

IN THE DISTRICT COURT OF LANCASTER COUNTY, NEBRASKA

SWISHER INTERNATIONAL, INC.;)
CHEYENNE INTERNATIONAL, LLC; and)
the CIGAR ASSOCIATION OF AMERICA,)
INC.)
Plaintiffs,)

Case No. _____

v.)

COMPLAINT FOR DECLARATORY
AND INJUNCTIVE RELIEF

DOUGLAS J. PETERSON, IN HIS OFFICIAL)
CAPACITY AS NEBRASKA ATTORNEY)
GENERAL; THE NEBRASKA)
DEPARTMENT OF REVENUE; and TONY)
FULTON, IN HIS OFFICIAL CAPACITY AS)
NEBRASKA TAX COMMISSIONER,)
Defendants

INTRODUCTION

1. By improperly applying the term “Cigarette” in Nebraska Revised Statute § 69-2702(4) to cover certain cigars, Defendants seek to arbitrarily treat some manufacturers of those cigars differently than other manufacturers of the same product. In doing so, Defendants are unfairly and arbitrarily tilting the competitive field to favor certain companies. Even worse, Defendants’ supposed justification for doing so is that the arbitrary treatment supposedly results from agreements with the manufacturers that are being given the unfair advantage. Defendants’ improper change also departs from the way that the same statutory language has been interpreted for two decades. The improper change is unprecedented: The language is from a Model statute enacted pursuant to an agreement between certain cigarette manufacturers and forty-six states, including Nebraska, and no state has ever applied the term “Cigarette” as used in that agreement to cover cigars in the way that Defendants have done. In addition, Defendants improperly rushed this change through

by informal so-called guidance rather than following the required rulemaking process. Defendants' change, moreover, results in them improperly construing Nebraska statutes in a way that makes the statutes violate the Nebraska Constitution's ban on special legislation and the Nebraska Constitution's Equal Protection Clause.

Background

2. Over twenty years ago, Nebraska and 45 other states signed a settlement agreement (the "MSA") with certain cigarette manufacturers. The settlement agreement requires the signatory cigarette companies to pay large sums of money annually to the states, including Nebraska, in settlement of the states' claims for health care costs resulting from cigarette smoking. Each signatory cigarette company's annual share of this settlement amount is based on the amount of federal excise taxes it pays on its cigarette sales, and no sales of cigars and "Little Cigars" have any impact on the calculation. The fact that the payments are based on the amount of federal excise tax for cigarettes is crucial, because that cigarette federal excise tax does not apply to cigars.

3. In exchange for these settlement payments, each "Participating Manufacturer" receives a release from "any future Claims for reimbursement of health care costs allegedly associated with the use of or exposure to *Tobacco Products*." Notably, the definition of "Tobacco Products" under the MSA is "Cigarettes and smokeless tobacco products."

4. Neither the Federal Government, nor any of the parties to the MSA (including Nebraska) have ever previously interpreted the definition of "Cigarettes" in the MSA as including "Little Cigars." Therefore, no company has ever previously made any payments under the MSA for the sale of Little Cigars, and the Participating Manufacturers have never

before been released by any state for claims for reimbursement of health care costs related to the sale of Little Cigars.

5. Pursuant to the MSA, Nebraska enacted statutes, commonly known as “Escrow and Directory Statutes,” that expressly incorporate and refer to the Master Settlement Agreement. A key part of those Escrow and Directory Statutes is the definition of “Cigarette” in Nebraska Revised Statute § 69-2702(4). That definition of “Cigarette” is the same as the definition of “Cigarette” in the MSA. Using that definition of “Cigarette,” the Escrow Statutes provide that a cigarette manufacturer that has not signed the MSA (called a “Non-Participating Manufacturer” or “NPM”) must post a bond and make escrow payments based on their cigarette sales.

6. Under the terms of the MSA, the Escrow and Directory Statutes are expressly intended to be uniform. They are referred to as “Model” or “Qualifying” Statutes in the MSA.

7. Until Defendants’ recent change, no State—including Nebraska—has interpreted the term “Cigarette” in Escrow and Directory Statutes to apply to cigars, even with the same statutory definition of “Cigarette” as now applied in Nebraska.

8. The Escrow and Directory Statutes were described as leveling the competitive field by making sure that all manufacturers of cigarettes either pay under the MSA (in the case of Participating Manufacturers) or pay under the Escrow Statutes (in the case of Non-Participating Manufacturers). Importantly, these payments are based on the federal tax classification of a product, which must be determined by the federal government.

