

DISTRICT COURT, CITY AND COUNTY OF DENVER, COLORADO

Case No. 97CV3432

**RESPONSE TO MOTION OF CERTAIN DEFENDANTS TO DISMISS THE STATE'S
AMENDED COMPLAINT**

STATE OF COLORADO, ex rel. GALE A. NORTON, ATTORNEY GENERAL,

Plaintiff,

v.

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

Defendants.

GALE A. NORTON
Attorney General

MARTHA PHILLIPS ALLBRIGHT
Chief Deputy Attorney General

RICHARD A. WESTFALL
Solicitor General

JAN MICHAEL ZAVISLAN*
First Assistant Attorney General

MARIA E. BERKENKOTTER*
Assistant Attorney General

Attorneys for Plaintiff

Tobacco Litigation Unit
1525 Sherman Street, 5th Floor
Denver, Colorado 80203
Telephone: (303) 866-5079
FAX: (303) 866-5691

*Counsel of Record

Plaintiff State of Colorado, ex rel. Gale A. Norton, through the undersigned attorneys, hereby responds to the Motion of Certain Defendants to Dismiss the State's Amended Complaint.¹

INTRODUCTION

On June 5, 1997, the State filed a Complaint against seven domestic producers of tobacco products, the foreign parent corporation of Brown & Williamson, and two industry trade associations, challenging a massive and unprecedented course of unlawful conduct by the defendants. The Attorney General brings this action in a dual capacity: as attorney for the State of Colorado, and as the chief law enforcement officer empowered to protect the public health, safety and welfare.

It is critical for this Court to recognize that the defendants generally do not challenge the Attorney General's ability to seek civil penalties, injunctive relief or other enforcement remedies in this action. Instead, defendants focus their arguments on whether the State is entitled to damages as a remedy for their violations of the various statutes pled in the Amended Complaint. For the reasons set forth below, the motion to dismiss must be denied.

¹ On December 18, 1997, Defendants R.J. Reynolds Tobacco Co., Brown & Williamson Tobacco Corp., individually and as successor by merger to American Tobacco Co., Inc., Lorillard Tobacco Company, Philip Morris Inc., United States Tobacco Co., The Council for Tobacco Research - U.S.A., Inc., and Tobacco Institute, Inc. filed a consolidated Motion to Dismiss and Memorandum Brief. On December 19, 1997, Liggett Group, Inc. joined in that Motion and Memorandum Brief.

BACKGROUND

A. Statement of Facts.

The defendants are engaged in the business of producing and/or promoting the sale of a product which, when used as intended, exacts a staggering toll on society. Over 400,000 Americans die each year from smoking-related illnesses. Smoking is responsible for the death of about 90% of all people who die from lung cancer; 87% of all people who die from chronic obstructive pulmonary diseases; 21% of all people who die from coronary heart disease; and 18% of all people who die from strokes. (Amended Complaint ¶ 146).² Smokeless tobacco can be equally hazardous. It increases the risk of oral cancer, and cancers of the esophagus, gum, pharynx and larynx. (Amended Complaint ¶ 148).

When the first scientific studies were published suggesting a connection between defendants' tobacco products and these illnesses, the defendants responded quickly to what they termed the "Big Scare." (Amended Complaint ¶¶ 12, 43-50). Their principal response was to form, in 1953, a far-reaching conspiracy the central mission of which was to deceive and to mislead the American public about the health consequences of tobacco use. (Amended Complaint ¶¶ 49-56). Forty-five years later, this conspiracy is still in place. Defendants, individually and through their captive trade associations (the Council for Tobacco Research -- U.S.A., Inc. ("CTR"), which was originally called the Tobacco Industry Research Committee ("TIRC"), and the Tobacco Institute ("TI")), made repeated

² At this stage of the proceedings, this Court must accept as true these and all other factual allegations in the Amended Complaint. See Rosenthal v. Dean Witter Reynolds, Inc., 908 P.2d 1095, 1099 (Colo. 1995).

representations about the safety of their tobacco products. (Amended Complaint ¶¶ 59-63).

Defendants sought to cast doubt on the veracity of scientific studies critical of their products, and to offer supposedly independent research conducted under the auspices of the CTR. (Amended Complaint ¶¶ 57, 58). Defendants continue to deny that tobacco products cause cancer and other illnesses, even though their own research has long-confirmed the connection. (Amended Complaint ¶¶ 100-108).

Defendants also misrepresented the addictive nature of tobacco products -- continuously representing to the public that cigarettes and smokeless tobacco were not addictive. (Amended Complaint ¶¶ 5, 114). Notwithstanding these public statements, numerous internal documents of the defendants contain admissions by tobacco company researchers and executives acknowledging that nicotine is, in fact, addictive. (Amended Complaint ¶¶ 110-111). Defendants lied about their ability to control nicotine levels in their products, and hid the fact that they added chemicals to their products to enhance the addictive effect of nicotine. (Amended Complaint ¶¶ 115-116).

While defendants knew of both the addictive nature of nicotine and of the hazards of tobacco use, they nonetheless conspired to suppress and to restrain development of safer products. (Amended Complaint ¶¶ 73, 75, 79, 80, 85-91). As a result of this conspiracy, and despite their ability to produce “safer” cigarettes, the defendants did not market such products. (Amended Complaint ¶ 75).

Finally, and what is perhaps their most egregious offense, defendants have engaged in a long-standing advertising and marketing campaign directed at youth. These efforts have included sponsorship of athletic events and concerts and other entertainment venues particularly appealing to minors

(Amended Complaint ¶ 131), and the use of advertising images particularly appealing to minors.

(Amended Complaint ¶¶ 128-135). Advertising dollars focused on magazines and youth-oriented publications. (Amended Complaint ¶¶ 136-139).

Defendants' conduct, as alleged in the Amended Complaint, violates the Colorado Consumer Protection Act, §§ 6-1-101 through 115, C.R.S. (1997) ("CCPA"); the Colorado Antitrust Act of 1992, §§ 6-4-101 through 122, C.R.S. (1997); the Colorado Organized Crime Control Act, §§ 18-17-101 through 109, C.R.S. (1997) ("COCCA"); and the Abatement of Public Nuisance Act, §§ 16-13-301 through 316, C.R.S. (1997).

As a result of these statutory violations, the State has been forced to spend millions of dollars each year to provide or pay for health care for state employees, as well as for indigent and other eligible Colorado residents. (Amended Complaint ¶ 162). In fulfilling its statutory duties, the State has expended and will continue to expend substantial sums of money due to the increased cost of providing health care services for treatment of tobacco-caused diseases. As detailed in the Amended Complaint, these increased expenditures have been caused by the unlawful actions of the Defendants. (Amended Complaint ¶ 163).

B. The Legal Standard.

Motions to dismiss for failure to state a claim under Rule 12(b)(5), C.R.C.P., are viewed with disfavor by the courts. Rosenthal v. Dean Witter Reynolds, Inc., 908 P.2d 1095, 1099 (Colo. 1995). Such motions should be granted only if "it appears beyond doubt that the plaintiff can prove no set of

facts in support of his claim which would entitle him to relief.” Dunlap v. Colorado Springs Cablevision, Inc., 829 P.2d 1286, 1291 (Colo. 1992) (quoting Davison v. Dill, 503 P.2d 157, 162 (Colo. 1972)). Such motions “are rarely granted under our ‘notice pleadings.’” Id.

The allegations set forth in the Amended Complaint “must be viewed in the light most favorable to the plaintiff.” Rosenthal, 908 P.2d at 1099.

The chief function of a complaint is to give notice to the defendant of the transaction or occurrence that is the subject of plaintiff’s claims. (Citations omitted) Such a complaint should not be dismissed on motion for failure to state a claim so long as the pleader is entitled to some relief “upon any theory of the law.” (Citations omitted).

Id. at 1099-1100 (emphasis in original).

Defendants expend considerable energy challenging particular remedies sought by the State under the statutory violations pled. However, a motion to dismiss for failure to state a claim is not intended to address the availability of the relief requested. “[I]t need not appear that plaintiff can obtain the particular relief prayed for, so long as the court can ascertain that some relief may be granted.” 5A WRIGHT & MILLER, FEDERAL PRACTICE AND PROCEDURE §1357 at 339 (2d ed. 1987); see Norwalk CORE v. Norwalk Redevelopment Agency, 395 F.2d 920, 925-26 (2d Cir. 1968) (complaint should not be dismissed for legal insufficiency “except where there is a failure to state a claim on which some relief, not limited by the request in the complaint, can be granted”); Asher v. Reliance Ins. Co., 308 F. Supp. 847, 850 (N.D. Cal. 1970) (unavailability of certain forms of relief does not render claim susceptible to motion to dismiss); McHugh v. Reserve Mining Co., 27 F.R.D. 505, 506 (N.D. Ohio 1961) (unavailability of some part of the relief sought “is of no importance at all”). Thus, in those

instances in which defendants' motion challenges only a limited part of the relief sought by the State, the motion must be denied so long as some relief may be granted to the State.

ARGUMENT

I. THE STATE'S CLAIMS ARE NOT PRECLUDED BY THE COLORADO MEDICAL ASSISTANCE ACT OR BY ISSUES RELATED TO PROXIMATE CAUSE

A. The Colorado Medical Assistance Act Does Not Bar the State's Statutory Claims.

The Attorney General brings this case pursuant to her constitutional and statutory duties as legal counselor and advisor to the State and as the chief law enforcement officer responsible for prosecuting civil law enforcement actions on behalf of the people of the State of Colorado. The Attorney General asserts only statutory claims for relief in the Amended Complaint, choosing not to assert any claims under the common law or under the reimbursement provisions of the Colorado Medical Assistance Act, § 26-4-403(3), C.R.S. (1997) ("CMAA").

It is true that, at common law, a party generally could not assert tort claims for injuries suffered by a third party. The defendants have provided ample support for this proposition. In this limited context, the CMAA's abrogation of that common law rule creates an exclusive remedy had the State pursued common law tort claims against these defendants.³ Thus, it is obvious why the defendants

³ The decisions in similar tobacco litigation upon which defendants so strongly rely stand for nothing more than this simple proposition. See Maryland v. Philip Morris, Inc., No. 96122017/CL211487, slip op. (Cir. Ct. of Baltimore City, Md., May 21, 1997); Iowa v. R.J. Reynolds Tobacco Co., No. CL 71048, slip

resort to recasting the State's Amended Complaint as one sounding in tort. The State, however, has not asserted any common law tort claims.

As detailed in the Amended Complaint, the State alleges that defendants have engaged in a long-standing conspiracy to restrain competition, to deceive and mislead the American public, and to encourage Colorado's youth to begin a life-long addiction to tobacco products. When these statutory violations are established at trial, the State will be entitled to recover its damages proximately caused by defendants' conduct, as well as a variety of civil penalties and other sanctions. That one measure of those damages may be the State's increased health care costs, including Medicaid expenditures, does not convert this case into a tort action to recover Medicaid costs under the CMAA.

