailers and manufacturers have an interest in conveying truthful information about their products to adults, and adults have a corresponding interest in receiving truthful information about tobacco products." *Id.* at 564.

Like the outdoor advertising restrictions in *Reilly*, the POS requirements would violate Defendants' constitutionally protected commercial speech rights by commandeering one of the few remaining avenues for Defendants to communicate with adult tobacco consumers. As noted above, there are myriad less burdensome means for the Government to disseminate information about the health risks and addictiveness of smoking without extinguishing one of Defendants'

final mechanisms for advertising their products. The First Amendment requires this Court to select those less burdensome alternatives.[6]

CONCLUSION

For the reasons set forth above, Defendants respectfully request that the Court decline to impose Order #1015's POS requirements.

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Respectfully submitted,

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[6] Even if this Court concludes that the POS requirements are governed by *Zauderer*'s relaxed standard for "purely factual and uncontroversial" disclosures, they are still unconstitutional because they are "unjustified and unduly burdensome" in light of the substantial economic and other burdens placed on Defendants (and retailers) and the less burdensome alternatives available for communicating the Government's message.

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