9. Defendants’ new unprecedented interpretation that the term “Cigarette” in the Escrow and Directory Statutes applies to certain cigars upends the purpose of those statutes

by radically tilting the competitive field. Until now, Non-Participating Manufacturers that make cigarettes and cigars, and cigar manufacturers that do not make cigarettes, have had no MSA obligations whatsoever relating to cigars. Under the state's new, incorrect application, however, these companies must make escrow payments for sales of certain cigars. But Participating Manufacturers *do not pay anything* under the Escrow and Directory Statutes for sales of the same types of cigars, *nor do they pay anything* under the MSA for the sale of the same types of cigars. That advantage is arbitrary. Defendants have acknowledged the differential treatment.

10. Perhaps unintentionally, moreover, Defendants' new interpretation of "cigarette" might have the effect of releasing the Participating Manufacturers from all claims related to sales of the cigars in question, for nothing in return. This is because the Release given by Nebraska in the MSA applies to "Cigarettes," as defined in the MSA and employed in Nebraska Revised Statute § 69-2702(4). If Nebraska applies that definition of "Cigarette" to the cigars in question, that interpretation might result in Nebraska expanding the scope of the Release in the MSA to cover those sales of the cigars in question by Participating Manufacturers.

11. Defendants' errors are compounded by the fact that they resulted in incomplete and potentially misleading testimony before the Nebraska Unicameral in connection with consideration of a recent bill (LB 397) that became law in 2019. That testimony is discussed further below.

12. Plaintiffs thus bring three claims summarized here and stated more fully below.

- a. *First*, the so-called guidance is invalid under Nebraska Revised Statute § 84-911 because it is a rule or regulation under Nebraska Revised Statute § 84-901(2), but

Defendants failed to follow the required rulemaking process, and it violates Plaintiffs' constitutional rights. Defendants should be temporarily and permanently enjoined from using the so-called guidance.

- b. *Second*, Defendants' recent decision to depart from how the term "Cigarette" in Nebraska Revised Statute § 69-2702(4) has been interpreted for over two decades in order to stretch it to apply to the cigars in question causes the Nebraska Escrow and Directory Statutes, Nebraska Revised Statutes §§ 69-2701 to 69-2711, to violate the Nebraska Constitution's ban on special legislation because it creates arbitrary distinctions between the treatment of manufacturers of the same products. Defendants should be temporarily and permanently enjoined from reclassifying the cigars in question as cigarettes for purposes of those statutes.
- c. *Third*, Defendants' recent decision to depart from how the term "Cigarette" in Nebraska Revised Statute § 69-2702(4) has been interpreted for over two decades in order to stretch it to apply to the cigars in question causes the Nebraska Escrow and Directory Statutes, Nebraska Revised Statutes §§ 69-2701 to 69-2711, to violate the Nebraska Constitution's Equal Protection Clause because it creates distinctions between manufacturers of the same products that lack any rational basis. Defendants should be temporarily and permanently enjoined from reclassifying the cigars in question as cigarettes for purposes of those statutes.

PARTIES

13. Plaintiff Swisher International, Inc. (“Swisher”) is a Delaware corporation with its principal place of business located in Jacksonville, Florida. Swisher manufactures cigars that have been sold in Nebraska and which Defendants purport to regulate and potentially confiscate pursuant to a Notice issued by the Department of Revenue on August 22nd (the “August 22nd Notice”) as more fully explained below.

14. Plaintiff Cheyenne International, LLC (“Cheyenne”) is a North Carolina limited liability company with its principal place of business in Grover, North Carolina. Cheyenne manufactures cigars that have been sold in Nebraska and that Defendants purport to regulate and potentially confiscate pursuant to the August 22nd Notice.

15. Plaintiff Cigar Association of America, Inc. (“CAA”) is a trade association and is a New York not-for-profit corporation with a principal place of business in Washington, D.C. CAA represents the interests of the plaintiffs and other cigar manufacturers who are affected by the August 22nd Notice.