There are basically two ways that one statute can preclude application of another. First, a statute may contain language expressly evincing the General Assembly's intent to exclude the application of other statutory remedies. See Collard v. Hohnstein, 174 P. 596, 597 (Colo. 1918) ("The rule is that a remedy provided by one statute does not abolish that given by another, or by common law, unless specifically so provided"). There is absolutely no language in the CMAA that specifically provides, or

op. (D. Polk County, Iowa, August 26, 1997); and McGraw v. The American Tobacco Co., No. 94-C-1707, Letter Opinion (Cir. Ct. Kanawha County, W.Va., February 13, 1997). (Defendants' Memorandum, Exhibits 1, 2 and 3). Not one of these cases, however, nor any case cited by defendants, supports the proposition that statutory claims are similarly preempted. In fact, the courts in each of these cases sustained state statutory claims similar to those brought in this case. See Maryland, slip op. at 35-41; Iowa, slip op. at 8-10; McGraw v. The American Tobacco Co., No. 94-C-1707, slip op. (Cir. Ct. of Kanawha County, W.Va., May 9, 1997) (**TAB A**).

even suggests, that the CMAA is intended to be the exclusive remedy for damages caused by violations of other statutes.⁴

Second, if a general provision in a statute conflicts with a special provision in another, and that conflict is irreconcilable, then the special provision will supersede the general provision. § 2-4-205, C.R.S. (1997). There is no conflict, let alone an irreconcilable one, between the State's statutory claims and the application of the CMAA. Each of the statutes relied upon by the State arise out of the exercise of the State's police power, and are deemed necessary to safeguard the health, welfare, and safety of the State and its citizens. It is safe to say that an action under section 403(3) of the CMAA by the Colorado State Department of Health Care Policy and Finance against a third party who may be liable to a recipient of medical assistance, especially where such liability is predicated on the tortious conduct of that third party, serves a different purpose.

For these reasons, defendants' motion to dismiss on the basis of the "exclusivity" of the CMAA must be denied.

B. The State Has Adequately Pled That Its Injuries Were Proximately Caused By Defendants' Conduct.

In arguing that all of the State's damages claims must be dismissed, defendants mix together concepts of proximate cause, remoteness and directness of injury, as well as principles of standing. All

⁴ None of the cases relied upon by defendants even remotely suggest that the CMAA preempts the State's statutory claims. See Tucker v. Gorman, 944 P.2d 653 (Colo. App. 1997), cert. granted, (Oct. 20, 1997); Kildahl v. Tagge, 942 P.2d 1283 (Colo. App. 1996), cert. denied, (Sept. 2, 1997); Henry v. Kemp, 829 P.2d 505 (Colo. App. 1992).

of these arguments are addressed in the State's specific responses to challenges under the CCPA, the Colorado Antitrust Act, the Public Nuisance Act and COCCA. What will be discussed here is the gravamen of defendants' challenge to the State's damages claims -- that there are "too many intervening factors and contingencies that must be considered before any damages could be properly and legally assessed." (Defendants' Memorandum, p. 16.)

Proximate cause is a question of fact. Graven v. Vail Assocs., Inc., 909 P.2d 514, 521 (Colo. 1996). When issues turn upon disputed facts, the matter may not be disposed of in a pretrial motion under Rule 12. Cline v. Rabson, 856 P.2d 1, 2-3 (Colo. App. 1992) (inappropriate for trial court to act in capacity of pre-trial factfinder).

A defendant proximately causes an injury when his or her wrongful conduct is a substantial factor in bringing about the plaintiff's injury. Lyons v. Nasby, 770 P.2d 1250, 1256 (Colo. 1989). A defendant's conduct is considered a substantial factor when it is of sufficient significance in producing the harm so as to lead reasonable persons to regard it as a cause and to attach responsibility. Sharp v. Kaiser Found. Health Plan of Colo., 710 P.2d 1153, 1155 (Colo. App. 1985), aff'd, 741 P.2d 714 (Colo. 1987).

Colorado does not require an alleged cause to be the sole cause of an injury. Nicholas v. North Carolina Med. Ctr., Inc., 902 P.2d 462, 471 (Colo. App. 1995), aff'd, 914 P.2d 902 (Colo. 1996). If a defendant's conduct is a substantial contributing cause of injury, it is irrelevant to the causation analysis whether other factors, including forces beyond the defendant's control, also contributed to the

injury. Rupert v. Clayton Brokerage Co. of St. Louis, Inc., 737 P.2d 1106, 1112 (Colo. 1987).

When an injury would not have occurred “but for” the defendant’s conduct, causation is established.

Id. Where, as here, the defendants argue that various factors may have contributed to the State’s injuries, the ultimate determination that a particular factor was a substantial factor for purposes of establishing proximate cause must be made by a trier of fact. Graven, 909 P.2d at 520-21.

The defendants, citing Lyons, argue that the State’s damage claims must fail because the chain of causation may be so attenuated that no proximate cause exists as a matter of law. 770 P.2d at 1257. But in Lyons, the Colorado Supreme Court reversed the district court’s order granting the defendant’s Rule 12(b)(5) motion. The Supreme Court held that “[w]hether proximate cause exists is a question for the jury and only in the clearest of cases, where reasonable minds could draw but one inference from the evidence, does it become one of law to be determined by the court.” Id. at 1256. See also Sharp, 710 P.2d at 1155.

The State’s claims involve allegations of a long-standing conspiracy among multiple defendants to suppress competition, to defraud the people and the State of Colorado and to conceal from them material information. While the allegations may be complex, this factor does not establish that the connections in the evidence are so attenuated as to make proof of proximate cause impossible as a matter of law. This case is not so “clear” that reasonable minds could draw only one inference from the evidence that will be presented. Therefore, dismissal for lack of proximate cause under Rule 12(b)(5) of the State’s request for damages must be denied.

II. THE STATE MAY PURSUE ITS CONSUMER PROTECTION ACT CLAIMS

A. The Colorado Consumer Protection Act.

The Colorado Consumer Protection Act, §§ 6-1-101 through 307, C.R.S. (1997) (“CCPA”), is an exercise of the State’s police power designed “to abate evils which are deemed to arise from the pursuit of business.” People ex rel. Dunbar v. Gym of America, Inc., 493 P.2d 660, 667 (Colo. 1972). In adopting the CCPA, the General Assembly intended to provide “prompt, economical, and readily available remedies against consumer fraud.” Western Food Plan, Inc. v. District Court, 598 P.2d 1038, 1041 (Colo. 1979).

Section 105 of the CCPA provides a list of legislatively determined deceptive trade practices, including four specific practices engaged in by the defendants: § 105(1)(c) -- knowingly making a false representation as to affiliation, connection, or association with or certification by another; § 105(1)(e) -- knowingly making a false representation as to the characteristics, ingredients, uses, benefits, alterations, or quantities of goods, food, services, or property; § 105(1)(g) -- representing that goods, food, services, or property are of a particular standard, quality, or grade, or that goods are of a particular style or model, if the person making the representation knows or should know that they are of another; and § 105(1)(u) -- failing to disclose material information concerning goods, services, or property, which information was known at the time of an advertisement or sale, if such failure to disclose such information was intended to induce the consumer to enter into a transaction.

To remedy these, and other deceptive trade practices, the General Assembly has prescribed a number of broad remedies, including injunctive and other equitable relief (§ 6-1-110), civil penalties (§ 6-1-112), damages, including treble damages (§ 6-1-113), costs and attorney fees (§ 6-1-113) and certain criminal penalties (§§ 6-1-114 and 6-1-305).

B. Section 6-1-106(1) of the CCPA Does Not Insulate Defendants' Conduct.

Section 6-1-106(1) of the CCPA provides a limited exemption for conduct that is “in compliance with the orders or rules of, or a statute administered by, a federal, state, or local governmental agency.” §§ 6-1-106(1), C.R.S. (1997) (emphasis added). Defendants, relying on Suarez v. United Van Lines, Inc., 791 F. Supp. 815 (D. Colo. 1992), argue that their successful use of this exemption depends only upon a showing that their activities “fall under” any order, rule, or statute of a federal agency.

Defendants' reliance on Suarez is entirely misplaced.⁵ Contrary to the dictum in Suarez, section 106(1) does not offer a defense to a defendant whose conduct merely “falls under” some federal rule, order or statute. Section 106(1) is much narrower; it expressly immunizes only conduct that is “in compliance” with a state or federal rule, order, or statute. § 6-1-106(1), C.R.S. The fact of regulation alone is not enough to meet the requirements of section 106(1) -- conduct must actually be shown to

⁵ In Suarez, the federal district court considered whether the Carmack Amendment to the Interstate Commerce Act (49 U.S.C. §11707) preempted the application of the CCPA to the defendant's conduct. Utilizing traditional preemption analysis, the court concluded that the Carmack Amendment preempted plaintiff's claims. 791 F. Supp. at 816. In dictum, the court inexplicably stated that section 106(1) excludes activity that “falls under a statute administered by a federal, state or local agency.” Id. at 817.

“comply” with the dictates of a relevant regulatory scheme. See State ex rel. Woodard v. May Dep’t Stores Co., 849 P. 2d 802, 811 (Colo. App. 1992), aff’d in part, rev’d in part on other grounds, 863 P.2d 967 (Colo. 1993) (holding that, since May D & F’s conduct was “not in compliance with the applicable FTC guidelines, it is not exempt from the CCPA”).

Defendants also assert that “[t]he State does not, and cannot, claim that the cigarette manufacturers have not fully complied with the mandates of the exhaustive federal regulatory program administered by the FTC . . .” (Defendants’ Memorandum, p. 23). At the center of defendants’ argument is a trade rule promulgated by the Federal Trade Commission (“FTC”) in 1964, and the extensive findings supporting that trade rule. See 29 Fed. Reg. 8324-8375 (July 2, 1964) (Defendants’ Memorandum, Exhibit 10). This trade rule, however, was vacated by the FTC the following year and removed from the Code of Federal Regulations. See 30 Fed. Reg. 9484, 9485 (July 29, 1965) (**TAB B**).

Thus, all defendants are left with to support their argument is a reservation of authority to the FTC “with respect to unfair or deceptive acts or practices in the advertising of cigarettes” in the Federal Cigarette Labeling and Advertising Act, 15 U.S.C. § 1336 (“FCLAA”), and a few enforcement actions undertaken by the FTC in the intervening thirty-three years.⁶ Defendants make no attempt to explain

⁶ Defendants also cite, without explaining how it is relevant to an analysis under section 106(1) of the CCPA, the FTC’s obligation under 15 U.S.C. §1337 to submit an annual report to Congress “concerning (1) current practices and methods of cigarette advertising and promotion, and (2) such recommendations for legislation as it may deem appropriate.” (Defendants’ Memorandum, p. 22). Clearly, this obligation does not preempt application of the CCPA to defendants’ conduct.

how either this reservation of enforcement authority, or the meager enforcement activity of the FTC, constitutes a “rule, order or statute” with which defendants must comply for purposes of section 106(1) of the CCPA.⁷ In any event, the question whether defendants acted “in compliance” with some federal rule, order or statute is a decidedly factual one inappropriate for consideration under Rule 12(b)(5).

C. The State Has Standing To Pursue Its CCPA Claims.

Defendants next argue that the State may not seek damages under the CCPA because the State is not a “person” as defined in the CCPA. This argument does not in any way challenge the authority of the Attorney General to seek enforcement remedies against these defendants. A “person” under the CCPA is defined as:

[A]n individual, corporation, business trust, estate, trust, partnership, unincorporated association, or two or more thereof having a joint or common interest, or any other legal or commercial entity.

§ 6-1-102(6), C.R.S. (1997) (emphasis added). Defendants argue that since this definition does not contain the language “government or governmental subdivision or agency” which is included in Colorado’s general statutory definition of the term “person,” § 2-4-401(8), C.R.S. (1997), the General Assembly must have intended to exclude governmental entities, such as the State, from seeking damages

⁷ Defendants cite no authority for the proposition that the Federal Trade Commission Act in any way “occupies the field” or otherwise preempts the operation of state deceptive trade practices statutes. Numerous court decisions stand for exactly the opposite proposition -- that state and federal deceptive trade statutes serve complimentary purposes and can be enforced simultaneously. See, e.g., Bailey Employment System, Inc. v. Hahn, 545 F. Supp. 62 (D. Conn. 1982); Hinds v. Paul’s Auto Werkstatt, Inc., 810 P.2d 874 (Ore. App. 1991); State v. Amoco Oil Co., 293 N.W.2d 487 (Wis. 1980).

under the CCPA. This argument, which is wholly unsupported by case law, is unavailing for several important reasons.

First, the CCPA's definition of "person" contains critical language which reflects the General Assembly's intent to encompass the State within section 102(6). Unlike section 2-4-401(8), the CCPA's definition of "person" includes the phrase "any other legal or commercial entity." The adjective "any" used in a statute is interpreted to mean "all." Winslow v. Morgan County Comm'rs, 697 P.2d 1141, 1142 (Colo. 1985); Austin v. Weld County, 702 P.2d 293, 294 (Colo. App. 1985). It cannot be disputed that the State of Colorado is a "legal entity" under any definition.

Moreover, general provisions, terms, phrases, and expressions used in a statute are to be liberally construed in order that the true intent and meaning of the statute can be given effect. § 2-4-212, C.R.S. (1997). The Colorado Supreme Court has stated that an "expansive approach" must be taken in interpreting the CCPA. May Dep't Stores Co. v. State ex rel. Woodard, 863 P.2d at 973 n.10. In defining "person" to include "any other legal or commercial entity" the legislature evinced no intent to exclude any legal entity from the definition. Rather, relying on the common usage of the language of section 6-1-102(6), and taking an expansive approach to interpreting the CCPA, it is clear that the State is a "person" under the CCPA.

Significantly, in a case involving these same tobacco defendants, a trial court in Maryland held that the state was a "person" under Maryland's Consumer Protection Act. Relying on a definition of "person" identical to that contained in the CCPA, that court was persuaded that the language "or any

other legal or commercial entity” made it clear that the state was a “person” entitled to seek damages for deceptive trade practices. Maryland v. Philip Morris, Inc., No. 96122017/CL211487, slip op. at 36-37 (Cir. Ct. of Baltimore City, Md., May 21, 1997) (Defendants’ Memorandum, Exhibit 1).

Finally, defendants’ argument that the CCPA’s internal construction demonstrates that the Attorney General has no private damage remedy, completely misses the point. The Attorney General does not seek compensatory damages in this action in her capacity as law enforcer under the CCPA.⁸ Rather, with respect to this damages claim, she represents the State of Colorado as its legal counsel in an effort to recover the State’s damages proximately caused by defendants’ deceptive trade practices.

Because the State of Colorado is a “person” under the CCPA, it is entitled to seek damages under section 113 of that Act. Accordingly, defendants’ motion to dismiss the State’s damages claims under the CCPA must be denied.

D. The State’s First Claim for Relief is Not Preempted by the Cigarette Labeling and Advertising Act.

1. Preemption of the State’s claims must be narrowly construed.

Preemption analysis starts with the assumption that federal law does not supersede the State’s historic police powers “unless that is the clear and manifest purpose of Congress.” Cipollone v. Liggett Group, Inc., 505 U.S. 504, 516 (1992) (citing Rice v. Santa Fe Elevator Corp., 331 U.S. 218, 230

⁸ It is in the context of an enforcement action brought by the Attorney General under section 110 or section 112 of the CCPA that statutory attorney fees under section 6-1-113(4), C.R.S. (1997) become relevant. As a person entitled to seek damages under section 113 of the CCPA, the State relies on section 6-1-113(2)(b), C.R.S. (1997), for its entitlement to costs and attorney fees should it prevail in this action.

(1947)); see also Ingersoll-Rand Co. v. McClendon, 498 U.S. 133, 138 (1990) (“[t]he purpose of Congress [is] the ultimate touchstone” of preemption analysis).

The health and safety of each State’s citizens “are primarily, and historically . . . matter[s] of local concern.” Medtronic v. Lohr, ___ U.S. ___, 116 S.Ct. 2240, 2245 (1996). “States traditionally have had great latitude under their police powers to legislate as to the protection of the lives, limbs, health, comfort, and quiet of all persons.” Id. Accordingly, courts are reluctant to find preemption where the result would displace the power of a state to protect the health and safety of its citizens. Wisconsin Public Intervenor v. Mortier, 501 U.S. 597, 605 (1991); Hillsborough County v. Automated Medical Labs, Inc., 471 U.S. 707, 715 (1985).

Courts have expressly applied the health and safety presumption against challenges that state laws or claims are preempted by the Federal Cigarette Labeling and Advertising Act (“FCLAA”), 15 U.S.C. §§ 1331-1341. Cipollone, 505 U.S. at 518; Philip Morris, Inc. v. Harshbarger, 122 F.3d 58, 68 (1st Cir. 1997); Castano v. American Tobacco Co., 870 F. Supp. 1425, 1431 (E.D. La. 1994). Courts must construe the express preemption provision in the FCLAA as narrowly as possible so as to preserve maximum state authority consistent with the Supremacy Clause. See Cipollone, 505 U.S. at 518-520.

2. The CCPA is a proper exercise of police power.

In the first major decision interpreting the CCPA, the Colorado Supreme Court established clearly the purpose and importance of the CCPA:

The right to regulate in the name of the police power is especially clear when the legislative intent is to regulate commercial activities and practices which, because of their nature, may prove injurious, offensive, or dangerous to the public. And this police power relates not only to the public's physical or mental health and safety, but also to the public financial safety. There is a necessary residuum of power which the state possesses to safeguard the interests of its people, and pursuant to this power laws may be passed to protect the public from financial loss, and to abate evils which are deemed to arise from the pursuit of business.

People ex rel. Dunbar v. Gym of America, Inc., 493 P.2d 660, 667 (Colo. 1972) (citations omitted).

Thus, the Court's analysis of the preemptive effect, if any, of the FCLAA on the First Claim for Relief must be drawn as narrowly as possible.⁹ Such an analysis must begin with an examination of the First Claim for Relief in the context of the express preemption language in the original Act and in the 1969 amendments to that Act.

3. The 1965 Act.

Adopted in July 1965, section 5 of the original version of the FCLAA contained the following provision regarding preemption:

- (a) No statement relating to smoking and health, other than the statement required by section 4 of this Act, shall be required on any cigarette package.

⁹ The enactment of express preemption language in the FCLAA "implies that matters beyond that reach are not pre-empted." Cipollone, 505 U.S. at 516.

(b) No statement relating to smoking and health shall be required in the advertising of any cigarettes the packages of which are labeled in conformity with the provisions of this Act.

This original Act was designed to expire on July 1, 1969. Cipollone, 505 U.S. at 514.

Recognizing the precise and narrow nature of this preemption language, the United States Supreme Court concluded that “these provisions merely prohibited state and federal rulemaking bodies from mandating particular cautionary statements on cigarette labels . . . or in cigarette advertisements” Id. at 518. This language did not preempt state law damages actions. Id. at 519-20. Thus, to the extent that the State’s Amended Complaint alleges deceptive trade practices which occurred prior to July 1, 1969, the First Claim for Relief is not preempted by the FCLAA.

4. The 1969 Act.

In 1969, Congress passed the Public Health Cigarette Smoking Act which amended the FCLAA in several ways. In addition to strengthening the warning label required on cigarette packages, Congress modified the preemption provision by replacing the original section 5(b) with a provision that reads:

(b) No requirement or prohibition based on smoking and health shall be imposed under State law with respect to the advertising or promotion of any cigarettes the packages of which are labeled in conformity with the provisions of this Chapter.

15 U.S.C. § 1334(b). Critical to the analysis of whether a particular statute or claim is preempted by this provision is the nature of the duty imposed by that statute or claim. Cipollone, 505 U.S. at 528-29.

If a claim imposes a specific duty “based on smoking and health,” then it is preempted. If the duty imposed is a different or more general one -- such as the duty not to deceive -- then the FCLAA provides no protection. Id.

The State’s First Claim for Relief does not impose a specific duty based on smoking and health. Rather, it flows from the more general obligation not to deceive embodied in section 6-1-105(1)(u) of the CCPA. The CPPA was not promulgated by the General Assembly for the purpose of requiring cigarette manufacturers to warn the public about the dangers of smoking, or to prohibit the advertising or sale of cigarettes unless accompanied by a particular warning. It is, instead, a general police power statute designed to combat deceptive advertising. Gym of America, 493 P.2d at 667.

That such statutory claims survive a preemption analysis under the FCLAA is clear from the following language in Cipollone:

First, in the 1969 Act, Congress offered no sign that it wished to insulate cigarette manufacturers from longstanding rules governing fraud. To the contrary, both the 1965 and the 1969 Acts explicitly reserved the FTC’s authority to identify and punish deceptive advertising practices -- an authority that the FTC had long exercised and continues to exercise This indicates that Congress intended the phrase “relating to smoking and health” (which was essentially unchanged by the 1969 Act) to be construed narrowly, so as not to proscribe the regulation of deceptive advertising.

Id. at 529 (emphasis added).¹⁰ Other courts have sustained claims under state deceptive trade practices statutes, concluding that the general duty not to deceive imposed by such statutes took them

¹⁰ The Court found further evidence of the narrow scope of the FCLAA’s preemption language in the Senate Report on the 1969 Act. “The Senate Report emphasized that the ‘preemption of regulation or

outside the preemptive scope of the FCLAA. See Burton v. R.J. Reynolds Tobacco Co., 884 F. Supp. 1515, 1521 (D. Kan. 1995); Castano v. American Tobacco Co., 870 F. Supp. 1425, 1433 (E.D. La. 1994).

It would be an incongruous reading of Cipollone to conclude that the State could challenge defendants' affirmative misrepresentations (which defendants do not claim are preempted) regarding nicotine addiction, nicotine manipulation and the health effects of smoking and, at the same time, conclude that defendants' failure to disclose material information relating to the falsity of those representations was immunized by the 1969 Act.

In this case, the State does not seek to compel disclosures of product ingredients, nor to impose greater warning requirements in defendants' advertising or promotions. This is not a failure to warn case similar to that brought by the plaintiff in Cipollone.¹¹ Failure to warn claims challenge the sufficiency of package labels and warnings utilizing common law tort principles. Clearly, the FCLAA was intended to be preemptive to avoid differing package labeling requirements from state to state. Cipollone, 505 U.S. at 513-14. In contrast, the State's First Claim for Relief alleges that defendants committed a deceptive trade practice by failing to disclose material information that would have revealed the falsity of the

prohibition with respect to cigarette advertising is narrowly phrased to preempt only State action based on smoking and health. It would in no way affect the power of any State . . . with respect to the taxation or the sale of cigarettes to minors, or the prohibition of smoking in public buildings, or similar police regulations.” 505 U.S. at 529 n.26 (quoting S. Rep. No. 91-566, p. 12 (1969)) (emphasis in original).

¹¹ In Castano, the court determined that plaintiff's fraudulent concealment and Consumer Protection Law claims were not failure to warn claims. 870 F. Supp. at 1436.

representations that they made to the public. Nothing in the FCLAA suggests an intent by Congress to preempt the State from enforcing its laws against deceptive and misleading advertisements.¹²

Because the State's failure to disclose claim does not arise from a specific state-imposed duty "with respect to smoking and health" under the 1969 Act, but rather from a general duty not to deceive, it is not preempted under the narrow holding of Cipollone.

5. The Comprehensive Smokeless Tobacco Health Education Act.

Any preemption analysis of the First Claim for Relief's allegations concerning deceptive trade practices relating to smokeless tobacco products is governed by the express language of the Comprehensive Smokeless Tobacco Health Education Act, 15 U.S.C. §§ 4401-4408 ("CSTHEA").