16. Plaintiffs have not assigned the rights at issue in this lawsuit.

17. Defendant Tony Fulton is the Tax Commissioner of the State of Nebraska acting in his official capacity.

18. Defendant Nebraska Department of Revenue is an administrative agency of the State of Nebraska.

19. Defendant Douglas J. Peterson is the Attorney General of the State of Nebraska acting in his official capacity.

JURISDICTION, DECLARATORY RELIEF, AND VENUE

20. The Court has subject matter jurisdiction pursuant to Neb. Rev. Stat. §§ 24-302, 25-21,149, and 84-911. Declaratory relief is available pursuant to Neb. Rev. Stat. §§ 25-21,149, 25-21,159, and 84-911. Injunctive relief, including temporary injunctive relief, is available pursuant to Nebraska Revised Statute §§ 25-1062 to 25-1080.

21. Venue is proper in this judicial district pursuant to Neb. Rev. Stat. §§ 25-403.01, 25-21,206, and 84-911.

FACTS

22. In 1998, Nebraska and forty-five other states entered into the MSA with certain cigarette manufacturers. The terms of the MSA included provisions for states to enact “Qualifying” and “Model” Statutes.

23. Nebraska enacted statutes that referred to and incorporated terms from the MSA. These statutes, codified at Neb. Rev. Stat. § 67-2901 *et seq.*, specifically express the legislative intent that the statutes be considered “Model” and “Qualifying” statutes “as those terms are defined” in the MSA. Neb. Rev. Stat. § 69-2711.

24. The MSA and the Qualifying and Model Statutes apply to “Cigarettes.”

25. For more than two decades, all forty-six states that are parties to the MSA have maintained the consistent, and uniform, position that the MSA and the Model and Qualifying Statutes do not apply to any cigar products, as determined by the federal government.

26. Forty-five of the States that were parties to the MSA, and have enacted the Qualifying and Model statutes, continue to maintain that straightforward position that cigarettes and cigars are different. The MSA applies to cigarettes, not cigars.

27. That distinction between cigars and cigarettes is central to the MSA and the Model or Qualifying Statutes such as those enacted by Nebraska. A core concept of the MSA and those statutes is a manufacturer's "Market Share," defined according to the federal excise tax payments by a cigarette manufacturer. As is explained further below, the federal excise tax for cigarettes does not apply to cigars, and therefore a manufacturer's "Market Share" is completely unaffected by the sale of cigars.

28. Effective September 1, 2019, Nebraska has become the only State to adopt the incorrect position that certain cigars should be treated as cigarettes for purposes of the Model and Qualifying Statutes.

29. As explained further below, Nebraska's outlier position is incorrect. That position, moreover, is based on a patently inaccurate interpretation of the MSA, of federal excise tax law, and of the Model and Qualifying Statutes.

30. Nebraska's incorrect outlier position was adopted without following the proper administrative procedures, and it is unconstitutional.

31. Defendants have acted improperly by issuing standards of general applicability that affect public rights, affect public interests, and are intended to bind the public and impose penalties through so-called guidance documents issued on short notice rather than by the required statutory rule making process.

A. There has been a long-standing distinction between cigars and cigarettes.

32. For purposes of the federal excise tax, the Federal Government has long recognized a basic distinction between cigars and cigarettes based on various factors, including the fact that cigars are wrapped in tobacco while cigarettes are wrapped in paper. Under federal

law for purposes of the federal excise tax, a cigar “means any roll of tobacco wrapped in leaf tobacco or in any substance containing tobacco....” 26 U.S.C. § 5702(a).

33. Plaintiffs’ cigars, including the types of cigars in question here, have never been subject to the federal excise tax for cigarettes. That cigarette federal excise tax is separate from the cigar federal excise tax, and it is contained at 26 U.S.C. § 5702(b). Under federal law, a roll of tobacco wrapped in paper is a cigarette, not a cigar.

B. The Master Settlement Agreement

34. The MSA resolved lawsuits that the states had brought against the cigarette manufacturers for healthcare costs incurred by the states from the effects of cigarette smoking.

35. Two crucial definitions in the MSA incorporated and relied upon the federal excise tax for cigarettes. One of those crucial definitions was of the term “Market Share” and one was of the term “Cigarette.”

36. The MSA defined “Market Share,” in pertinent part as “a Tobacco Product Manufacturer’s respective share (expressed as a percentage) of the total number of individual **Cigarettes** sold in the fifty United States, the District of Columbia and Puerto Rico during the applicable calendar year *as measured by excise taxes collected by the federal government*” (MSA ¶ II(z) at 8) (emphasis added).

37. The MSA defined cigarette as follows:

“Cigarette” means any product that contains nicotine, is intended to be burned or heated under ordinary conditions of use, and consists of or contains *(1) any roll of tobacco wrapped in paper or in any substance not containing tobacco*; or (2) tobacco, in any form, that is functional in the product, which, because of its appearance, the type of tobacco used in the filler, or its packaging and labeling, is likely to be offered to, or purchased by, consumers as a cigarette; or (3) *any roll of tobacco wrapped in any substance containing tobacco which, because of its appearance, the type of tobacco used in the filler, or its packaging and labeling, it likely to be offered to, or purchased by, consumers as a cigarette* described in clause (1) of this definition. The term “Cigarette” includes “roll-your-own” (i.e.,

any tobacco which, because of its appearance, type, packaging, or labeling is suitable for use and likely to be offered to, or purchased by, consumers as tobacco for making cigarettes). Except as provided in subsections II(z) and II(mm), 0.0325 ounces of “roll-your-own tobacco shall constitute one individual “Cigarette.”

(MSA ¶ II(m) at 6-7) (emphasis added). The highlighted parts of that statute are identical to the definition of cigarette for the federal excise tax in 26 U.S.C. § 5702(b).

38. The distinction in federal excise taxes between cigars and cigarettes is central to the MSA and the Model or Qualifying Statutes, such as those enacted by Nebraska, as exemplified by the MSA’s explicit incorporation of federal excise taxes on cigarettes.

C. The Nebraska Escrow and Directory Statutes

39. Nebraska enacted statutes that refer to and incorporate terms from the MSA. These statutes, codified at Neb. Rev. Stat. § 67-2701 *et seq.*, specifically express the legislative intent that the statutes be considered “Model” and “Qualifying” statutes “as those terms are defined in the Master Settlement Agreement.” Neb. Rev. Stat. § 69-2711.

40. Neb. Rev. Stat. § 69-2703 requires any tobacco product manufacturer selling cigarettes in Nebraska to either become a party to the MSA (any such manufacturer is known as a “Participating Manufacturer”) or register with the State as a “Non-Participating Manufacturer.” Non-Participating Manufacturers are required to place funds into an escrow account based on cigarettes sold within Nebraska. The statute contains no such requirement on manufacturers that sell cigars in Nebraska.

41. The MSA’s concept of Market Share based upon the federal excise tax distinction between cigars and cigarettes is incorporated by reference into Nebraska’s statute governing an NPM’s obligation to make escrow payments. Neb. Rev. Stat. § 69-2703(2)(b)(ii).

42. Neb. Rev. Stat. § 69-2706 requires cigarette manufacturers to certify compliance with the Escrow and Directory Statutes located at Neb. Rev. Stat. § 69-2701 *et seq.*

43. The Tax Commissioner is charged with developing, maintaining, and publishing a directory of certifying cigarette manufacturers and all brand families that are listed in such certifications (“Directory”). Neb. Rev. Stat. § 69-2706(2).

44. Neb. Rev. Stat. § 69-2706(4) makes it unlawful for any person to affix a Nebraska stamp to any package or container of cigarettes of a manufacturer or brand family not listed in the Directory.

45. Neb. Rev. Stat. § 69-2707.01 requires that any Non-Participating Manufacturer subject to the certification requirements of § 69-2706 regarding cigarettes post a bond, or its cash equivalent, of at least one hundred thousand dollars.

46. Non-Participating Manufacturers are required to make quarterly payments into escrow accounts based on the number of cigarettes sold in the previous calendar quarter. This escrow program is intended to charge Non-Participating Manufacturers a per-carton amount that is equivalent to the per-carton amount that Participating Manufacturers pay under the MSA for their cigarette sales, so that Non-Participating Manufacturers do not have a price advantage over any Participating Manufacturer for cigarette sales. There are penalties for a Non-Participating Manufacturer’s noncompliance. Neb. Rev. Stat. § 69-2703.

47. Plaintiffs, as manufacturers of cigars, before September 1, 2019, have never been subject to chapter Neb. Rev. Stat. §69-2701 *et. seq.* with respect to their sale of cigars. Nor have Plaintiffs’ cigar products been subject to similar Qualifying Statutes in other Settling States for their sales of cigars.

D. LB 397

48. On May 30, 2019, the Governor signed Legislative Bill 397 (“LB 397”) which made amendments to various statutes relating to cigarettes and tobacco products.