Section 4406(b) provides, with respect to state and local action:

No statement relating to the use of smokeless tobacco products and health, other than the statements required by section 4402 of this title, shall be required by any State or local statute or regulation to be included on any package or in any advertisement (unless the advertisement is an outdoor billboard advertisement) of a smokeless tobacco product.

15 U.S.C. § 4406(b). The Supreme Court, in Cipollone, interpreted this provision to preempt "only positive enactments by legislatures or administrative agencies that mandate particular warning labels."

505 U.S. at 518-19. Significantly, the CSTHEA also contains a "savings clause," which narrows the

¹² Defendants allege that the entirety of the State's First Claim for Relief is preempted by the FCLAA, including the allegations regarding nicotine addiction and the defendants' manipulation of nicotine. However, neither of these issues was even mentioned in the Congressional reports accompanying the original statute or the 1969 amendments.

scope of its preemptive effect to expressly permit state laws and claims unrelated to “statements required” by the Act:

Nothing in this chapter shall relieve any person from liability at common law or under State statutory law to any other person.

15 U.S.C. §4406(c). Because the CSTHEA expressly limits its preemptive effect to state labeling requirements, the State’s First Claim for Relief, which contains no such requirement, is not preempted as it relates to smokeless tobacco products.

III. THE STATE HAS STANDING TO PURSUE ITS ANTITRUST CLAIMS

The defendants argue that the State’s Fifth Claim for Relief should be dismissed because the State lacks standing to assert an antitrust claim. The defendants’ arguments concerning standing -- none of which are directed at the Attorney General’s authority to pursue injunctions, civil penalties or other sanctions under the Colorado Antitrust Act -- fundamentally misconstrue both the nature of the State’s antitrust claim and the law of antitrust standing and, for the reasons detailed below, must fail.

A. The Colorado Antitrust Act is Intended to Promote the Unrestricted Production of the Highest Quality and Safest Goods.

The defendants have not challenged the State’s substantive claim that the defendants violated the Colorado Antitrust Act. Instead, they rely on a handful of cases, taken out of context, to argue that the State lacks standing to challenge their anticompetitive conduct. Because the purposes underlying the antitrust laws are such an integral part of these decisions, a basic review of these laws is imperative in order to analyze the shortcomings of defendants’ standing arguments.

One of the fundamental tenets of the antitrust laws is that unfettered competition is critical to a free market economy and to the production of the highest quality goods at the lowest prices. Standard Oil Co. v. F.T.C., 340 U.S. 231, 248 (1951) (“The heart of our national economic policy long has been faith in the value of competition”); National Society of Professional Engineers v. United States, 435 U.S. 679, 695 (1978) (“The Sherman Act reflects a legislative judgment that ultimately competition will produce not only lower prices, but also better goods and services”). Conduct which unreasonably restrains or decreases competition is antithetical to this fundamental principle. That is why, under both state and federal antitrust law, it is illegal to conspire, combine or agree to restrain trade or commerce. § 6-4-104, C.R.S.; 15 U.S.C. §1.

Certain types of collusive conduct, like price-fixing, bid rigging, market allocation arrangements, and output restrictions, have such predictable and pernicious anticompetitive effects, and so lack any redeeming value, that they are conclusively presumed to be unreasonable and therefore illegal. See, e.g., United States v. Topco Assocs., Inc., 405 U.S. 596 (1972); Northern Pac. Ry. Co. v. United States, 356 U.S. 1, 5 (1958); United States v. Socony-Vacuum Oil Co., 310 U.S. 150 (1940).¹³ This per se label means that a plaintiff need only prove that the prohibited practice occurred, and is not required affirmatively to demonstrate its competitive unreasonableness. At the same time, a defendant is

¹³ Other types of restraints are analyzed under the “rule of reason,” according to which the finder of fact must determine whether the questioned practice imposes an unreasonable restraint on competition, taking into account a variety of factors, including specific information about the relevant business, its condition before and after the restraint was imposed, and the restraint’s history, nature, and effect. Arizona v. Maricopa County Med. Soc., 457 U.S. 332, 343 and n.13 (1982).

prohibited from attempting to justify the restraint as reasonable. Northern Pac. Ry. Co., 356 U.S. at 5; Socony-Vacuum, 310 U.S. at 220-21. Additionally, no elaborate study of the marketplace is required if the restraint is deemed per se unlawful. National Society of Professional Engineers, 435 U.S. at 692.

It is against this general legal backdrop that the State has alleged -- and for purposes of the defendants' motion these allegations must be accepted as true -- that the defendants have engaged in per se violations of the Colorado Antitrust Act by participating in two long-standing agreements to restrict output. First, the State has alleged that the defendants entered into an agreement over 40 years ago, which agreement continues today, jointly to restrict and suppress their research and development programs in order to prevent any one of them from manufacturing and selling safer tobacco products.¹⁴ This type of collusive output restriction is clearly prohibited by the antitrust laws Allied Tube & Conduit Corp. v. Indian Head, Inc., 486 U.S. 492, 500 (1988) (agreements to restrict competition with respect to any aspect of a product run afoul of the antitrust laws); § 6-4-102, C.R.S. (General Assembly expressly recognizing that competition is fundamental to production of the highest quality commodities and services).

Second, the State has alleged that the defendants also conspired to suppress the flow of complete and accurate information about the health effects of their products. The defendants' agreement has effectively prohibited the competitive flow of information from the defendants about the quality and safety characteristics of their product for more than 40 years, and has deprived consumers

of the ability to make informed choices about the critical issue of safety in a competitive marketplace. Such an agreement is a patent violation of the antitrust laws. See F.T.C. v. Indiana Federation of Dentists, 476 U.S. 447 (1986) (dentists and their trade association conspired unreasonably to restrain trade by agreeing not to provide insurance company with information requested by insurer to evaluate necessity of services and make payment decisions); Sugar Institute v. United States, 297 U.S. 553, 596-97 (1936); United States v. Gasoline Retail Dealers Ass'n, 285 F.2d 688, 691 (7th Cir. 1961) (agreement to limit advertising held to be a per se violation of the Sherman Act).

These output restrictions, the State contends, ultimately caused the tobacco products consumed by Colorado citizens to be more hazardous than they would have been in the absence of the conspiracy. As a direct consequence, the State, which is one of the largest health care purchasers in Colorado, has incurred and will continue to incur much higher health care costs for smoking-related illnesses suffered by its indigent residents and has paid and will continue to pay higher health insurance premiums for its employees.

B. The State Has Suffered Antitrust Injury.

The defendants argue that the State's antitrust claim must be dismissed because the State has not suffered "antitrust injury," and thus lacks antitrust standing. The basic thrust of this argument is that

¹⁴ As alleged in the Amended Complaint (¶¶ 72-97), many of the defendants successfully designed products which effectively reduced known health risks of smoking. Yet, except for some minor test marketing, none of these products were ever manufactured or sold because of the on-going conspiracy.

the State's injuries, if any, flow from the defendants' tortious conduct, not from their violations of the antitrust law.

There are two basic problems with the defendants' argument concerning antitrust injury. The first is that it ignores the facts of this case. As explained above, this case squarely presents serious allegations of anticompetitive conduct which must be accepted as true for purposes of the defendants' motion.

The second problem with the defendants' argument is that it ignores the law. The defendants' position, albeit an illogical one, seems to be that if they committed a tort, then they cannot have also violated the antitrust laws. This is simply not the law. The fact that certain conduct may give rise to both an antitrust claim and another type of claim for relief, including personal injury claims, does not -- as a matter of law or public policy -- exempt the conduct at issue from the antitrust laws. See Hayes v. Solomon, 597 F.2d 958, 972-73 (5th Cir. 1979), cert. denied, 444 U.S. 1078 (1980). Such a holding would effectively vitiate the antitrust laws with respect to all potentially dangerous goods and services.

The Supreme Court has expressly rejected defendants' argument. National Society of Professional Engineers, 435 U.S. at 695-96 (exceptions to the Sherman Act for anticompetitive agreements relating to "potentially dangerous goods and services would be tantamount to a repeal of the statute"). The State's Amended Complaint alleges, inter alia, that the defendants engaged in a long-standing conspiracy pursuant to which they purposefully banned the development and sale of

innovations which would have made their deadly products safer and saved countless lives. The antitrust laws apply to these defendants just as they apply to every other manufacturer.

The defendants also have misconstrued the law regarding antitrust injury. Antitrust injury is one of multiple factors¹⁵ which are relevant in determining whether a plaintiff has

¹⁵ In Associated Gen. Contractors of Cal., Inc. v. California State Council of Carpenters, 459 U.S. 519 (1983), the Supreme Court elaborated on various factors which may be considered in analyzing antitrust standing, noting that it is “virtually impossible to announce a black-letter rule that will dictate the result in every case.” Id. at 536. The factors identified include the causal connection between the antitrust violation and the harm alleged, improper motive, the directness or indirectness of the injury alleged, whether the injury was of a type that Congress sought to redress through the antitrust laws, the speculative nature of damages, the risk of duplicative recoveries or complex apportionment of damages, and whether the denial of standing would leave a significant violation unremedied. Id. at 537-46.

standing to maintain an antitrust damages case.¹⁶ Antitrust injury is defined as:

- (1) injury of the type the antitrust laws were intended to prevent; and
- (2) that flows from that which makes the defendants' acts unlawful.

Brunswick Corp. v. Pueblo Bowl-O-Mat, 429 U.S. 477, 489 (1977).

The purpose of antitrust injury analysis is to deny standing in antitrust cases to plaintiffs seeking to recover damages for losses resulting from increased competition. P. AREEDA & H. HOVENKAMP, ANTITRUST LAW, ¶ 360a at p. 210 (1995) (at its most fundamental level, the antitrust injury requirement precludes recovery for losses resulting from increased competition, even if such competition was caused by conduct violating the antitrust laws). This is because the antitrust laws are designed to promote and increase unfettered competition. Allowing a plaintiff to recover for injuries sustained due to increased competition is antithetical to the purpose of the antitrust laws. Cargill, Inc. v. Monfort of Colo., Inc., 479 U.S. 104, 117 (1986) (“threat of lost profits due to possible price competition following a merger does not constitute threat of antitrust injury”); Brunswick, 429 U.S. 477 (1977); Brown Shoe Co. v. United States, 370 U.S. 294, 320 (1962) (the antitrust laws were enacted for “the protection of competition, not competitors”).

The State’s Amended Complaint, in sharp contrast, seeks to recover damages which flow from a reduction in competition among the defendants caused by their conspiracy to restrict the manufacture and sale of safer products and the dissemination of complete and accurate information about their

¹⁶ The defendants have not challenged the State’s ability to seek civil penalties or injunctive relief. For this reason alone, as explained on pages 5-6 of this Response, the defendants’ motion to dismiss the

products. Such harm is precisely the type of injury that the antitrust laws were designed to prevent.

National Society of Professional Engineers, 435 U.S. at 695; Indiana Federation of Dentists, 476 U.S. 447 (1986).

Significantly, courts considering the issue of antitrust injury in other state tobacco litigation have reached this same conclusion. See Minnesota v. Philip Morris, Inc., No. C1-94-8565, slip op. at 7-8 (D. Ramsey County, MN., May 19, 1995) (**TAB C**) (Order denying defendants' motion to dismiss); Minnesota v. Philip Morris, Inc., No. C1-94-8565, slip op. at 3-8 (D. Ramsey County, MN., January 26, 1998) (**TAB D**) (Order denying defendants' motion for summary judgment on the State's antitrust claims); Washington v. American Tobacco Co., Inc., No. 96-2-15056-8 SEA, slip op. at 3, 7-10 (King County Super. Ct., WA., November 19, 1996) (**TAB E**) (Order on Defendants' Joint motion to dismiss). For all these reasons, the defendants' argument concerning antitrust injury must fail.