49. LB 397 amended the definition of “Cigarette” for purposes of the State excise tax.

50. Prior to the enactment of LB 397, the definition of “cigarette” for purposes of the state excise tax was “any roll for smoking made wholly or in part of tobacco irrespective of size or shape and whether or not such tobacco is flavored, adulterated, or mixed with any other ingredient, the wrapper or cover of which is made of paper or any other material excepting tobacco.” Neb. Rev. Stat. § 77-2601.

51. LB 397 amended the definition of “cigarette” for purposes of the state excise tax in Neb. Rev. Stat. § 77-2601 to conform it to the definition set forth in the MSA and as adopted by other states subject to the MSA as follows:

any product that contains nicotine, is intended to be burned or heated under ordinary conditions of use, and consists of or contains (a) any roll of tobacco wrapped in paper or in any substance not containing tobacco; or (b) tobacco, in any form, that is functional in the product, which because of its appearance, the type of tobacco used in the filler, or its packaging and labeling, is likely to be offered to, or purchased by, consumers as a cigarette; or (c) any roll of tobacco wrapped in any substance containing tobacco which, because of its appearance, the type of tobacco used in the filler, or its packaging and labeling is likely to be offered to, or purchased by consumers as a cigarette described in clause (5)(a) of this definition.

LB 397 adopted the same definition of “Cigarette” as the MSA. (MSA ¶ II(m)).

52. LB 397 *did not* amend, change, or affect the definition of “Cigarette” in Nebraska Revised Statute § 69-2702(4), which is used in the Escrow and Directory statutes.

53. While the Nebraska Legislature has the power to change the rate at which cigars are taxed, Defendants have improperly changed the tax rate of certain cigars by so-called guidance that did not follow the rulemaking process, and they have improperly changed the interpretation of “Cigarette” for purposes of the Escrow and Directory Statutes.

54. While some other states (New Hampshire, Iowa, Montana, and Massachusetts) tax certain cigars at the same rate as cigarettes for purposes of state excise tax, none has attempted to reclassify certain little cigars to be cigarettes for the purposes of the Escrow and Directory statutes as Defendants have done here.

E. The requirement that these types of changes be done by rule or regulation.

55. In 2017, the Nebraska Legislature amended the definition of “rule or regulation” in the Administrative Procedure Act to prevent administrative agencies from issuing the types of legally binding standards at issue here through guidance documents. After that amendment, any standard affecting private rights, private interests, or procedures available to the public is considered a “rule or regulation” as defined in Nebraska Revised Statute § 84-901. Defendants have engaged in precisely the type of conduct that the Legislature prohibited by that amendment by issuing public standards that are meant to bind the public with the force of law in the form of guidance documents, rather than through the required statutory rulemaking process.

56. That 2017 amendment to the definition of “rule or regulation” was through LB 209. The bill’s sponsor, Senator Watermeier, testified on the floor of the Unicameral that: “The language clarifies that standards affecting private rights, private interest, or procedures available to the public are regulations underneath the Administrative Procedure Act, not guidance documents. Returning this language to the act... will ensure that agencies are aware that any such standards would need to follow the formal promulgation process.” Nebraska Legislature Floor Debate, April 20, 2017 at 65.

57. In testimony in favor of LB 209 before the Government, Military and Veterans Affairs Committee, a representative of Nebraska Appleseed noted that: “[T]his language ensures that government agencies will remain accountable to the public when internal management rules

are issued that also impact private citizens' interests or rights. Essentially this change is important because it effectively closes a loophole that agencies could have utilized to avoid the application of the APA.” Transcript of Government, Military and Veterans Affairs Committee, January 27, 2017 at 7.

F. The new interpretations here were called guidance but actually are rules and regulations that failed to go through the rulemaking process.

58. The Department of Revenue first issued a Notice on August 1, 2019 (the “August 1 Notice”), stating that “certain little cigars, certain filtered and non-filtered little cigars, and certain flavored little cigars may be reclassified as cigarettes effective September 1, 2019. The size of a product does not control the determination of whether it is reclassified as a cigarette. Rather, the manner in which it is marketed and/or consumed determines whether the tobacco product is considered a cigarette under the new definition.” This Notice provided no other indication as to which products this “reclassification” would apply.

59. Plaintiffs and other industry members engaged in dialogues with Nebraska officials regarding the guidance.

60. On August 22, 2019, the Department of Revenue issued the August 22nd Notice stating that certain little cigar products can only be legally sold in Nebraska “if they are: (1) Listed in the Nebraska Directory of Certified Tobacco Product Manufacturers and Brands (Directory); (2) Stamped with a Nebraska cigarette tax stamp; and (3) Designated as Fire Standard Compliant.”

61. That August 22nd notice also stated that “certain little cigars, certain filtered and non-filtered little cigars, and certain flavored little cigars may be reclassified as cigarettes effective September 1, 2019.” The Notice created criteria, discussed below, that would be used to determine which cigars would be treated as cigarettes.

62. The August 22nd Notice contained a specific directive aimed at the conduct of retailers stating that:

Retailers are reminded that beginning September 1, 2019, little cigars/cigarettes and any other products meeting the new cigarette definition on your retail point of sale displays must meet the requirements noted above. If the cigarettes do not meet the requirements, the cigarettes are contraband and will be confiscated during a retail compliance inspection under Neb. Rev. Stat. § 77-2620.

63. The August 22nd Notice also threatened retailers and stamping agents. It stated: “Retailers and stamping agents who do not comply with LB 397 could be subject to civil and/or criminal penalties, and their license may be suspended or revoked.”

64. The August 22nd Notice also cautioned manufacturers, such as Plaintiffs, that: “Manufacturers of products for sale in Nebraska that meet the new cigarette definition must have the products listed on the Directory and ensure their products are FSC compliant, if they intend to continue to utilize the Nebraska market on and after September 1, 2019.”

65. On the same day, the Department of Revenue issued a document entitled “Criteria for Tobacco Products Labeled as Anything Other Than a Cigarette” (“Criteria”). This document states that:

[A] tobacco product labeled as anything other than a cigarette or not bearing a label, including but not limited to certain little cigars, certain filtered little cigars, and certain flavored little cigars will be reclassified as a cigarette if the product meets two or more of the following criteria: (1) a pack contains 20 or 25 sticks; (2) a carton contains eight or ten packs; (3) the stick length is 2 ¾ inches to 5 inches stick and diameter is equal to or less than 8.20 millimeters; (4) the product is sold in soft packs, hard packs, flip-top boxes, or clamshell packages; or (5) the product is sold with a cigarette-type filter.

None of those five criteria are contained in any Nebraska statute. Nor are they used in any other state.

66. Additionally, the Department of Revenue issued a document entitled “Examples,” showing pictures of certain cigars it now considers cigarettes (“Example Document”).

67. The effect of the August 22nd Notice, Criteria, and Example Document is to improperly force cigar manufacturers to comply with the Escrow and Directory Statutes for the ostensible purpose of protecting Market Share Adjustments that, by the terms of the MSA, cannot take account of cigar sales because they are not taxed as cigarettes under the federal excise tax statutes.

68. The effect of the August 22nd Notice, Criteria, and Example Document is to promulgate a new administrative “rule or regulation,” within the meaning of Neb. Rev. Stat. § 84-901(2), changing over nineteen years of practice that have been consistent with the framework of the MSA.

69. But the new “rule or regulation” set forth in the August 22nd Notice, Criteria, and Example Document is not the result of following proper rule-making, and it ignores the fact that the definition of “Cigarette” for purposes of Nebraska’s Escrow and Directory statutes has been unchanged for twenty years.

70. Nor are the August 22nd Notice, Criteria, and Example Document the result of a proper and required administrative rulemaking process that would provide affected parties with notice and opportunity to be heard. Indeed, the August 22nd Notice, Criteria, and Example Document provided little notice to the parties it affects, having been issued a mere **ten (10)** days before the changes it proposed would take effect.

71. On September 10th, the Nebraska Department of Revenue posted a notice on its website listing the brand families of cigars that are being reclassified as cigarettes, including for

purposes of the Escrow and Directory Statutes. That notice lists brands sold by Plaintiffs Swisher and Cheyenne.