C. The State Need Not Be A Market Participant Nor Suffer Direct Injuries To Have Standing To Pursue Its Damages Claims.

The defendants also argue that the State lacks standing to seek damages because it is not suing as a consumer, competitor, or other participant in the Colorado cigarette market. This argument must be rejected for two reasons. First, the antitrust laws do not require a plaintiff to be a market participant and, second, Colorado antitrust law expressly expands the State's standing to seek indirect injuries.

State's antitrust claim should be denied.

1. The State need not be a market participant.

Contrary to the defendants' argument, the antitrust laws do not require that a plaintiff be a participant in the market that is alleged to have been restrained. In Blue Shield of Virginia v. McCready, 457 U.S. 465 (1982), the Supreme Court considered this precise issue and held that an individual who was not a participant within the restrained market had standing to sue for treble damages under § 4 of the Clayton Act.¹⁷ The Court concluded that the plaintiff, who had been forced to pay costs that she would not have incurred in the absence of the conspiracy, had standing because the injury she suffered was "inextricably intertwined with the injury the conspirators sought to inflict on psychologists and the psychotherapy market." McCready, 457 U.S. at 484.

The Court's decision in McCready was greatly influenced by the fact that there was relatively little risk of duplicate recovery engendered by the plaintiff's claim. McCready's psychologist -- who was part of the group targeted by the alleged conspiracy -- had been paid for his services by McCready, and thus had not been injured by the anticompetitive conduct at issue. McCready, in contrast, was "out of pocket" as a consequence of the alleged conspiracy. McCready, 457 U.S. at

¹⁷ The plaintiff in McCready was a psychotherapy patient who asserted an antitrust claim against her group health care insurance plan and a trade association of psychiatrists for allegedly engaging in a conspiracy to exclude and boycott clinical psychologists from receiving compensation under the plaintiff's insurance plan. Plaintiff alleged that as a result of the conspiracy, her insurance company denied her claims for the cost of treatments she received from a psychologist, thus causing her to be injured in her business or property.

475. Thus, in analyzing this antitrust standing issue the Court looked ultimately to who it was that bore the costs associated with the conspiracy and whether there was risk of duplicate recovery.¹⁸

In the present case, there is no question that the State has borne the costs of the conspiracy alleged in the Amended Complaint and that there is almost no risk of duplicate recoveries. It is clear that with respect to indigent tobacco users, whose smoking-related health care costs are covered by the State, that it is the State -- not tobacco users -- that pays for the costs that flow from the conspiracy. Just like the psychologists in McCready, indigent Colorado residents who suffered adverse health consequences from smoking would not have standing to assert an antitrust claim. This is because the increased costs of health care for such residents were either paid for or reimbursed by the State. See Rozema v. The Marshfield Clinic, 977 F. Supp. 1362 (W.D. Wis. 1997) (indigent plaintiffs who have been reimbursed by co-plaintiff Wisconsin Department of Health and Family Services had no standing because they had not suffered any injuries as a result of the defendants' conduct).

¹⁸ Courts before and after McCready have also recognized that a plaintiff need not be a consumer, competitor or participant in the restrained market in order to have antitrust standing. See Mandeville Island Farms, Inc. v. American Crystal Sugar Co., 334 U.S. 219, 236 (1948) (The Sherman Act “does not confine its protection to consumers, or to purchasers, or to sellers. . . . The Act is comprehensive in its terms and coverage, protecting all who are made victims of the forbidden practices by whomever they may be perpetrated”); Ostrofe v. H.S. Crocker Co., Inc., 740 F.2d 739, 746 (9th Cir. 1984); Crimpers Promotions, Inc. v. Home Box Office, Inc., 724 F.2d 290, 296 n. 6 (2d Cir. 1983); Ashmore v. Northeast Petroleum, 843 F. Supp. 759, 769 n.16 (D. Me. 1994); Donahue v. Pendleton Woolen Mills, Inc., 633 F. Supp. 1423, 1438 (S.D.N.Y. 1986).

2. The State has standing to sue for its indirect injuries.

The defendants attempt to take advantage of a doctrine that has developed in federal antitrust law which holds that only parties directly harmed by antitrust violations have standing to assert damage claims based on such violations. This standing prerequisite, known as the indirect purchaser doctrine, was first announced by the Supreme Court in Illinois Brick Co. v. Illinois, 431 U.S. 720 (1977).

In Illinois Brick, the State of Illinois and local governmental entities brought a treble damages action alleging that certain concrete block manufacturers had engaged in a price-fixing conspiracy. The defendants moved to dismiss the complaint on the ground that the plaintiffs lacked standing to assert a damages action under the Clayton Act. The issue before the Court turned on whether indirect purchasers (that is, individuals or entities in the chain of manufacturing or distribution other than the overcharged direct purchaser) had standing to sue under the Clayton Act for treble damages.

The Court concluded that granting damages standing to such indirect purchasers would create risks of double recovery against defendants and necessitate complex and costly inquiries into just how much injury had been passed on to the plaintiffs. Illinois Brick, 431 U.S. at 730-32. Accordingly, the Court held that the plaintiffs lacked standing to bring a claim for treble damages to recover for overcharges resulting from the alleged price-fixing conspiracy. Only those who purchased directly from the conspirators were determined to have standing.

By arguing that the State is not a participant in the relevant market, the defendants are essentially trying to argue that the State's injuries in this case are not sufficiently direct. The critical flaw with this

argument is that Colorado's antitrust statute is fundamentally and purposefully different from the federal antitrust provisions out of which the indirect purchaser doctrine arises. Section 6-4-111(2), C.R.S. -- which the defendants do not mention, analyze or even cite -- contains what is known as a partial Illinois Brick repealer. It expressly provides:

The attorney general may bring a civil action on behalf of any governmental or public entity, with the written consent of such entity, injured, either directly or indirectly, in its business or property by reason of any violation of this article

§ 6-4-111(2), C.R.S. (emphasis added). This provision of the Colorado Antitrust Act is designed to grant indirect purchaser standing to the State.¹⁹

Not only have the defendants studiously omitted reference to this statute, they have also overlooked decisions from other jurisdictions, interpreting very similar indirect purchaser statutes, which have held that other states have standing to assert antitrust claims against these same defendants for the very same restraints of trade. Minnesota v. Philip Morris, Inc., slip op. at p. 8 (**TAB C**); Maryland v. Philip Morris, Inc., No. 96122017/CL211487, slip op. at 40-41 (Cir. Ct. for Baltimore City, Md., May 21, 1997) (Defendants' Memorandum, Exhibit 1). See also Washington v. American Tobacco Co., Inc., No. 96-2-15056-0 SEA, slip op. at 2-10 (King County Super. Ct., Wa., November 19, 1996) (**TAB E**); McGraw v. The American Tobacco Co., No. 94-C-1707, slip op. at p. 7-8 (Cir. Ct. of Kanawha County, W.Va., May 9, 1997) (**TAB A**).

¹⁹ The Supreme Court has held that states are not precluded from passing legislation granting indirect purchaser standing under state antitrust laws. California v. ARC America Corp., 490 U.S. 93, 102 (1989).

In light of this express grant of standing to assert claims for indirect injuries sustained by Colorado governmental or public entities, the defendants' argument must be rejected.

D. The Defendants Have Misconstrued The “Business Or Property” Component Of Antitrust Standing Analysis.

Finally, the defendants argue that the State lacks standing to bring this action for damages because it has not suffered injury to its “business or property.” The shortcomings of this argument, when examined in the context of the antitrust laws, are readily apparent.

The phrase “business or property” is deemed to have little effect on modern antitrust cases. P. AREEDA & H. HOVENKAMP, ANTITRUST LAW, ¶ 360C (1995). This is because the term “property” has been defined expansively. *Id.* at 208. The Supreme Court has held that any person whose money has been diminished by reason of an antitrust violation is injured in his property. Reiter v. Sonotone Corp., 442 U.S. 330, 339 (1979). For purposes of antitrust cases, this means that the “business or property” element is almost always satisfied. P. AREEDA & H. HOVENKAMP, ANTITRUST LAW, ¶ 361 (1995). The one State which has ruled on this specific issue held that the State’s increased health care costs constitute a proper allegation of injury to business or property. People v. Philip Morris, Inc., No. 96 L13146, slip op. at p. 11 (Cir. Ct. of Cook County, Ill., November 13, 1997) (**TAB F**).

The defendants try to circumvent this broad definition by relying on a series of cases involving personal injury claims asserted under the federal Racketeer Influenced and Corrupt Organizations Act (“RICO”) to buttress its contention that the State has not sustained injury to its business or property.

These cases generally hold that pain and suffering and other “personal injuries” do not constitute business or property injury.²⁰

There are three significant problems with this argument. The first problem is that, if it is followed to its logical conclusion, it will mean that manufacturers of dangerous products who do business in Colorado will be able to enter into blatantly anticompetitive agreements concerning the safety dimensions of their products without fear of exposure under the antitrust laws in this State. This is because manufacturers will be able to argue that any injuries flowing from an agreement not to compete based on safety issues are really personal injuries. Such a result would not only be illogical, it would be in direct contravention of the Supreme Court’s holdings: (1) that agreements to restrict competition along any product dimension, including safety, violate the antitrust laws, National Society of Professional Engineers v. United States, 435 U.S. 679, 695 (1978), and (2) that agreements to restrain the competitive flow of information from sellers about the quality and characteristics of their products run afoul of the antitrust laws. F.T.C. v. Indiana Federation of Dentists, 476 U.S. 447 (1986).

The second problem with defendants’ argument in this regard is that, even if this Court concludes that the State’s economic injuries are somehow indirect because they flow from personal

²⁰ See Doe v. Roe, 958 F.2d 763 (7th Cir. 1992) (value of a client’s sexual activity was not “business or property” for purposes of RICO); Bast v. Cohen, Dunn & Sinclair, P.C., 59 F.3d 492 (4th Cir. 1995) (mental anguish did not constitute business or property in a RICO case); Genty v. Resolution Trust Corp., 937 F.2d 899 (3rd Cir. 1991) (personal injuries due to exposure to toxic waste did not constitute injury to business or property under RICO, although economic harm occasioned by loss of market value to home did constitute such injury); Allman v. Philip Morris, Inc., 865 F. Supp. 665 (S.D. Cal. 1994) (the expense of purchasing nicotine patches was not injury to plaintiffs’ business or property for purposes of RICO);

injuries sustained by tobacco users, section 6-4-111(2), C.R.S. clearly grants the State indirect purchaser standing to sue for such economic injuries in any event.²¹

The third problem with the defendants' argument concerning business or property is that the State does not allege that Colorado has somehow become sick, been wounded or otherwise sustained a "personal injury" as a result of the defendants' conduct. Instead, the State has alleged that it has incurred, in addition to other damages, increased health care costs in its capacity as one of the largest purchasers of health care in Colorado as a direct result of the defendants' patently anticompetitive agreements. The type of purely economic damages which the State has sustained flows from the challenged illegal conduct and is encompassed by the Supreme Court's expansive definition of the term "property." See Reiter, 442 U.S. at 339.

For all of these reasons, the defendants' motion to dismiss the State's antitrust claim must be denied.

IV. MARKETING TO CHILDREN -- THE STATE'S PUBLIC NUISANCE CLAIMS

and Grogan v. Platt, 835 F.2d 844 (11th Cir.), cert. denied, 488 U.S. 981 (1988) (injuries resulting from murder of federal agents did not constitute injury to business or property for purposes of RICO).