F. Incomplete and potentially misleading testimony before the Unicameral.

72. There was incomplete and potentially misleading testimony before the Unicameral regarding LB 397 in 2019. The testimony suggested that the Bill was intended to prevent Participating Manufacturers from reducing their MSA payments through adjustments pursuant to the MSA and a later agreement called the NPM Adjustment Settlement Agreement. That testimony referred to potential disputes under those Agreements regarding with whether the State had diligently enforced obligations. Specifically, the obligations require states, including Nebraska, to “diligently enforce” provisions preventing manufacturers of *cigarettes* subject to the federal excise tax for cigarettes from gaining an unfair commercial advantage by either not signing the MSA or complying with the state escrow statues. That testimony was incomplete and potentially misleading, because the MSA adjustments in question do not relate to cigar sales. They relate to sales of products subject to the federal excise tax for cigarettes, which does not apply to cigars. To the extent the testimony related to the NPM Adjustment Settlement Agreement, moreover, the testimony was incomplete and potentially misleading in suggesting that a change was needed to fix an existing problem. In fact, the status quo did not create a problem. It was not until Defendants took the actions in question by issuing so-called guidance that there was a problem. Nowhere in the testimony did a witness mention the result that Defendants now have acknowledged— Defendants are treating different manufacturers of the same product differently, with Participating Manufacturers able to sell the same product without making any payments under either the MSA or the Escrow and Directory Statutes.

F. Plaintiffs will suffer irreparable harm absent an injunction.

73. Plaintiffs will suffer irreparable harm absent an injunction. Plaintiffs are subject to a competitive disadvantage that will cause them to lose market share and lose customer goodwill. Plaintiffs are required to make payments pursuant to the Escrow and Directory Statutes while other manufacturers of the same product do not have to make any corresponding payments—not pursuant to the Escrow and Directory Statutes, and not pursuant to the MSA.

CLAIMS FOR RELIEF

Count I

Declaratory Judgment and Injunctive Relief Based On The Fact That the August 22nd Notice, Criteria, and Example Document Are Invalid Rules and Regulations.

74. Plaintiffs incorporate by reference all previous paragraphs in this Complaint as if fully set forth herein.

75. Plaintiffs bring this Claim against all Defendants.

76. The so-called guidance issued by Defendants actually is a rule or regulation under the criteria in Nebraska Revised Statute § 84-901(2). The August 22nd Notice, Criteria, and Example Document are standards of general application that affect private rights, affect private interests, and were issued to be relied upon to bind the public including retailers, wholesalers, distributors, licensed stamping agents, and Plaintiffs, as manufacturers of cigars. They also impose penalties. Specifically:

- a. The August 22nd Notice sought to bind the public with the force of law by stating that certain little cigar products can only be legally sold in Nebraska “if they are:
(1) Listed in the Nebraska Directory of Certified Tobacco Product Manufacturers and Brands (Directory); (2) Stamped with a Nebraska cigarette tax stamp; and (3) Designated as Fire Standard Compliant.”

- b. The August 22nd Notice threatened retailers that “If the cigarettes do not meet the requirements, the cigarettes are contraband and will be confiscated during a retail compliance inspection under Neb. Rev. Stat. § 77-2620.”
- c. The August 22nd Notice threatened retailers and stamping agents with civil and/or criminal penalties for non-compliance with the August 22nd Notice, Criteria, and Example Document.
- d. The August 22nd Notice also was directed at Plaintiffs: “Manufacturers of products for sale in Nebraska that meet the new cigarette definition must have the products listed on the Directory and ensure their products are FSC compliant, if they intend to continue to utilize the Nebraska market on and after September 1, 2019.”
- e. The Department of Revenue also published the Criteria which unabashedly went beyond the language of LB 397 by stating that:

[A] tobacco product labeled as anything other than a cigarette or not bearing a label, including but not limited to certain little cigars, certain filtered little cigars, and certain flavored little cigars will be reclassified as a cigarette if the product meets two or more of the following criteria: (1) a pack contains 20 or 25 sticks; (2) a carton contains eight or ten packs; (3) the stick length is 2 ¾ inches to 5 inches and stick diameter is equal to or less than 8.20 millimeters; (4) the product is sold in soft packs, hard packs, flip-top boxes, or clamshell packages; or (5) the product is sold with a cigarette-type filter.
- f. The Example Document also contained pictures of certain cigars that the Department of Revenue now considered to be cigarettes.
- g. The application of the August 22nd Notice, Criteria, and Example Document interferes with, impairs, and threatens to interfere with and impair Plaintiffs legal rights and privileges.

77. Nebraska Revised Statute § 84-911(2) states that: “The court shall declare the rule or regulation invalid if it finds that it violates constitutional provisions... or was adopted without compliance with the statutory procedures.” (emphasis added).

78. The August 22nd Notice, Criteria, and Example Document were adopted and issued to the public without compliance with the statutory procedures containing the requirements for rulemaking, and they violate constitutional provisions. They thus are invalid under Nebraska Revised Statute § 84-911(2).

79. Defendants are authorized to issue regulations. Nebraska Revised Statute § 69-2703 provides that: “The Tax Commissioner may adopt and promulgate rules and regulations necessary to effect the purposes of Sections 69-2703 to 69-2711.”

80. Consistent with that statute, any action by the Tax Commissioner and/or the Nebraska Department of Revenue to treat cigars as cigarettes must be pursuant to rules and regulations.

81. A declaration that the guidance is an invalid rule and regulation and temporary and permanent injunctive relief enjoining the enforcement of the August 22nd Notice, Criteria, and Example Document and enjoining related actions by Defendants are necessary to prevent irreparable injury to Plaintiffs.

82. It is futile for Plaintiffs to attempt any further administrative relief. Defendants’ position is clear and unchanging.

Count II
Declaratory Judgment and Injunctive Relief
Against Unconstitutional Special Legislation
In Violation of Article III, § 18 of the Nebraska Constitution

83. Plaintiffs incorporate all previous paragraphs of this Complaint.

84. Plaintiffs bring this claim against the individual Defendants in their official capacities.

85. Article III, § 18 of the Nebraska Constitution prohibits special legislation.

86. That prohibition on special legislation precludes arbitrary and unreasonable methods of classification.

87. Defendants' actions changing the way that the term "Cigarette" is interpreted for purposes of Nebraska Revised Statute § 69-2702(4) by stretching the term to cover certain cigars causes the Escrow and Directory Statutes, Nebraska Revised Statute §§ 69-2701 to 69-2711, to violate the ban on special legislation. That change in interpretation causes those statutes to operate in an arbitrary manner. Cigarette companies that are already Participating Manufacturers under the MSA can sell "little cigar" products without any obligation to pay Nebraska anything under the MSA or under the Escrow and Directory Statutes. According to the Nebraska Attorney General's office, these cigarette companies would merely need to certify that their little cigar products constitute "cigarettes" without making any additional payments under the MSA. However, if a company is a Non-Participating Manufacturer also manufacturing cigars, or a company that has never manufactured cigarettes, they will be required to pay \$7.16 into an escrow account for each carton of cigars sold in Nebraska. This creates a situation where cigar manufacturers – which are not party to the MSA – are being arbitrarily disadvantaged in favor of those companies that are signatories to the MSA.

88. Plaintiffs will be irreparably harmed unless Defendants are temporarily and permanently enjoined from continuing their departure from how the term "Cigarette" in Nebraska Revised Statute § 69-2702(4) has been interpreted for two decades, and declaratory relief also is proper.

Count III
Declaratory And Injunctive Relief
Against Violation of Equal Protection Clause,
Article I, § 3, Nebraska Constitution

89. Plaintiffs incorporate all previous paragraphs of this Complaint.

90. Plaintiffs bring this claim against the individual Defendants in their official capacities.

91. Article I, § 3 of the Nebraska Constitution imposes equal protection obligations on the State of Nebraska.

92. Defendants' actions have violated those equal protection obligations.

93. With no rational basis, Defendants have treated some manufacturers of certain cigars differently than other manufacturers of the same product.

94. Companies that are already Participating Manufacturers to the MSA (i.e., cigarette manufacturers) can release new "little cigar" products without needing to place additional money into escrow under Nebraska's laws. According to the Nebraska Attorney General's office, Participating Manufacturers would merely need to certify that the little cigar product constitutes a cigarette without making any additional MSA payments. However, if a company is a Non-Participating Manufacturer or a company that has never manufactured cigarettes, they will be required to acquire the cigarette tax stamp and pay into an escrow account a charge of \$7.16 per carton. This creates a situation where cigar manufacturers – not previously bound to the MSA – are being discriminated against in favor of those companies that are signatories to the MSA because they manufacture cigarettes. There is no rational basis for that different treatment of manufacturers of the same product, which violates equal protection as guaranteed in the Nebraska Constitution.

95. Plaintiffs will be irreparably harmed absent injunctive relief, and the other requirements for an injunction are satisfied. Plaintiffs are entitled to injunctive and declaratory relief.

Prayer for Relief

Wherefore, Plaintiffs request declaratory judgments and temporary and permanent injunctive relief as requested in this Complaint.

Respectfully submitted this 24th day of September, 2019.

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