²¹ The defendants' reliance on City and County of San Francisco v. Philip Morris, Inc., 957 F. Supp. 1130 (N.D. Cal 1997) is misplaced. In City and County of San Francisco, the court determined that the plaintiffs' RICO claims were derivative of the primary victims' claims. Because the court held that the primary victims, individual smokers, suffered personal injuries, the plaintiffs were held not to have suffered injury to their business or property. Because the court's analysis arose in the context of a RICO claim, rather than a state antitrust act, the court in City and County of San Francisco appropriately did not address the application of indirect purchaser standing to the facts of the case.

The State's Sixth and Seventh Claims for Relief focus primarily on the defendants' illegal marketing of tobacco products to Colorado's children. Specifically, the Seventh Claim for Relief alleges that the defendants contributed to the delinquency of generations of minors, a class 4 felony, by inducing, aiding and encouraging minors to purchase tobacco products in violation of section 18-13-121(2), C.R.S. (1997) (any person under the age of eighteen who purchases tobacco products in Colorado commits a class 2 petty offense). The proceeds traceable to such conduct are a class 1 public nuisance subject to forfeiture under 16-13-303(3)(b), C.R.S. (1997).²²

The State's Sixth Claim for Relief asserts that defendants' conduct also constitutes a class 3 public nuisance as a "business, occupation, operation or activity prohibited by a Colorado statute." See § 16-13-305(1)(a), C.R.S. (1997).

²² Section 16-13-303(3)(b), C.R.S. (1997) defines as a class 1 public nuisance subject to forfeiture "all proceeds traceable to any public nuisance act." Section 16-13-301(2.3) defines "public nuisance act" as "any of the crimes, offenses or violations set forth in section 16-13-303(1)(a) to (1)(m), regardless of the location where the act occurred." Section 16-13-303(1)(i) applies to "any felony not otherwise included in this section."

A. The FCLAA Does Not Preempt the State’s Public Nuisance Claims.

Defendants contend that because the State’s public nuisance claims involve allegations that the defendants targeted minors in their advertising campaigns, they must be preempted under the Federal Cigarette Labeling and Advertising Act, 15 U.S.C. §§ 1331-1341 (“FCLAA”). In defendants’ view, federal law should supersede and invalidate virtually any effort by a state to protect its children from the dangers of tobacco, if such effort has any effect whatsoever upon tobacco advertising. Because the FCLAA is concerned with warning labels on cigarette packages and not with the state’s historic police powers to protect its youth, this argument must fail.

The “appropriate inquiry,” in analyzing whether a claim for relief is preempted under the FCLAA, “is not whether a claim challenges the ‘propriety’ of advertising and promotion, but whether the claim would require the imposition under state law of a requirement or prohibition based on smoking and health with respect to advertising or promotion.” Cipollone v. Liggett Group, Inc., 505 U.S. 504, 525 (1992).²³ Even if the State’s public nuisance claims amount to a “requirement or prohibition” within the meaning of the FCLAA, they are nonetheless not preempted by the FCLAA because they are neither “based on smoking and health” nor “with respect to advertising and promotion.”

The California Supreme Court recently reviewed an identical preemption argument under the FCLAA advanced by tobacco company defendants in a lawsuit challenging R.J. Reynolds “Old Joe Camel” advertising campaign. That court acknowledged the fallacy of this preemption argument:

²³ Cipollone is discussed in greater detail in Section II D. of this Response, supra. at pp. 17-23.

Reynolds argues that because its cigarettes are labeled in conformity with federal law, California may not impose any regulation with respect to advertising the cigarettes if the regulation is “based on smoking and health.” The prohibition against selling cigarettes to minors is based on underlying health concerns, the argument continues, and therefore the state may not impose any requirement or prohibition with respect to advertisements of cigarettes that target minors.

Reynolds contends, in effect, that if it had used billboards depicting Old Joe Camel stating in huge block letters, “Kids, be the first in your fourth grade class cool enough to smoke Camels”; or, to use the example of the Court of Appeals, “if Reynolds had . . . presented Teenage Ninja Mutant Turtles on children’s lunch boxes to promote cigarette smoking,” California could do nothing about it, for any attempt to do so would be a requirement or prohibition “based on smoking and health.” Only the federal government, Reynolds claims, can prevent advertisements that urge minors to smoke, no matter how blatantly.

Mangini v. R.J. Reynolds Tobacco Co., 875 P.2d 73, 79 (Cal. 1994).

The Mangini court properly applied the Cipollone standards to conclude that the plaintiff’s claims were not preempted by the FCLAA. It held that “Congress left the states free to exercise their police power to protect minors from advertising that encourages them to violate the law.” Id. at 83.²⁴ The court further held that the plaintiff’s claim was not preempted by the FCLAA because the predicate duty at issue was not based on smoking and health, but rather on the prohibition against engaging in unfair competition by advertising illegal conduct or by encouraging others to violate the law. Id. at 80. “[T]he phrase based on smoking and health fairly but narrowly construed does not encompass the

²⁴ See S. REP. NO. 91-566, at 12 (1969), reprinted in 1970 U.S.C.C.A.N. 2652, 2663 (preemption under FCLAA “would in no way affect the power of any state . . . with respect to . . . the sale of cigarettes to minors”).

more general legal duty not to 'unfairly assist or advertise illegal conduct.' Id. (quoting Cipollone, 505 U.S. at 529).²⁵

Similarly, in Penn Adver. of Baltimore, Inc. v. Mayor and City Council of Baltimore, 63 F.3d 1318 (4th Cir. 1995), vacated and remanded on other grounds, ___ U.S. ___, 116 S.Ct. 2575, modified, 101 F.3d 332 (4th Cir. 1996), the Fourth Circuit Court of Appeals held that a Baltimore ordinance prohibiting the placement of outdoor cigarette advertising in certain areas of the city frequented by minors was not preempted by the FCLAA. The court of appeals found that the ordinance had been enacted to effectuate a state prohibition against minors possessing or using tobacco products. Id. at 1321.

The Colorado statutes at issue here are part of a larger effort by this State to protect its children at a time in their lives when they are not mature enough to make informed decisions on their own.²⁶ The duty underlying the tobacco prohibitions in Colorado is to avoid the physical and emotional endangerment of children. Because the predicate duty is not one based upon smoking and health, a claim based upon section 18-13-121, C.R.S. (1997), is not preempted by the FCLAA.²⁷

²⁵ The court in Mangini also noted that the original version of the state prohibition against the sale of tobacco to minors had been enacted in 1891, "long before current health concerns, and specifically the health concerns that fuel this lawsuit, arose." 875 P.2d at 81. "This shows," wrote the court, "that the state's protective role, and not primarily health concerns, motivated the prohibition against selling cigarettes to minors." Id.

²⁶ The original versions of the Colorado statutes at issue here also flow from a long history of efforts to protect Colorado's youth dating back more than 100 years. L. 1891, Colo. Sess. Laws, p. 60, §§ 4-9 (state penal code addressing good morals and the protection of children included a prohibition against

Moreover, the prohibitions against the purchase of tobacco products by minors and contributing to the delinquency of minors are not requirements “with respect to cigarette advertising or promotion.” Cipollone, 505 U.S. at 525. Neither statute attempts to regulate or control the content of defendants’ advertising. This factor was significant in Penn Advertising, where the regulation “simply restrict[ed] the location of cigarette advertising signs, irrespective of the nature of the message communicated.” 63 F.3d at 1324.

Likewise, in Mangini, the California Supreme Court held that the plaintiff’s claim was not preempted by the FCLAA because the prohibitions against advertisements targeting minors did “not require Reynolds to adopt any particular label or advertisement ‘with respect to any relationship between smoking and health’; rather, they forbid any advertisements soliciting unlawful purchases by minors.” 875 P.2d at 80 (emphasis added). Unlike the statutes framing the State’s public nuisance claims, and in contrast to the claims and remedies in Penn Advertising and Mangini, courts have limited the application of Cipollone to requirements that seek to directly regulate the content and format of advertising. See Vango Media, Inc. v. City of New York, 34 F.3d 68 (2d Cir. 1994) (city ordinance requiring the display on city-licensed taxicabs of one public health message relating to smoking and health for every four cigarette advertisements was preempted under the FCLAA); Chiglo v. City of selling cigarettes to any person under the age of 16); L. 1891, Colo. Sess. Laws, p. 131, §1 (making it unlawful to sell or give tobacco to children under 16 years of age).

²⁷ The national policy supporting a State’s police power to regulate in the interests of the health and safety of its children is further reflected in federal legislation, enacted in 1992, which expressly supports,

Preston, 909 F. Supp. 675 (D. Minn. 1995) (a local ordinance prohibiting the display of “point of sale” advertising of cigarettes in retail establishments and dictating the size and content of signage stating that tobacco products were for sale was preempted).²⁸

For all of these reasons, defendants’ preemption argument must fail.

B. The Smokeless Tobacco Act Does Not Preempt the State’s Public Nuisance Claims.

As alleged in the Amended Complaint, a large share of the tobacco illegally acquired and used by minors in Colorado involves products other than cigarettes, primarily smokeless tobacco.

Smokeless tobacco is regulated under a different federal statute, the Comprehensive Smokeless Tobacco Health Education Act 15 U.S.C. §§4401-4408 (“CSTHEA”). The CSTHEA has its own distinct and decidedly narrow preemption provision, which expressly defers to claims under state law that concern any issue other than package labeling. 15 U.S.C. § 4406(c).²⁹ The State’s public nuisance claims, which are not based on package labeling, cannot be preempted by CSTHEA.

through block grants, state and local regulations that prohibit and discourage tobacco use by minors. P.L. 102-321, Title II, § 202 (July 10, 1992), codified at 42 U.S.C. § 300x-26(a).

²⁸ Defendants also rely on Sparks v. R.J. Reynolds Tobacco Co., Case No. C94-783C (W.D. Wa. Dec. 9, 1994), as “[t]he only federal court decision on point.” Defendants’ Memorandum at pp. 36-37. However, like Vango and Chiglo, Sparks is readily distinguished. The “requirement” at issue in Sparks involved an injunction sought by plaintiff to compel Reynolds to issue “corrective advertising” to counter the effects of Reynolds’ “Old Joe Camel” campaign.

²⁹ See Section II D. of this Response, supra. at p. 23.

C. The Bagby Doctrine Does Not Bar the State’s Public Nuisance Claim.

Defendants argue that the felony of contributing to the delinquency of a minor cannot form the basis for the State’s class 1 public nuisance claim because the General Assembly intended all prosecutions involving minors and tobacco to be made under section 18-13-121, C.R.S. (1997). This argument misstates Colorado law relating to the ability of a prosecutor to charge under either a general or a special criminal statute unless a legislative intent is shown to limit prosecution to the special statute. See People v. Westrum, 624 P.2d 1302, 1303 (Colo. 1981).³⁰

The rule defendants seek to invoke to block the State’s class 1 public nuisance claim was first, and most clearly, articulated in People v. Bagby, 734 P.2d 1059 (Colo. 1987). In Bagby, the defendant was charged with a class 5 felony, offering a false instrument for filing (§ 18-5-114, C.R.S. (1997)). She moved to dismiss this charge, arguing that the Colorado Liquor Code defined as a misdemeanor the identical conduct of submitting false information on an application for a liquor license. See § 12-47-903(1)(a), C.R.S. (1997) (formerly at § 12-47-130, C.R.S.). Citing the rule articulated in Westrum, the Supreme Court upheld the dismissal of the felony count, concluding that the General Assembly intended to limit prosecutions involving conduct in the context of liquor sales and licensing to the special provisions of the Colorado Liquor Code. Bagby, 734 P.2d at 1062.

³⁰ It is far from clear that this rule, and defendants’ attempt to invoke it, has any relevance in the context of a civil public nuisance action. In any event, because defendants so completely misapply it to the facts of this case, and without conceding its applicability in the civil context, the State will address it here.

Bagby is inapplicable to the State’s class 1 public nuisance claim for at least two critical reasons. First, the Bagby court limited its holding to the circumstances of that case. It took great care to describe the Liquor Code as a “comprehensive regulatory program, with detailed attention to various types of punishment for different violations thereof.” Id. That regulatory scheme stands in stark contrast to the minimal prohibitions regarding underage tobacco purchases contained in section 18-13-121(2), C.R.S. (1997). It stretches credulity to argue that this single section is comparable in any fashion to the comprehensive regulatory structure of the Liquor Code.³¹

More fundamentally, unlike the defendant in Bagby, these defendants could not face prosecution under two enactments providing different degrees of punishment. The State has not alleged that defendants violated subsection (1) of section 18-13-121 (knowingly furnishing tobacco products to minors), and defendants could not violate subsection (2) of section 18-31-121 (illegal purchase of tobacco products by minors). The Amended Complaint only alleges that defendants violated section 18-6-701 by inducing, aiding or encouraging minors to purchase tobacco products in violation of state law. Thus, the factual scenario which gave rise to the holding in Bagby, and to defendants’ argument, does not exist here.³²

³¹ Because both section 18-13-121(2), C.R.S. (illegal tobacco purchases) and section 18-6-701, C.R.S. (contributing to the delinquency of a minor) are both contained in the Criminal Code, defendants’ argument is also defeated by application of section 18-1-408(7), C.R.S. (1997). This section provides that the same conduct, if defined as criminal conduct in different enactments of the Code, may be prosecuted under either enactments even if one provides for a harsher penalty than the other.

³² Defendants also rely on People v. O’Donnell, 926 P.2d 114 (Colo. App. 1996). In O’Donnell, the defendant faced a felony prosecution for contributing to the delinquency of a minor by providing alcohol to

Finally, this Court should ignore defendants' plaintive cry that it is "inconceivable" that conduct defined as a petty offense under section 18-13-121(1) could be prosecuted as a felony under section 18-6-701. Putting aside the fact that the State has not alleged that defendants violated 18-13-121(1) ("furnishing" tobacco to minors), this is precisely what the General Assembly intended when it defined the crime of contributing to the delinquency of minors to include inducing, aiding or encouraging a child to violate "any federal or state law, municipal or county ordinance." § 18-6-701(1), C.R.S. (1997) (emphasis added). The General Assembly properly concluded that conduct aimed at encouraging children to violate any law was so morally reprehensible as to warrant severe criminal penalties.

D. The State Is Entitled To Establish At Trial That The Proceeds Of Cigarette Purchases By Minors Are Traceable To Defendants' Conduct.

The defendants contend that the Court should dismiss the State's claim for proceeds traceable to the defendants' public nuisance because of the complexity involved in tracing such proceeds. Defendants' argument contravenes the fundamental legal standards applicable to a Rule 12(b)(5) motion to dismiss and, accordingly, must be denied.

The court, in reviewing a Rule 12(b)(5) motion, can consider only matters stated therein and must not go beyond the confines of the pleading. Rosenthal v. Dean Witter Reynolds, Inc., 908 P.2d 1095, 1099 (Colo. 1995). Here, the State has properly alleged that the defendants engaged in

juveniles. O'Donnell's conduct was also proscribed as a misdemeanor under a specific section of the Liquor Code. Invoking the holding of Bagby, the Court of Appeals concluded that the prosecutor was limited to proceeding under the Liquor Code. 926 P.2d at 116. There is no similar overlap between section 18-6-701 and the proscriptions contained in section 18-13-121(2).

wrongful conduct, that the defendants obtained proceeds from that conduct, and that all proceeds traceable to the wrongful conduct should be forfeited to the State. (Amended Complaint ¶¶ 149-153, 190-192). These factual allegations must be deemed true and admitted for purposes of the defendants' motion.

Where an issue turns upon disputed facts, the matter may not be disposed of in a pretrial motion under Rules 12 or 56, C.R.C.P. Cline v. Rabson, 856 P.2d 1, 2-3 (Colo. App. 1992) (inappropriate for trial court to act in capacity of pre-trial factfinder). Proof that certain proceeds are traceable to the defendants' conduct is an evidentiary hurdle that the State must establish at trial. But that hurdle remains an issue of fact, not of law. See Northwest Water Corp. v Pennetta, 479 P.2d 398, 401 (Colo. App. 1970) (issues involved in proving a private nuisance claim are questions of fact).

The only authority that defendants rely upon to support their concern that the State faces an impossible task in tracing the proceeds from their conduct is People v. Cerrone, 780 P.2d 562 (Colo. App. 1989). This case is irrelevant because, in relation to the items of personal property which the trial court ordered forfeited, it involved an appeal from a full evidentiary hearing on the merits before a trial court acting as finder of fact. Although the defendants may later try to argue that Cerrone outlines the burden of proof that the State bears at trial, Cerrone does not suggest that this Court may rule on this factual issue in the context of a Rule 12(b)(5) motion to dismiss.

V. THE STATE'S COCCA CLAIMS SHOULD NOT BE DISMISSED.

The defendants argue that the State's claims for damages under the Colorado Organized Crime

Control Act, §§ 18-17-101 through 109, C.R.S. (1997) (“COCCA”), should be dismissed because the State: (1) is not a “person” with standing to sue for treble damages; (2) has not alleged that it detrimentally relied upon the defendants’ alleged acts of mail and wire fraud; and (3) has not sufficiently alleged defendants’ violations of COCCA. Defendants do not challenge the Attorney General’s authority to seek an injunction or other civil sanctions under COCCA. Defendants’ arguments misconstrue the plain language of COCCA, and merely raise factual issues about defendants’ alleged conduct which are inappropriate for resolution in a Rule 12(b)(5) motion. None of these arguments provides a basis for dismissal of the State’s COCCA claims.

COCCA was adopted by the Colorado General Assembly in 1981 to provide enhanced criminal sanctions and civil remedies for certain types of unlawful business-related activities. People v. Chaussee, 880 P.2d 749, 754 (Colo. 1994). COCCA imposes stringent civil remedies upon those who use or invest proceeds received from a pattern of racketeering in the establishment or operation of an enterprise, § 18-17-104(1), C.R.S. (1997); acquire or maintain an interest in or control of an enterprise through a pattern of racketeering, § 18-17-104(2), C.R.S. (1997); knowingly conduct or participate in an enterprise through a pattern of racketeering, § 18-17-104(3), C.R.S. (1997); or conspire to engage in any of these other prohibitions, § 18-17-104(4), C.R.S. (1997). Such racketeering activity generally consists of a series of related felonies defined by state and federal law. § 18-17-103(3) and (5), C.R.S. (1997).

COCCA was patterned after the federal Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. §§ 1961-1968 (“RICO”). Federal cases interpreting RICO, while not dispositive, are instructive in analyzing similar issues arising under COCCA. New Crawford Valley, Ltd. v. Benedict, 877 P.2d 1363, 1370 (Colo. App. 1993). Where there is Colorado authority interpreting COCCA, that authority is controlling. Tallitsch v. Child Support Servs., Inc., 926 P.2d 143, 147 (Colo. App. 1996). When construing the provisions of COCCA, the court is required to use rules of liberal construction to effectuate the intent and purpose of the statute. § 18-17-108, C.R.S. (1997).

COCCA varies from its counterpart RICO provisions in several critical respects. A comparison of the parallel provisions of both statutes reveals COCCA’s broader, more flexible terms, as well as its more expansive remedies. Compare § 18-17-106(1)-(12), C.R.S. (1997) with 18 U.S.C. § 1964(a)-(d). For instance, COCCA provides a damages remedy for “any person injured” by a statutory violation, not merely for those injured in their “business or property” as required by RICO. Compare § 18-17-106(7), C.R.S. (1997) with 18 U.S.C. § 1964(c).

COCCA’s comprehensive civil remedies are available to the Attorney General, the state district attorneys, and to any person injured by reason of any of these unlawful acts. § 18-17-106, C.R.S. These remedies include injunctive relief, property seizures and forfeitures, treble damages, attorney fees, and costs. § 18-17-106, C.R.S. (1997).

The State’s Amended Complaint sets forth two COCCA claims. The Eighth Claim for Relief alleges that each defendant associated with a racketeering enterprise -- in this case, a collective group of

tobacco companies, public relations firms, trade associations, research entities and other persons -- and knowingly conducted and participated in the affairs of the enterprise through a pattern of racketeering activities (mail and wire fraud), in violation of § 18-17-104(3). (Amended Complaint ¶ 194).

The Ninth Claim for Relief alleges that the defendants conspired to receive racketeering proceeds and to use such proceeds to establish a racketeering enterprise; maintained an interest in or control of such enterprise; and knowingly conducted or participated in the enterprise through certain mail and wire fraud racketeering activities, in violation of § 18-17-104(4) (Amended Complaint ¶ 196).

Each of these COCCA violations has caused the State of Colorado to sustain damages in the form of millions of dollars in additional health care expenditures for its employees and indigent residents.

A. The State Is A “Person” Entitled To Seek Treble Damages, Attorney Fees And Costs Under COCCA.

Defendants argue that the State lacks standing to seek treble damages pursuant to its Eighth and Ninth Claims for Relief because the State is not an injured “person” under COCCA.³³ This argument overlooks the plain language of COCCA and conflicts with its underlying intent and purpose.

COCCA defines the term “person” as “any individual or entity holding or capable of holding a legal or beneficial interest in property.” § 18-17-103(4), C.R.S. (emphasis added). The phrase “any entity” clearly indicates the General Assembly’s intent to extend COCCA’s provisions to the State as an

³³ Defendants do not challenge the State’s standing to bring a law enforcement action for, among other things, injunctive relief, civil forfeiture of racketeering proceeds, or other money judgments provided by section 18-17-106(1)-(5), (8) and (10), C.R.S. (1997). All that the defendants challenge in their Rule 12(b)(5) motion is the State’s standing to recover damages.

entity capable of holding a legal or beneficial interest in property. Numerous Colorado statutes recognize this capability. See, e.g. Colo. Const. Art. XXVII, § 1; § 24-80-209, C.R.S. (1997); §§ 25-25-104(1) and 108, C.R.S. (1997); § 17-24-106.6, C.R.S. (1997); § 24-1-133, C.R.S. (1997).

In an attempt to show that the State is not a person under COCCA, the defendants rely upon United States v. Bonanno, 879 F.2d 20 (2nd Cir. 1989), a Second Circuit opinion holding that the United States was not a “person” capable of recovering treble damages under RICO. This case provides no support for the defendants’ argument.

Defendants’ use Bonanno to draw an analogy between the federal government suing for damages under RICO and the State of Colorado suing for damages under COCCA. The holding in Bonanno does not apply to COCCA, because the dual structure of RICO which formed the basis for that decision has no parallel in COCCA. In Bonanno, the Court relied on the distinctive “dual structure” of RICO, establishing “two classes of actions,” whereby the governing sovereign has a host of exclusive enforcement remedies, including criminal sanctions, penalties, forfeitures and injunctive relief, while injured parties other than the government have recourse only to damages. 879 F.2d at 24. The same cannot be said of COCCA, which has its own unique structure. Both the State of Colorado, through the Attorney General, and private persons may seek enforcement remedies under COCCA, including: injunctive relief, § 18-17-106(5), C.R.S. (1997) (state enforcement) and § 18-17-106(6), C.R.S. (1997) (any person injured); and civil forfeiture, § 18-17-106(2), C.R.S. (1997) (state enforcement)

and § 18-17-106(7)(b), C.R.S. (1997) (any injured person has right or claim to forfeited property). In fact, the only remedy reserved exclusively to the State in its enforcement capacity is criminal sanctions, § 18-17-105, C.R.S. (1997).

More importantly, the court in Bonanno expressly recognized that state governmental entities and their subdivisions are “persons” that have standing to sue for damages under RICO.

879 F.2d at 25.³⁴ It would be illogical to conclude that, while the State could sue for damages under RICO, it could not proceed similarly under COCCA. This is especially true given the fact that, in enacting COCCA, the General Assembly expressed its intent to enhance sanctions and expand remedies because the remedies available to the State at the time were “unnecessarily limited in scope and impact.” § 18-17-102, C.R.S. (1997).

The defendants’ argument that the State is not a person under COCCA must fail.

B. The State Has Sufficiently Alleged The Defendants’ Pattern Of Racketeering Activity.

Defendants argue that the State’s Amended Complaint fails to describe the conduct which gives rise to the COCCA predicate offenses of mail and wire fraud. They further argue that the Amended Complaint fails to describe how the State was affected by defendants’ fraudulent conduct. These arguments ignore the fact that the Amended Complaint details the numerous, repeated and intentional racketeering activities engaged in by the defendants over a period of decades, and its impact upon the State of Colorado. Certainly, the State’s Amended Complaint provides defendants sufficient information to understand the allegations and to prepare a response.

To state a claim under COCCA, the State must describe defendants’ pattern of racketeering activity. A pattern of racketeering activity means “engaging in at least two acts of racketeering activity

³⁴ See Alcorn County v. U.S. Interstate Supplies, Inc., 731 F.2d 1160 (5th Cir. 1984)) (county government permitted to maintain claim for treble damages under RICO in bid to recover amounts paid for

which are related to the conduct of the enterprise.” § 18-17-103(3), C.R.S.; Chaussee, 880 P.2d at 758. Such violations are known as “predicate acts.” See, e.g., New Crawford Valley, 877 P.2d at 1371.

In this action, the State alleges that during the relevant times described in the Amended Complaint, defendants engaged in a pattern of racketeering activity by repeatedly violating two federal criminal statutes -- mail fraud, 18 U.S.C. § 1341, and wire fraud, 18 U.S.C. § 1343. The elements of mail fraud are (1) a scheme to defraud, and (2) a mailing made for the purpose of executing the scheme. Schmuck v. United States, 489 U.S. 705, 710 (1989). The elements of wire fraud are virtually identical to mail fraud, the only difference being that the fraudulent scheme must be facilitated by an interstate wire communication, typically by telephone, radio, or television. 18 U.S.C. § 1343.

The State has pled each of the elements of its COCCA claims with sufficient particularity under Rule 9(b), C.R.C.P. The Amended Complaint meets these standards because it describes clearly and in detail the ongoing fraudulent schemes that the defendants utilized to market their tobacco products and to maximize their monetary profits. The Amended Complaint describes defendants’ coordinated efforts, beginning in 1953, to form an enterprise to disseminate misleading information about defendants’ tobacco companies and their products. (Amended Complaint ¶¶ 51-53). Among other things, this enterprise disseminated false or fraudulent advertisements, broadcast commercials, and other communications which were intended by defendants to mislead the public about the health effects of purchases made in violation of state bidding laws); Pennsylvania v. Cianfrani, 600 F. Supp. 1364 (E.D. Pa. 1985) (Commonwealth prevails on claim to recover treble damages under RICO for payroll fraud).

tobacco use. (Amended Complaint ¶¶ 57-63, 69, 120). The Amended Complaint also describes how the activities were facilitated in the normal course of defendants' business through the use of mail, radio, television, and telephone communications for the purpose of maximizing sales of defendants' tobacco products and obtaining money from those sales. (Amended Complaint ¶¶ 155-160). Finally, the Amended Complaint describes how, as a result of defendants' conduct, the State has incurred millions of dollars in costs annually for its increased health care expenditures related to tobacco illnesses. (Amended Complaint, ¶¶ 162-163).

C. The State Is Not Required To Show That It Relied Upon Defendants' Fraudulent Conduct.

Next, the defendants argue, without the benefit of any legal authority, that the State's request for damages under COCCA must be dismissed because the State has failed to allege that it was the intended recipient of the defendants' fraudulent conduct or that it relied upon any fraudulent communication made by any of the defendants.

Colorado courts have not yet addressed this legal issue in the context of a COCCA case. While detrimental reliance is required under RICO, such reliance need not be that of the plaintiff. Armco Indus. Credit Corp. v. SLT Warehouse Co., 782 F.2d 475, 482 (5th Cir. 1986) (“[t]o find a violation of the federal mail fraud statute [as an alleged predicate act under RICO] it is not necessary that the victim have detrimentally relied on the mailed representations”). See also Israel Travel Advisory Serv. v. Israel Identity Tours, 61 F.3d 1250, 1257 (7th Cir. 1995) (a business may assert a RICO injury where defendant directs a campaign of misinformation at its customers); Mid Atlantic Telecom,

Inc. v. Long Distance Servs., Inc., 18 F.3d 260 (4th Cir. 1994), cert. denied, 513 U.S. 931 (1994) (long distance telephone carrier permitted to maintain RICO claim against competitor for allegedly fraudulently billing customers and diverting business away from plaintiff); Prudential Ins. Co. of America v. United States Gypsum Co., 828 F. Supp. 287 (D.N.J. 1993) (building owner permitted to maintain RICO claim for economic injuries against asbestos manufacturers who allegedly misinformed the public about the safety of asbestos); Galerie Furstenberg v. Coffaro, 697 F. Supp. 1282 (S.D.N.Y. 1988) (plaintiff properly alleged predicate acts of mail and wire fraud by claiming that defendant sold counterfeit artwork to third party customers, thereby depriving plaintiff of sales of original works).

In this case, the State has sufficiently alleged such reliance. The Amended Complaint adequately describes the defendants' misrepresentations, the fact that such misrepresentations were made with the express intent that the public would rely on such representations, and the fact that such misrepresentations encouraged more smoking. No additional reliance by the State is required to support its damages claim under COCCA.

D. The State Should Be Granted Leave To Amend Its Ninth Claim For Relief.

The State concedes that its Ninth Claim for Relief is incomplete. Thus, the State requests leave to amend this claim to include a proper reference to the alleged violation of section 18-17-104(4), R.C.S. (1997). Granting such leave at this time is necessary to secure just, speedy, and inexpensive determination of all issues in this case and would clearly serve the interests of justice. See Varner v.

District Court, 618 P.2d 1388, 1390 (Colo. 1980); In re Estate of Blacher, 857 P.2d 566, 568-69 (Colo. App. 1993).

VI. THE ATTORNEY GENERAL MAY SEEK RESTITUTION AND DISGORGEMENT

Defendants mischaracterize the equitable remedies sought in the Amended Complaint as just another form of damages to compensate the State of Colorado for its tobacco-related health care expenditures. They argue that the State is not entitled to the equitable remedy of restitution, because it has not conferred a benefit upon the defendants and because it already has an adequate remedy at law.³⁵ This is not, however, a case in which the State seeks restitution to compensate for its damages caused by defendants' conduct. Rather, as is made clear in the State's Amended Complaint, it is the Attorney General, relying upon specific statutory authority, who demands that defendants disgorge the proceeds of their illegal conduct.

A. The Attorney General has Specific Statutory Authority to Seek Restitution From These Defendants.

The CCPA expressly authorizes the Attorney General to seek restitution as an enforcement mechanism to enforce its prohibitions against deceptive trade practices. Section 110 of the CCPA provides, in part;

³⁵ Disgorgement of profits is essentially nothing more than one of several possible vehicles for restitution. See Earthinfo, Inc. v. Hydrosphere Resource Consultants, Inc., 900 P.2d 113, 118 (Colo. 1995). Therefore these remedies are considered synonymous for purposes of the following argument.

The court may make such orders or judgments as may be necessary . . . to prevent any unjust enrichment by any person through the use or employment of any deceptive trade practice.

§ 6-1-110(1), C.R.S. (1997). The only limitation expressed in section 110(1) is that the defendants' unjust enrichment must occur "through the use or employment of any deceptive trade practice." This section does not require that the State or the Attorney General must first confer some benefit upon a defendant. In fact, such a requirement would render this legislatively-created enforcement remedy meaningless for the simple reason that a defendant, engaging in a deceptive trade practice, would never have a "benefit" conferred upon it by the State. The legislative purpose behind the CCPA to provide "prompt, economical, and readily available remedies against consumer fraud" would be frustrated if the Attorney General could not seek restitution. Western Food Plan, Inc. v. District Court, 598 P.2d 1038, 1041 (Colo. 1979).

Similarly, COCCA permits the Attorney General to obtain "[a]ll property, real or personal, including money, used in the course of, intended for use in the course of, derived from, or realized through conduct in violation of . . . [the Act]." § 18-17-106(2), C.R.S. (1997) (emphasis added). Although characterized in COCCA as a "civil forfeiture," rather than as restitution or disgorgement, the purpose is the same -- to deprive a defendant of the proceeds of his illegal conduct. That clear legislative purpose is not served if the Attorney General must first establish that the State conferred some benefit upon that defendant.

B. Common law Requirements In Colorado Do Not Apply To The Extent That They Have Been Modified Or Superseded By Statute.

Where a statute such as the CCPA specifically provides that the court may order disgorgement, the language of that statute controls, not the common law. In a statutory enforcement action brought on behalf of the public, the ordinary requirements of equity are relaxed in order to fulfill the legislative purposes of the statute being enforced. See Western Food Plan, 598 P.2d at 1041; Lloyd A. Fry Roofing Co. v. State Dept. of Health Air Pollution Variance Board, 553 P.2d 800, 808 (Colo. 1976) (Attorney General need not show irreparable harm to obtain injunctive relief). Courts in other jurisdictions have likewise determined that statutory law enforcement authorities may seek equitable remedies on broader grounds than normally allowed in private causes of action. See F.T.C. v. GEM Merchandising Corp., 87 F.3d 466, 470 (11th Cir. 1996) (F.T.C. entitled to seek disgorgement of profits, because purpose “is not to compensate the victims of fraud, but to deprive the wrongdoer of his ill-gotten gain”); People v. Thomas Shelton Powers, M.D., Inc., 3 Cal. Rptr. 2d 34 (Cal. App. 1992) (district attorney entitled to seek restitution under state unfair business practices statute to deprive developer of unjust profits from sale of homes in violation of city ordinance).

Because the restitution sought by the Attorney General in this case is specifically authorized by statute, and is designed to divest the defendants of the proceeds of their illegal conduct, defendants’ motion to dismiss these remedies must be denied.

CONCLUSION

The bulk of defendants' challenge to the Amended Complaint concerns whether the State, as an injured party, may sue for damages under the various statutory violations pled. Untouched by credible argument is the Attorney General's enforcement authority to bring each of the Claims for Relief in the Amended Complaint. This fact alone is enough to warrant a denial of defendants' motion. To the extent this Court nonetheless finds it necessary to consider the defendants' motion to dismiss, then, for the reasons set forth in this Response, each of those challenges must be denied.

DATED this 20th day of March, 1998.

GALE A. NORTON
Attorney General

MARTHA PHILLIPS ALLBRIGHT
Chief Deputy Attorney General

RICHARD A. WESTFALL
Solicitor General

JAN MICHAEL ZAVISLAN, 11636*
First Assistant Attorney General

MARIA E. BERKENKOTTER, 16781*
Assistant Attorney General

Attorneys for Plaintiff

Tobacco Litigation Unit
1525 Sherman Street, 5th Floor
Denver, Colorado 80203
Telephone: (303) 866-3613
FAX: (303) 866-5691

*Counsel of Record

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